



U.S. Department of the Interior  
Office of Inspector General

## AUDIT REPORT

**INDEPENDENT AUDITORS' REPORT  
ON THE OFFICE OF SPECIAL TRUSTEE  
FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS AND  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
FINANCIAL STATEMENTS FOR  
FISCAL YEARS 2001 AND 2000  
MANAGED BY THE  
OFFICE OF TRUST FUNDS MANAGEMENT**

**REPORT NO. 2002-I-0027  
APRIL 2002**

**1232a-TO Internal Audit Case File**

Documents accumulated in the review & examination of BIA/OST operations by BIA or DOI auditors, to ensure accuracy, propriety, legality, & reliability of the use of assets. Include correspondence, draft & final reports, responses/comments, recommendations, corrective actions, & related working papers.

Destroy when no longer needed for reference.

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**FIELITZ**



# United States Department of the Interior

Office of Inspector General  
Washington, D.C. 20240

April 25, 2002

## Memorandum

To: Special Trustee for American Indians, Office of the Special Trustee

From: Roger La Rouché  
Assistant Inspector General for Audits

Subject: Independent Auditors' Reports on the Office of the Special Trustee for American Indians Tribal and Other Trust Funds and Individual Indian Monies Trust Funds Financial Statements for Fiscal Years 2001 and 2000 Managed by the Office of Trust Funds Management (No. 2002-I-0027)

The Office of the Special Trustee for American Indians (OST) contracted with KPMG LLP, an independent certified public accounting firm, to audit the OST's financial statements for fiscal year 2001. The OST's financial report contains separate financial statements and related notes for Tribal and Other Trust Funds and Individual Indian Monies Trust Funds. The contract required that KPMG perform the audit in accordance with auditing standards generally accepted in the United States of America.

In connection with the contract, we monitored the progress of the audit at key points and reviewed KPMG's reports and related working papers and inquired of their representatives. Our review, as differentiated from an audit in accordance with generally accepted government auditing standards, was not intended to enable us to express, and we do not express, opinions on the OST's financial statements or on conclusions about the effectiveness of internal controls or on conclusions about compliance with laws and regulations. KPMG is responsible for the auditors' reports on the fiscal year 2001 financial statements (see Attachment) and for the conclusions expressed in the reports. However, our review disclosed no instances where KPMG did not comply in all material respects with generally accepted auditing standards.

In its audit reports dated January 4, 2002, KPMG issued qualified opinions on the OST's financial statements for fiscal year 2001 because cash balances reflected in the accompanying financial statements were materially greater than balances reported by the U.S. Treasury, inadequacies in certain Department of the Interior accounting systems made it impracticable to extend auditing procedures to satisfy auditors as to the fairness of trust fund balances, and certain parties for whom the Office of Trust Funds Management (OTFM) holds monetary assets in trust do not agree with balances recorded by the OTFM; and certain of these parties have filed or are expected to file claims against the U.S. Government. The fiscal year 2000 financial statements were audited by other auditors

whose report, dated December 15, 2000, was qualified because cash balances were materially greater than those reported by the U.S. Treasury, major deficiencies in the accounting systems' controls and records caused the systems to be unreliable, and certain Trust Fund beneficiaries disagreed with balances recorded by the OTFM and had filed or were expected to file claims against the OTFM.

KPMG found two reportable material weaknesses and one reportable condition related to reliance on processing of trust transactions at the Bureau of Indian Affairs, financial reporting regarding unresolved matters from prior periods, and internal controls over information technology systems. With regard to compliance with laws and regulations, KPMG found no instances of noncompliance that are required to be reported.

The OST concurred with all three recommendations. We consider the recommendations resolved but not implemented and, accordingly, the recommendations will be referred to the Assistant Secretary for Policy, Management and Budget for tracking of implementation.

Section 5(a) of the *Inspector General Act* (5 U.S.C. app. 3) requires the Office of Inspector General to list this report in its semiannual report to the United States Congress.

This report is intended for the information of management of the OST, the Office of Management and Budget, and the U.S. Congress. However, this report is a matter of public record, and its distribution is not limited.

Attachment



**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS AND  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**



**FINANCIAL STATEMENTS AND AUDIT REPORTS  
SEPTEMBER 30, 2001**

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS AND  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

**Table of Contents**

	<b>Tab</b>
Letter from the Director	1
Management's Overview of Indian Trust Funds	2
Tribal and Other Trust Funds Financial Statements	3
Individual Indian Monies Trust Funds Financial Statements	4
Auditors' report on Internal Control over Financial Reporting and Compliance with Laws and Regulations	5



## United States Department of the Interior

### OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS

Office of Trust Funds Management  
305 Marquette N.W. Suite 1000  
Albuquerque, New Mexico 87102

#### LETTER FROM THE DIRECTOR

##### HISTORY OF THE OFFICE OF TRUST FUNDS MANAGEMENT (OTFM)

The OTFM was first established within the Bureau of Indian Affairs (BIA) in 1989, pursuant to Secretarial Order Number 3187 dated October 26, 1989. This order combined the trust funds accounting and investment functions within the BIA into one office, OTFM.

In October 1994, the U.S. Congress passed the American Indian Trust Fund Management Reform Act (Public Law 103-412). This statute established within the Department of the Interior (the Department) the Office of the Special Trustee for American Indians (OST). The OST is headed by the Special Trustee who reports directly to the Secretary of the Department of the Interior (the Secretary), is appointed by the President of the United States of America, and is responsible for the oversight of the Department's reform and coordination efforts of all Departmental activities involved in the management of Indian trust assets.

In February 1996, OTFM was transferred intact out of the BIA and placed within the OST. Certain financial trust service employees in region and field offices located throughout the U.S. were also transferred from BIA and made part of OTFM and OST. Today, the Director of OTFM reports to the Special Trustee.

OTFM is responsible for the receipt, investment and disbursement of Indian trust funds to tribal account holders and individual beneficiaries. The balances that have accumulated in trust have resulted generally from judgment awards, settlements of claims, land use agreements, royalties on natural resource depletion, other proceeds derived directly from trust resources and investment income. As presented in the fiscal year 2001 financial statements, American Indian trust fund accounts total approximately \$3.2 billion. Of this amount, about \$400 million is owned by approximately 247,000 individuals, with most of the remainder owned by over 300 tribes.

##### POINTS OF SPECIAL INTEREST FOR FISCAL YEAR 2001

Fiscal year 2001 has been another busy year for the OTFM. The following items are some of the special points of interest that have occurred during fiscal year 2001.

##### ❖ TRUST FUNDS ACCOUNTING SYSTEM

Fiscal year 2001 was the first full year during which all tribal and individual trust fund accounts were operationally accounted for on the new Trust Funds Accounting System (TFAS). Through the use of certain TFAS cash management features and the establishment of a lockbox for returned checks, OTFM has enhanced overall cash management for trust funds. In addition, TFAS provides for the notification of upcoming investment maturities and related interest payments. TFAS also facilitates the printing of statements of performance for each tribal and individual trust fund account, on a quarterly basis.

❖ CHANGES IN LEADERSHIP

In fiscal year 2001 the Nation elected George W. Bush, Jr. President of the United States of America. Upon taking office, President Bush nominated Gale A. Norton to be Secretary of the Interior. Ms. Norton was sworn in as the 48<sup>th</sup> Secretary of the Interior on January 31, 2001 after being confirmed by the U.S. Senate Energy and Natural Resources Committee.

OTFM also experienced changes in leadership. On July 13, 2001 it was announced that Donna Erwin, Director of OTFM since it became part of OST, was promoted to Deputy Special Trustee, Trust Systems and Projects in the OST and responsible for a wide range of Departmental trust reform efforts. Simultaneously, Douglas Lords, Deputy Director to Ms. Erwin since 1994, was named to the OTFM Director's position. Prior to OTFM, Mr. Lords was with the BIA, Western Region Office, and prior to BIA, Mr. Lords was in public accounting.

❖ TRUST REFORM TRAINING

Beginning in January 2001 and in accordance with the Department's High Level Implementation Plan, the Department initiated its Indian trust reform training program. The objective of the training initiative is to support the systems implementation and specialized skills training for the overall trust reform effort in order to increase the job performance and inter-organizational effectiveness of Departmental and tribal personnel who manage Indian trust assets on behalf of the Secretary.

Two courses have been developed and are offered at several locations nationwide. The goal of the two courses - *Trust Foundations I* and *Trust Foundations II*, is, through theory and practice, to provide an overview of how a trust process can work. Students will understand the process of Change Management and the Role of Management as well as become familiar with the concepts of Fiduciary Conduct, the Privacy Act, the Freedom of Information Act and Risk Management. Participation in the training program is expected of all employees in the Department who engage in any manner in the discharge of the Federal government's fiduciary obligations to the Indian beneficiaries for the assets held in trust. This introductory non-technical training also is offered to any person engaged in the trust asset management process at the tribal level.

❖ REVISED REGULATIONS AFFECTING TRUST FUNDS

Effective March 23, 2001 revisions were made to pertinent regulations dealing with funds held in trust - standardizing the process for collecting, distributing, and accounting for individual Indian monies and monies held in trust for tribal governments. The revised and updated regulations can be found in Title 25 of the Code of Federal Regulations (CFR), Part 115 (Trust Funds for Tribes and Individual Indians).

❖ OUTREACH TO ACCOUNT HOLDERS

In 2001, OTFM's outreach efforts continued to make OTFM services more visible. Our field staff increasingly attended and assisted in conducting regional-level Allottee Outreach Meetings. These meetings are attended by many individual Indian account holders and include personnel from Minerals Management Service and the BIA. The meetings provide a forum that allows interested parties to ask questions and obtain information regarding Indian trust funds. Closer to "home", field staff attended local community and tribal council meetings, providing information and addressing trust fund issues and assisting to clarify related concerns. These contacts with beneficiaries are a valuable source of information for the trustee.

More recently, OTFM contributed to the development of an Indian minerals management brochure titled, "Quick Reference – Trust Management of Your Mineral Resources". The brochure explains in plain English terms the minerals management process for oil and gas and other hard minerals for Indian mineral owners. The five DOI agencies contributing to the document highlighted their areas of expertise and responsibilities and provided phone numbers for further assistance.

❖ UPDATE – ROLLOUT OF CUSTOMER STRATASTATION (CSS)

In 2001, OTFM implemented CSS at all its field locations (Regional and Agency offices). CSS, sometimes referred to as the "electronic worktickets" system, provides for the local input of most trust data at field locations and facilitates the data's electronic transmission, review, and authorization processes. Benefits being realized from this application include, i) increased efficiencies in processing receipts and disbursements, ii) streamlined integration between batching and balancing processes, and iii) it allows for the electronic auditing of cash activity.

❖ UPDATE – LOCATING WHEREABOUTS UNKNOWN ACCOUNT HOLDERS

The Whereabouts Unknown situation can never totally be resolved. Considering the overall number of accounts and the volume of changes requested (or not requested) by account holders, OTFM recognizes that, at any given point in time, the number of whereabouts unknown accounts will never be zero. (Private sector operations (e.g., insurance companies and financial institutions, etc.) also have the problem of not having current addresses for their account holders.)

In the latter part of 2000, OTFM began working with Trans Union Credit Bureau to secure valid and current account holder addresses. Many addresses were obtained through Trans Union's assistance, and in 2001, OTFM worked diligently to confirm and validate the addresses obtained. In spite of our productive efforts however, the total number of whereabouts unknown accounts increased by approximately 7,000 accounts (as of September 30, 2001 versus September 30, 2000).

In the forthcoming year, OTFM plans to further intensify and expand its proactive efforts in locating whereabouts unknown account holders. These plans include using other Trans Union products/services, continued assistance from tribal officials and OTFM outreach initiatives, and publication of whereabouts unknown lists in widely distributed Indian publications. In addition, requests will be made of other Governmental agencies for their assistance.

Fiscal year 2001 has been a year with interesting and progressive changes for both the OST and OTFM. We look forward to the coming year and are optimistic with regards to continued improvements in the management of Indian Trust Funds. OTFM is committed to continuous improvement of services to each beneficiary.



Douglas Lords  
Director, Office of Trust Funds Management

## INDIAN TRUST FUNDS

### Historical Perspective

The legislation, which authorizes the Secretary of the Interior ("the Secretary") to manage the Tribal and Other Trust Funds, and Individual Indian Monies Trust Funds ("Trust Funds"), recognizes the unique trust relationship that exists between the Indian tribes, individual Indians and the U.S. Federal Government. Agreements between the U.S. Federal Government and the various Indian tribes, many in the form of treaties, recognize the sovereignty of the tribes. During the course of the Nation's history and the U.S. Federal Government's evolving policies toward Indian tribes and individual Indians, the trust relationship has retained characteristics based upon tribal sovereignty.

### Mission Statement of OST/OTFM

To assure the highest level of accuracy, responsiveness and service in the receipt, investment and disbursement of all judgment awards, special acts and income from trust resources belonging to Native Americans in accordance with the American Indian Trust Fund Management Reform Act of 1994.

### Designated Trustee

The Secretary is designated by the U.S. Congress as the primary U.S. Federal Government trustee with fiduciary responsibility for the monetary and non-monetary resources held in trust on behalf of American Indian tribes, individual Indians, and other trust funds. In carrying out the management and oversight of Indian trust assets, the Secretary has fiduciary responsibilities including but not limited to, i) collect all monies due from third parties related to the use of Indian lands and the extraction of natural resources from Indian lands, ii) ensure that trust accounts are properly maintained and balances invested, iii) disburse monies to appropriate beneficiaries, and iv) ensure that accurate and complete reports are provided to trust beneficiaries in accordance with applicable law.

### Trust Funds

The monetary balances that have accumulated in the Trust Funds have resulted generally from judgment awards, settlement of claims, land use agreements, royalties on natural resource depletion, other proceeds derived directly from trust resources, and investment income.

Many of the Tribal and Other Trust Funds ("Tribal" Trust Funds) are managed based on U.S. Congressional Acts or particular bequests establishing the funds. For Federal budget purposes, the Trust Funds are reported in two Trust Fund Balance categories, *Held for Indian tribes* and *Held by the Department of the Interior and considered to be U.S. Government funds*. The first category represents funds which are considered non-Federal monies held on behalf of Indian tribes. The second category represents funds which are considered Federal monies, some of which will be transferred to the Held for Indian tribes category provided certain conditions are satisfied or the corpus of the fund may be non-expendable. The Individual Indian Monies Trust Funds ("IIM" Trust Funds) are a deposit fund for individuals who have a beneficial interest. The management of the Trust Funds and related trust assets are performed within various offices within the U.S. Department of the Interior ("Department").

### Special Trustee

Prior to February 9, 1996, the Secretary delegated the authority for management of the Trust Funds, including accounting and financial reporting, to the Assistant Secretary - Indian Affairs, who carried out the management of the Trust Funds through the Bureau of Indian Affairs ("BIA"). On February 9, 1996, in accordance with the authority provided by The American Indian Trust Fund Management Reform Act of 1994 (Pub.L. 103-412) ("the Reform Act"), Secretarial Order 3197 established the Office of the Special Trustee for American Indians ("OST") and delegated all program and administrative authority necessary to carry out the responsibilities of the OST to the Special Trustee for American Indians ("Special Trustee"). Secretarial Order 3197 also transferred intact, the OTFM and other financial trust service functions from the BIA to the OST.

The Special Trustee reports directly to the Secretary and pursuant to the Reform Act is responsible for the oversight of the Department's reform and coordination efforts of all Departmental activities involving policies, procedures, systems and practices used in managing Indian trust assets by various agencies and offices in the Department - not limited to the Office of Trust Funds Management (OTFM), the BIA, Minerals Management Service (MMS), and the Bureau of Land Management (BLM).

### **Trust Assets Management and Trust Funds Management**

Indian trust funds are managed under the authority delegated to the OST. The management of the Indian trust assets that produce those funds is a process that is dependent upon the processing of trust related transactions with the accounting systems of the Department, including but not limited to the BIA, MMS, and certain other Departmental agencies. The BIA, MMS, and other Departmental agencies are responsible for managing the trust resources located within the boundaries of Indian reservations and trust lands as well as the processing of data regarding the ownership and lease of Indian lands. The OTFM is responsible for the management of Trust Funds on behalf of the trust beneficiaries and is significantly dependent and reliant upon the receipt of timely and accurate information derived from the records of the ownership and the lease of trust resources maintained by the BIA and other Departmental agencies.

The DOI maintains staff through a network of Regional, Agency and Field Offices located throughout the United States. The Regional Offices provide administrative and operational support for their respective Agency and Field Offices. Agency and Field Offices are strategically located near the tribes and individuals served. OST personnel are located at the various locations and offices and perform the redelegated functions particular to monetary Trust Funds activities.

### **Organization of the OTFM**

The OTFM, established October 26, 1989, and located in Albuquerque, New Mexico, manages and is accountable for tribal and other trust funds and individual Indian monies trust funds held in trust by the OST. The OTFM carries out its responsibilities through the following divisions.

The Division of Quality Assurance plans, develops, and controls the OTFM management systems review and evaluation program. The Division advises the Director, OTFM, on the efficiency, economy, legality and effectiveness of operations at the program and field level. It ensures that all laws and regulations mandated are received, communicated, and complied with throughout OTFM. It conducts analyses, evaluations, and reviews of operations, including the timely and accurate reconciliation of all cash, assets, and systems. It serves as the liaison between the Office and external audit and evaluation organizations. The Division provides continuing oversight of trust fund systems at headquarters and field operations, identifies problems, and develops recommended action plans for the correction of identified weaknesses. The Division coordinates the development of trust funds policies issued in directives and, in coordination with the OST Directives Officer, assures that all policies and procedures are issued through the approved directives system prior to implementation.

The Division of Trust Funds Systems provides daily OST systems support for the trust funds systems currently in place. It ensures proper maintenance of the existing systems to support the financial management of trust funds. The Division is responsible for testing and implementing automated trust funds financial systems and provides technical support for trust fund aspects of automated data processing, including hardware and software recommendations, acquisitions, installation, and training; and ensures necessary interfaces with other systems. It identifies training needs and provides ongoing training in the operation of automated systems. It manages the OTFM local area network, identifies and installs trust fund related computer equipment and software, and ensures that applications are compatible with other mainframe systems.

The Division of Trust Funds Accounting operates and controls accounting activities which properly record and report all funds received, disbursed, invested, and held in trust for individual Indians and Indian tribes. It plans,

develops, and recommends policies and procedures governing trust operations. It also coordinates with other Federal agencies as necessary in the maintenance of trust accounts.

The Division of Trust Funds Services plans, develops, operates, and controls the buying, selling, and trading of investment instruments in accordance with applicable laws, regulations, and policies. The Division plans, develops, and recommends policies and procedures governing the investment of controlled trust fund accounts, including: accounts belonging to minors; accounts belonging to adult Indians in situations where competent authority has determined that the account must be supervised; accounts of tribal funds made available through judgment awards; contributed funds; and funds deposited to other controlled accounts. The Division provides technical advice and assistance to Indian tribes in developing financial plans requiring access to tribal funds and provides assistance in developing investment strategies for tribal and individual Indian trust funds. It provides technical advice and assistance to BIA Regional offices, agencies, and Indian tribes in developing financial plans and investment strategies for tribal trust funds. The Division functions as the liaison between the OTFM and other public or private sector organizations involved with investments and provides technical information to BIA Regional and Agency operating officials and to tribes regarding the status of funds invested. The Division plans and implements the protocols for dealing with account owner (with the exception of IIM) concerns, questions, and suggestions; implements a tracking system for processing issues and responses; and provides status reports to the Director and other management officials.

The Division of Reporting/Reconciliation reconciles subsidiary and control accounts and monitors trust fund activities at the OTFM and field level. The Division prepares internal and external financial accounting reports and is responsible for their accuracy and timely submission.

The Division of Field Operations located in Oklahoma City, OK, is responsible for coordinating the administrative and technical execution of financial trust programs conducted at subordinate offices; providing or obtaining adequate technical service to guide and support field operations; and evaluating the performance of field level organizations. The Division, through its subordinate branches, is also responsible for the work processes relating to receiving, recording, and disbursing general trust and judgment funds collected by the BIA, belonging to individual Indian adults, minors, legal incompetents, deceased beneficiaries, and tribes; examining, verifying, and maintaining accounts and accounting data for IIM accounts; and preparing, maintaining, and reconciling records. It also responds to IIM account holders' questions concerning the status of accounts, receipts, or other related matters. The field activities of the OTFM are divided among 12 geographical jurisdictions.

### **The Reform Act and The High Level Implementation Plan**

The Reform Act provided the authority for the establishment of the OST and pursuant thereto, the Secretary established the OST via Secretarial Order 3197. In addition, the Reform Act directed the OST to consult with Indian tribes and Indian organizations to develop a comprehensive strategic plan to reform Trust Funds management. In April 1997 the Special trustee prepared and submitted to Congress and the Secretary a strategic plan. The Secretary and the Special Trustee agreed that selected improvements and clean up efforts should proceed as soon as possible. In July 1998 the Secretary published the first High Level Implementation Plan ("HLIP") for the Trust Management Improvement Project. The HLIP provides information on and describes each of the 13 Sub projects, responsible Bureaus and Offices, supporting tasks, critical milestones, work plans, resource estimates, and accountable officials. In February 2000 the Secretary published a revised and updated HLIP that identifies and outlines 11 specific subprojects for the improvement and operation of Trust Funds management for American Indians. (Two of the original subprojects were merged with other subprojects.) The 11 subprojects are in various stages of completion and implementation as of September 30, 2001.

### **The Office of Historical Trust Accounting**

In December 1999, the U.S. District Court, District of Columbia ruled that the Secretary has a duty "to provide plaintiffs an accurate accounting of all money in the IIM trust held in trust for the benefit of plaintiffs, without regard to when the funds were deposited." On appeal the Court of Appeals affirmed the District Court, stating,

that it is "clear that the Interior Secretary owes IIM trust beneficiaries an accounting for all funds held in trust by the United States for the benefit of ... an individual Indian which are deposited or invested pursuant to an Act of June 24, 1938."

On July 10, 2001, Secretarial Order 3231 established the Office of Historical Trust Accounting (OHTA) to plan, organize, direct, and execute the historical accounting of Individual Indian Money accounts. (The OHTA reports to the Office of the Secretary and is not part of the OST.) Furthermore, the order charges the OHTA to create a comprehensive plan outlining how the Department intends to proceed with the historical accounting.

Two reports, *Blueprint for Developing the Comprehensive Historical Accounting Plan for Individual Indian Money Accounts* and *Report Identifying Preliminary Work for the Historical Accounting* were issued by the OHTA on September 10, 2001 and November 7, 2001, respectively. These reports are posted on the OHTA website, <http://www.doi.gov/ohta>.

#### **The Office of Indian Trust Transition**

On November 20, 2001, Secretary Order 3235 established the Office of Indian Trust Transition to serve as a temporary office in the Office of the Secretary responsible for planning and implementing the process for transferring program functions and responsibilities for Indian trust (including trust reform) from certain Departmental bureaus and office to a new entity within the Department. In anticipation of the proposed trust management organization, the Department has submitted a reprogramming request involving funding to Congress. Congress has deferred action on the request pending completion of tribal consultations and, hearings on the reorganization proposal have been scheduled before the House Resources Committee in February 2002.

#### **U.S. District Court Order**

On December 5, 2001 the U.S. District Court (for the District of Columbia) issued a temporary restraining order requiring the Department to, "... immediately disconnect from the Internet all information technology systems that house or provide access to individual Indian trust data," as well as "... all computers within the custody and control of the Department of the Interior, its employees and contractors, that have access to individual Indian trust data." The disconnect of trust related accounting systems has impacted the processing of certain receipts and disbursements of the Trust Funds.

#### **Financial Statements and Annual Audits**

Since 1995, OTFM has contracted for an independent audit of the financial statements of the trust funds it manages for the benefit of individual Indians, tribes, and others. The 1995 audit covered the statement of assets and trust fund balances, internal controls, and compliance with laws and regulations. Audits for fiscal years 1996 through 2001 also included the statement of changes in trust fund balances.

The Office of Inspector General oversees the audit and reviews the resulting reports prior to their release to the public. Certain information in the financial statements of the trust funds is incorporated into the Department's consolidated financial statements.

The audits of the Trust Funds financial statements meet the audit requirement of the Reform Act.



**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Financial Statements

September 30, 2001 and 2000

(With Independent Auditors' Report Thereon)



6565 Americas Parkway, NE #700  
Post Office Box 3939  
Albuquerque, NM 87190

## Independent Auditors' Report

The Special Trustee  
U.S. Department of the Interior Office of the Special  
Trustee for American Indians:

We have audited the accompanying statement of assets and trust fund balances of the Tribal and Other Trust Funds managed by the U.S. Department of the Interior Office of the Special Trustee for American Indians (the OST) Office of Trust Funds Management (the OTFM) and the related statement of changes in trust fund balances as of and for the year ended September 30, 2001. These financial statements are the responsibility of management of the OTFM. Our responsibility is to express an opinion on these financial statements based on our audit. The accompanying financial statements of the Tribal and Other Trust Funds managed by the OTFM as of September 30, 2000, were audited by other auditors whose report, dated December 15, 2000, on those statements was qualified because (1) cash balances reflected in the financial statements were materially greater than balances reported by the U.S. Treasury, (2) inadequacies in various Department of the Interior Indian Trust Fund accounting systems and subsystems, controls and records caused the systems to be unreliable, and (3) various Tribal organizations and classes of individual Indians for whom the OTFM holds financial assets in trust do not agree with certain OTFM accountings and balances recorded by the OTFM; and certain of these parties have filed, or are expected to file, claims against the U.S. Federal Government.

Except as discussed in the fourth paragraph of this report, we conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 2, these financial statements were prepared on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As discussed in note 3, cash balances reflected in the accompanying financial statements are materially greater than balances reported by the U.S. Treasury. In addition, it was not practicable to extend our auditing procedures sufficiently to satisfy ourselves as to the fairness of trust fund balances in the accompanying financial statements as of September 30, 2001 due to inadequacies in certain Department of the Interior trust related accounting systems. Trust fund balances enter into the determination of financial position and changes in trust fund balances. Certain parties for whom the OTFM holds monetary assets in trust do not agree with balances recorded by the OTFM; certain of these parties have filed, or are expected to file, claims against the U.S. Federal Government.



In our opinion, except for the effects on the 2001 financial statements of such adjustments, if any, as might have been determined to be necessary had we been able to apply adequate procedures to support the difference in reported cash balances and determine the fairness of trust fund balances and related changes in trust fund balances, as discussed in the preceding paragraph, the financial statements referred to in the first paragraph above present fairly, in all material respects, the financial position of the Tribal and Other Trust Funds managed by the OTFM as of September 30, 2001, and the changes in trust fund balances for the year then ended in conformity with the basis of accounting described in note 2.

We have also issued a separate report dated January 4, 2002 on the OTFM internal control structure and on its compliance with laws and regulations.

KPMG LLP

January 4, 2002

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Statements of Assets and Trust Fund Balances – Cash Basis

September 30, 2001 and 2000

(In thousands)

<b>Assets</b>	<b>2001</b>	<b>2000</b>
Cash and cash equivalents (note 3)	\$ 748,467	395,367
Investments (note 4)	<u>2,056,550</u>	<u>2,340,819</u>
Total assets	<u>\$ 2,805,017</u>	<u>2,736,186</u>
<b>Trust Fund Balances (notes 6 and 8)</b>		
Held for Indian tribes	\$ 2,610,916	2,558,638
Held by the Department of the Interior and considered to be U.S. Government funds	<u>194,101</u>	<u>177,548</u>
Total trust fund balances	<u>\$ 2,805,017</u>	<u>2,736,186</u>

See accompanying notes to financial statements.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Statements of Changes in Trust Fund Balances – Cash Basis

Years ended September 30, 2001 and 2000

(In thousands)

	2001	2000
<b>Increases:</b>		
Receipts	\$ 360,435	329,441
Interest received on invested funds	169,074	164,736
Gain on disposition of investments, net	6,602	1,647
	536,111	495,824
<b>Decreases:</b>		
Disbursements to and on behalf of Indian tribes and other trust funds and withdrawal of trust funds by Indian tribes (note 8)	467,280	355,391
Increase in trust fund balances, net	68,831	140,433
Trust fund balances, beginning of year	2,736,186	2,595,753
Trust fund balances, end of year (notes 6 and 8)	\$ 2,805,017	2,736,186

See accompanying notes to financial statements.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

**(1) Background and Description of the Trust Funds**

**(a) Overview of the Trust Funds**

**Establishment and management of the Trust Funds** – The legislation which authorizes the Secretary of the U.S. Department of the Interior (the Secretary) to manage the Tribal and Other Trust Funds (Trust Funds) recognizes the unique trust relationship that exists between the Indian tribes, individual Indians, and the U.S. Federal Government. Agreements between the U.S. Federal Government and the various Indian tribes, many of these in the form of treaties, recognize the sovereignty of tribes. During the course of the Nation's history and the U.S. Federal Government's evolving policies toward Indian tribes, the trust relationship has retained characteristics based upon tribal sovereignty. The Secretary has been designated by the U.S. Congress as the primary U.S. Federal Government trustee with fiduciary responsibility for the monetary and nonmonetary resources held in trust on behalf of American Indian tribes, individual Indians, and other trust funds. In carrying out the management and oversight of the Indian trust assets, the Secretary has a fiduciary responsibility to collect all monies due from third parties related to the use of Indian lands and the extraction of natural resources from Indian lands, disburse such monies collected to the appropriate beneficiaries, ensure that trust accounts are properly maintained and invested, and ensure that accurate and complete reports are provided to the trust beneficiaries in accordance with applicable law.

The balances that have accumulated in the Trust Funds have resulted generally from judgment awards, settlement of claims, land use agreements, royalties on natural resource depletion, other proceeds derived directly from trust resources, and investment income.

The accompanying financial statements include only the monetary balances held in trust by the Office of the Special Trustee for American Indians (OST) Office of Trust Funds Management (OTFM) for trust beneficiaries and do not include (i) the account balances of OST or OTFM (federal appropriations, personnel, and administrative costs, etc.) or (ii) other Indian trust assets, including but not limited to, Indian lands, buildings, or other nonmonetary assets managed by the U.S. Department of the Interior (Department).

Prior to February 1996, the Secretary delegated authority for management of the Trust Funds, including accounting and financial reporting, to the Assistant Secretary – Indian Affairs, who carried out the management of the Trust Funds through the Bureau of Indian Affairs (BIA). On February 9, 1996, in accordance with the authority provided by The American Indian Trust Fund Management Reform Act of 1994 (Pub. L. 103-412) (the Reform Act), Secretarial Order 3197 established the OST and delegated all program and administrative authority necessary to carry out the responsibilities of the OST to the Special Trustee for American Indians (Special Trustee). In addition, the OTFM was transferred intact from the BIA to the OST.

**The Reform Act** – The Reform Act authorized the establishment of the OST which is headed by the Special Trustee who reports directly to the Secretary. Under this legislation, the Special Trustee is responsible for oversight, reform and coordination of the policies, procedures, systems and practices

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

used by various agencies of the Department, including but not limited to, the OTFM, the BIA, Minerals Management Service (MMS), and the Bureau of Land Management (BLM), in managing Indian trust assets.

The Reform Act included the following as prospective actions required of the Secretary necessary to properly discharge the trust responsibilities of the United States:

- Providing adequate systems for accounting for and reporting trust fund balances;
- Providing adequate controls over receipts and disbursements;
- Providing periodic, timely reconciliation to assure the accuracy of accounts;
- Determining accurate cash balances;
- Preparing and supplying account holders with periodic statements of their account performance and with balances of their account which shall be available on a daily basis;
- Establishing consistent, written policies and procedures for trust fund management and accounting;
- Providing adequate staffing, supervision, and training for trust fund management and accounting;
- Appropriately managing the natural resources located within boundaries of Indian reservations and trust lands;
- Properly accounting for and investing, as well as maximizing, in a manner consistent with the statutory restrictions imposed on the Secretary's investment options, the return on the investment of all trust fund monies;
- Preparing accurate and timely reports to account holders (and others, as required) on a periodic basis regarding all collections, disbursements, investments, and return on investments related to their trust accounts; and
- Maintaining complete, accurate and timely data regarding the ownership and lease of Indian lands.

Pursuant to the Reform Act, the Special Trustee was to prepare and submit a comprehensive strategic plan to identify all reforms to policies, procedures, practices and systems of the Department, the BIA, MMS, and the BLM together with a timetable for implementing the reforms identified. In April 1997, a Strategic Plan for trust improvement was submitted by the Special Trustee to the Secretary. The Secretary's decision on system improvements and data cleanup efforts was organized into 13 separate but complementary subprojects, which comprise the Trust Management Improvement Project, and the original High Level Implementation Plan (HLIP) which was approved in July 1998. The HLIP provides information on responsible Bureaus and Offices, supporting tasks, critical milestones, work plans, resource estimates, and accountable officials.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

In February 2000, a revised and updated HLIP was issued by the Secretary. The 13 subprojects were reduced to 11 in the revised and updated HLIP and those subprojects are in various stages of completion and implementation as of September 30, 2001.

**Office of the Special Trustee for American Indians** – Indian trust assets, including the Trust Funds, are managed under the delegated authority of the OST and the BIA. Management of Indian trust assets on behalf of the trust beneficiaries is a process that is dependent upon the processing of trust related transactions within the accounting systems of the Department, including but not limited to, the OTFM, the BIA, MMS, and certain other Departmental agencies. The BIA, MMS, and other Departmental agencies are responsible for managing the natural resources located within the boundaries of Indian reservations and trust lands as well as the processing of data regarding the ownership and lease of Indian lands. The OTFM is responsible for the management of Trust Funds on behalf of the trust beneficiaries.

- **Office of Trust Funds Management** – The OTFM, established October 26, 1989, and located in Albuquerque, New Mexico, manages the Tribal and Other Trust Funds and the Individual Indian Monies Trust Funds held in trust by the Department. The allocation and distribution of receipts and disbursements by the OTFM to trust beneficiaries is significantly dependent and reliant upon the receipt of timely and accurate information derived from the records of the ownership and lease of Indian land maintained by the BIA and other Departmental agencies (see note 7).
  - **Regional Offices** – The OTFM and the BIA maintain regional offices located throughout the U.S. which provide administrative and operational support for their respective agency and field offices.
  - **Agency and Field Offices** – The OTFM and the BIA maintain agency and field offices located throughout the U.S. which generally are physically located near the tribes and individual Indians served. OTFM and BIA personnel located at most of the agency offices perform various functions related to trust fund activities. Each of the agency and field offices are organized under one of the regional offices.

**(b) Description of the Trust Funds**

Certain of the Tribal and Other Trust Funds are subject to legal, regulatory, budgetary, court ordered or other restrictions (see note 6). A brief description of the Trust Funds follows:

- **Tribal Trust Funds** – Approximately 1,400 separate accounts comprise the Tribal Trust Funds which totaled approximately \$2,746,488,000 and \$2,681,029,000 as of September 30, 2001 and 2000, respectively.

Tribes realize receipts from a variety of sources, including judgment awards, settlement of claims, land use agreements, royalties on natural resource depletion, other proceeds directly derived from trust resources and investment income.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

- **Other Trust Funds** – Other Trust Funds represent other monetary assets currently managed by the OTFM. Authorization for management of these assets is based on U.S. Congressional Acts or the bequest establishing such funds. Other Trust Funds totaled approximately \$58,529,000 and \$55,157,000 as of September 30, 2001 and 2000, respectively.

Other trust funds realize receipts from a variety of sources, including contracts, leases, licenses, permits, rights of way, etc., settlement of Indian claims, donations and bequests, and investment income.

**(c) Investment of Trust Funds**

Authorizing legislation and a substantial body of case law specify how Indian trust funds should be managed and which financial instruments constitute appropriate investments for the Trust Funds. The Trust Funds invest in U.S. Federal Government securities, including U.S. Treasury and U.S. Federal Government Agency issues, as well as certain other securities that are guaranteed by the U.S. Federal Government.

**(2) Summary of Significant Accounting Policies**

**(a) Basis of Accounting**

The OTFM uses the cash basis of accounting for the Tribal and Other Trust Funds which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The cash basis of accounting differs from accounting principles generally accepted in the United States of America in that receivables and payables are not recorded and premiums and discounts are not amortized or accreted. Receipts are recorded when received and disbursements are recorded when paid. Investments are stated at historical cost. Interest received on invested funds reported in the statements of changes in trust fund balances reflects interest received during the fiscal year.

**(b) Cash and Cash Equivalents**

Management considers all highly liquid financial instruments with maturities of three months or less when purchased to be cash equivalents.

**(c) Investments**

Investment securities at September 30, 2001 and 2000 consist of U.S. Treasury and U.S. Federal Government Agency issues and other securities that are guaranteed by the U.S. Federal Government, mortgage-backed securities, and equity securities. Investment securities are recorded at historical cost. Interest and dividend income are recognized when received.

The Trust Funds investments have a concentration of credit risk in U.S. Federal Government securities, as mandated by 25 USC 162.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

**(d) Receipts**

Receipts from leasing activities, mineral royalties and sales of extracted minerals, timber and forest products, fees and fines, and the granting of easements are generated from a variety of nonmonetary assets that are held in trust by the U.S. Federal Government and managed by the BIA and other Federal Agencies on behalf of tribes. Receipts also include payments, claims and judgment awards to Indian tribes from the U.S. Federal Government. Receipts on hand at the regional and agency offices at September 30, 2001 and 2000, if any, awaiting deposit to Treasury are not included in the financial statements.

**(e) Disbursements**

Payments disbursed from the Trust Funds consist of judgment and settlement awards, accumulations of funds from various income producing activities such as leasing, royalty receipts, minerals extraction and timber and forest product sales and investment income. Under certain conditions, tribes disburse per capita payments to their enrolled members.

Pub. L. 103-412 specifically allows for the voluntary withdrawal of funds from the Trust Funds program. Except where prohibited by statute, an Indian tribe may submit a plan to withdraw some or all funds held in trust for the tribe in accordance with 25 CFR 1200.

**(f) Use of Estimates**

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets at the date of the financial statements and the reported amounts of increases and decreases in trust fund balances during the reporting period. Actual results could differ from those estimates.

**(g) Reclassifications**

Certain amounts in the prior year financial statements have been reclassified to conform to the current year presentation.

**(3) Cash and Cash Equivalents**

Cash equivalents of approximately \$747 million and \$395 million at September 30, 2001 and 2000, respectively, consist primarily of overnight investments with Treasury.

Cash balances reflected by the OTFM for the Tribal and Other Trust Funds and the Individual Indian Monies Trust Funds exceed the balances reported by Treasury by approximately \$33 million and \$35 million as of September 30, 2001 and 2000, respectively.

**(4) Investments**

The historical cost, gross unrealized holding gains, gross unrealized holding losses and fair value of investment securities by major security type and class of security at September 30, 2001 and 2000, were as follows:

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

<i>(In thousands)</i>	<u>Historical cost</u>	<u>Gross unrealized holding gains</u>	<u>Gross unrealized holding losses</u>	<u>Fair value</u>
<b>At September 30, 2001</b>				
U.S. Treasury and Agency securities	\$ 1,978,953	111,720	(184)	2,090,489
Mortgage-backed securities	77,597	3,608	—	81,205
	<u>\$ 2,056,550</u>	<u>115,328</u>	<u>(184)</u>	<u>2,171,694</u>
<b>At September 30, 2000</b>				
U.S. Treasury and Agency securities	\$ 2,214,548	41,477	(55,647)	2,200,378
Equity securities	4,899	—	(48)	4,851
Mortgage-backed securities	121,372	293	(2,886)	118,779
	<u>\$ 2,340,819</u>	<u>41,770</u>	<u>(58,581)</u>	<u>2,324,008</u>

Maturities of investment securities were as follows at September 30, 2001:

<i>(In thousands)</i>	<u>Historical cost</u>	<u>Fair value</u>
Due in one year or less	\$ 272,243	273,917
Due after one year through five years	594,703	625,337
Due after five years through ten years	837,644	874,640
Due after ten years	351,960	397,800
	<u>\$ 2,056,550</u>	<u>2,171,694</u>

**(5) Commitments and Contingencies**

The Secretary has been designated by the U.S. Congress as the primary U.S. Federal Government trustee with fiduciary responsibility for the monetary and nonmonetary resources held in trust on behalf of American Indian tribes, individual Indians, and other trust funds. In carrying out the management and oversight of the Indian trust assets, the Secretary has a fiduciary responsibility to collect all monies due from outside individuals and organizations for the use of Indian lands and the extraction of natural resources from Indian lands, disburse such monies collected to the appropriate beneficiaries, ensure that trust accounts are properly maintained and invested, and ensure that accurate and complete reports are provided to the account holders in accordance with applicable law.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

Tribal organizations have filed various claims against the U.S. Federal Government for failure to fulfill its fiduciary responsibilities and for other related charges. In addition, a class-action lawsuit brought by a group of individual Indians was filed against the U.S. Federal Government alleging breach of trust with respect to the United States' handling of IIM trust fund accounts and various other claims. Neither the OTFM nor the Office of the Solicitor for the Department can presently determine the outcome of these actions nor the total amount, responsibility and funding source of the potential liability. Accordingly, no amounts have been accrued in the accompanying Trust Funds financial statements for potential claims receivable from the U.S. Federal Government.

Any settlement resulting from an adverse outcome of the contingencies described above is generally not expected to be satisfied with trust fund balances.

**(6) Trust Fund Balances**

Trust fund balances are the aggregation of monetary assets held in trust and represent the amounts owed to beneficiaries as of September 30, 2001 and 2000 for which the OTFM has a fiduciary responsibility.

The Trust Funds contain the following Trust Fund Balance categories for Federal budget purposes which are reflected as separate components in the accompanying financial statements:

- *Held for Indian tribes* – These represent funds held on behalf of Indian tribes. These funds are considered non-Federal monies.
- *Held by the Department of the Interior and considered to be U.S. Government funds* – These represent funds, some of which will be transferred to the *Held for Indian tribes* category provided certain conditions are satisfied, or the corpus of the fund may be nonexpendable. These funds are considered Federal monies.

During the year ended September 30, 2001, there were no reclassifications of funds previously reported as Federal monies to non-Federal monies. During the year ended September 30, 2000, two accounts considered Federal monies were reclassified to funds considered non-Federal monies. The San Carlos Apache Tribe Water Rights Settlement Act of 1992 confirming event became effective as of December 28, 1999, and approximately \$58 million is now considered *Held for Indian tribes*. The Zuni Land Conservation Act of 1990 confirming event became effective as of August 31, 2000, and approximately \$18 million is now considered *Held for Indian tribes*.

A portion of trust fund balances represents prepayments and/or deposits on production type leases for which certain individual Indians and tribes hold an interest (see note 7). Any deposits in excess of production are returned to the depositor. Such excess deposits as of September 30, 2001 and 2000 have not been quantified.

Included in the Trust Funds are certain balances which are presently not identified to specific Indian tribes because judgment awards were granted to several Indian tribes in a particular geographic area for settlement of claims related to certain lands.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

**(7) Related Party Transactions with Other U.S. Federal Government Organizations**

**(a) *U.S. Department of the Interior Bureau of Indian Affairs***

The OTFM receives lease payments from the BIA which are collected from users of Indian lands or other nonmonetary assets managed by the Department on behalf of Indian tribes, other trust funds, and individual Indians. The BIA generally forwards the payments to designated collection officers upon receipt. Subsequently, instructions to enable the OTFM to record the receipts directly into the appropriate Tribal or Other Trust account(s) are forwarded to the OTFM, either manually or via electronic interface.

**(b) *U.S. Department of the Interior Minerals Management Service***

The OTFM receives royalty payments from MMS on behalf of Indian tribes and individual Indians holding mineral rights. MMS generally transfers the royalty payments to the OTFM following deposit to the Treasury. At the time the royalty payments are received, MMS provides the OTFM an allocation of 100% tribally-owned lease royalties, permitting the OTFM to record the receipts directly into tribal accounts. For tribally and individually co-owned leases, the royalty payments are forwarded by MMS and subsequently distributed to the proper account through the Royalty Distribution Reporting System maintained by the BIA. MMS and the BLM both perform verification and other monitoring procedures of mineral assets.

Oil and gas companies sometimes make overpayments to MMS and these overpayments may be disbursed by the OTFM to the beneficiaries. The overpayments generally result from payments being made based on estimated mineral production in order to comply with the Federal Oil and Gas Royalty Management Act of 1982 that requires timely distribution of royalties. Typically, oil and gas companies recover such overpayments by adjusting future payments. The amounts of such overpayments, if any, as of September 30, 2001 and 2000 are not readily determinable and have not been quantified in the financial statements.

**(c) *Other***

The Treasury holds cash and overnight investments and disburses for the OTFM. The Department's Office of the Solicitor serves as legal counsel for the OST and OTFM.

**(8) Transfers to Individual Indian Monies (IIM) Trust Funds**

The OTFM, pursuant to information provided by the BIA, utilizes special deposit accounts maintained within the IIM Trust Funds for both tribal and IIM beneficiaries as suspense accounts whereby funds are temporarily posted when the proper allocation information is not provided when the funds are received. Following determination of the proper allocation by the BIA, the funds are transferred from the special deposit accounts to the appropriate tribal and/or IIM account(s). In addition, certain oil and gas distributions and per capita disbursements authorized by tribes may result in transfers from the Tribal and Other Trust Funds to the IIM Trust Funds. Net transfers from the Tribal and Other Trust Funds to the IIM trust funds totaled approximately \$42 million and \$7 million during the years ended September 30, 2001 and 2000, respectively. These transfers are reflected as disbursements in the accompanying statements of

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

changes in trust fund balances. The amount of monies, if any, not yet transferred has not been quantified in the financial statements.

**(9) Subsequent Events**

In November 2001, Secretarial Order 3235 established the Office of Indian Trust Transition to serve as a temporary office in the Office of the Secretary responsible for planning and implementing the process for transferring program functions and responsibilities for Indian trust (including trust reform) from certain Departmental bureaus and offices to a new organization within the Department.

On December 5, 2001, the U.S. District Court (for the District of Columbia) issued a temporary restraining order requiring the Department to immediately disconnect from the internet all information technology systems that house or provide access to individual Indian trust data as well as all computers within the custody and control of the Department of the Interior that have access to individual Indian trust data. The disconnect of trust related information technology systems has impacted the processing of certain receipts and disbursements of the Trust Funds.



**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Financial Statements

September 30, 2001 and 2000

(With Independent Auditors' Report Thereon)



6565 Americas Parkway, NE #700  
Post Office Box 3939  
Albuquerque, NM 87190

## Independent Auditors' Report

The Special Trustee  
U.S. Department of the Interior Office of the Special  
Trustee for American Indians:

We have audited the accompanying statement of assets and trust fund balances of the Individual Indian Monies Trust Funds managed by the U.S. Department of the Interior Office of the Special Trustee for American Indians (the OST) Office of Trust Funds Management (the OTFM) and the related statement of changes in trust fund balances as of and for the year ended September 30, 2001. These financial statements are the responsibility of management of the OTFM. Our responsibility is to express an opinion on these financial statements based on our audit. The accompanying financial statements of the Individual Indian Monies Trust Funds managed by the OTFM as of September 30, 2000, were audited by other auditors whose report, dated December 15, 2000, on those statements was qualified because (1) cash balances reflected in the financial statements were materially greater than balances reported by the U.S. Treasury, (2) inadequacies in various Department of the Interior Indian Trust Fund accounting systems and subsystems, controls and records caused the systems to be unreliable, and (3) various Tribal organizations and classes of individual Indians for whom the OTFM holds financial assets in trust do not agree with certain OTFM accountings and balances recorded by the OTFM; and certain of these parties have filed, or are expected to file, claims against the U.S. Federal Government.

Except as discussed in the fourth paragraph of this report, we conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 2, these financial statements were prepared on the modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As discussed in note 3, cash balances reflected in the accompanying financial statements are materially greater than balances reported by the U.S. Treasury. In addition, it was not practicable to extend our auditing procedures sufficiently to satisfy ourselves as to the fairness of trust fund balances in the accompanying financial statements as of September 30, 2001 due to inadequacies in certain Department of the Interior trust related accounting systems. Trust fund balances enter into the determination of financial position and changes in trust fund balances. Certain parties for whom the OTFM holds monetary assets in trust do not agree with balances recorded by the OTFM; and certain of these parties have filed, or are expected to file, claims against the U.S. Federal Government.



In our opinion, except for the effects on the 2001 financial statements of such adjustments, if any, as might have been determined to be necessary had we been able to apply adequate procedures to support the difference in reported cash balances and determine the fairness of trust fund balances and related changes in trust fund balances, as discussed in the preceding paragraph, the financial statements referred to in the first paragraph above present fairly, in all material respects, the financial position of the Individual Indian Monies Trust Funds managed by the OTFM as of September 30, 2001, and the changes in trust fund balances for the year then ended in conformity with the basis of accounting described in note 2.

We have also issued a separate report dated January 4, 2002 on the OTFM internal control structure and on its compliance with laws and regulations.

KPMG LLP

January 4, 2002

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Statements of Assets and Trust Fund Balances – Modified Cash Basis

September 30, 2001 and 2000

(In thousands)

<b>Assets</b>	<b>2001</b>	<b>2000</b>
Cash and cash equivalents (note 3)	\$ 44,140	19,039
Investments (note 4)	354,580	375,383
Accrued interest receivable	5,420	5,447
Total assets	\$ 404,140	399,869
<b>Trust Fund Balances</b>		
Held for individual Indians (note 6)	\$ 404,140	399,869

See accompanying notes to financial statements.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Statements of Changes in Trust Fund Balances – Modified Cash Basis

Years ended September 30, 2001 and 2000

(In thousands)

	2001	2000
<b>Increases:</b>		
Receipts (note 8)	\$ 199,641	215,257
Interest and dividends earned on invested funds	26,262	30,271
Gain (loss) on disposition of investments, net	84	(364)
	225,987	245,164
<b>Decreases:</b>		
Disbursements to and on behalf of account holders	221,716	294,575
Increase (decrease) in trust fund balances, net	4,271	(49,411)
Trust fund balances, beginning of year	399,869	449,280
Trust fund balances, end of year (note 6)	\$ 404,140	399,869

See accompanying notes to financial statements.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

**(1) Background and Description of the Trust Funds**

**(a) Overview of the Trust Funds**

**Establishment and management of the Trust Funds** – The legislation which authorizes the Secretary of the U.S. Department of the Interior (the Secretary) to manage the Individual Indian Monies Trust Funds (IIM Trust Funds) recognizes the unique trust relationship that exists between the Indian tribes, individual Indians, and the U.S. Federal Government. Agreements between the U.S. Federal Government and the various Indian tribes, many of these in the form of treaties, recognize the sovereignty of tribes. During the course of the Nation's history and the U.S. Federal Government's varying policies toward individual Indians and Indian tribes, the trust relationship has retained characteristics based upon tribal sovereignty. The Secretary has been designated by the U.S. Congress as the primary U.S. Federal Government trustee with fiduciary responsibility for the monetary and nonmonetary resources held in trust on behalf of American Indian tribes, individual Indians, and other trust funds. In carrying out the management and oversight of the Indian trust assets, the Secretary has a fiduciary responsibility to collect all monies due from third parties related to the use of Indian lands and the extraction of natural resources from Indian lands, disburse such monies collected to the appropriate beneficiaries, ensure that trust accounts are properly maintained and invested, and ensure that accurate and complete reports are provided to the trust beneficiaries in accordance with applicable law.

The balances that have accumulated in the IIM Trust Funds have resulted generally from judgment awards, settlement of claims, land use agreements, royalties on natural resource depletion, other proceeds derived directly from trust resources, receipt of per capita distributions, and investment income.

The accompanying financial statements include only the monetary balances held in trust by the Office of the Special Trustee for American Indians (OST) Office of Trust Funds Management (OTFM) for trust beneficiaries and do not include (i) the account balances of OST or OTFM (federal appropriations, personnel and administrative costs, etc.) or (ii) other Indian trust assets, including but not limited to, Indian lands, buildings or other nonmonetary assets managed by the U.S. Department of the Interior (Department).

Prior to February 1996, the Secretary delegated authority for management of the Trust Funds, including accounting and financial reporting, to the Assistant Secretary – Indian Affairs, who carried out the management of the Trust Funds through the Bureau of Indian Affairs (BIA). On February 9, 1996, in accordance with the authority provided by The American Indian Trust Fund Management Reform Act of 1994 (Pub. L. 103-412) (the Reform Act), Secretarial Order 3197 established the OST and delegated all program and administrative authority necessary to carry out the responsibilities of the OST to the Special Trustee for American Indians (Special Trustee). In addition, the OTFM was transferred intact from the BIA to the OST.

**The Reform Act** – The Reform Act authorized the establishment of the OST which is headed by the Special Trustee who reports directly to the Secretary. Under this legislation, the Special Trustee is

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

responsible for oversight, reform and coordination of the policies, procedures, systems and practices used by various agencies of the Department, including but not limited to, the OTFM, the BIA, Minerals Management Service (MMS), and the Bureau of Land Management (BLM), in managing Indian trust assets.

The Reform Act included the following as prospective actions required of the Secretary necessary to properly discharge the trust responsibilities of the United States:

- Providing adequate systems for accounting for and reporting trust fund balances;
- Providing adequate controls over receipts and disbursements;
- Providing periodic, timely reconciliations to assure the accuracy of accounts;
- Determining accurate cash balances;
- Preparing and supplying account holders with periodic statements of their account performance and with balances of their account which shall be available on a daily basis;
- Establishing consistent, written policies and procedures for trust fund management and accounting;
- Providing adequate staffing, supervision, and training for trust fund management and accounting;
- Appropriately managing the natural resources located within boundaries of Indian reservations and trust lands;
- Properly accounting for and investing, as well as maximizing, in a manner consistent with the statutory restrictions imposed on the Secretary's investment options, the return on the investment of all trust fund monies;
- Preparing accurate and timely reports to account holders (and others, as required) on a periodic basis regarding all collections, disbursements, investments, and return on investments related to their trust accounts; and
- Maintaining complete, accurate and timely data regarding the ownership and lease of Indian lands.

Pursuant to the Reform Act, the Special Trustee was to prepare and submit a comprehensive strategic plan to identify all reforms to policies, procedures, practices and systems of the Department, the BIA, MMS, and the BLM together with a timetable for implementing the reforms identified. In April 1997, a Strategic Plan for trust improvement was submitted by the Special Trustee to the Secretary. The Secretary's decision on system improvements and data cleanup efforts was organized into 13 separate but complementary subprojects, which comprise the Trust Management Improvement Project, and the original High Level Implementation Plan (HLIP) which was approved in July 1998. The HLIP provides information on responsible Bureaus and Offices, supporting tasks, critical milestones, work plans, resource estimates and accountable officials.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

In February 2000, a revised and updated HLIP was issued by the Secretary. The 13 subprojects were reduced to 11 in the revised and updated HLIP and the subprojects are in various stages of completion and implementation as of September 30, 2001.

**Office of the Special Trustee for American Indians** – Indian trust assets, including the Trust Funds, are managed under the delegated authority of the OST and the BIA. Management of Indian trust assets on behalf of the trust beneficiaries is a process that is dependent upon the processing of trust related transactions within the accounting systems of the Department, including but not limited to, the OTFM, the BIA, MMS, and certain other Departmental agencies. The BIA, MMS, and other Departmental agencies are responsible for managing the natural resources located within the boundaries of Indian reservations and trust lands as well as the processing of data regarding the ownership and lease of Indian lands. The OTFM is responsible for the management of Trust Funds on behalf of the trust beneficiaries.

- **Office of Trust Funds Management** – The OTFM, established October 26, 1989, and located in Albuquerque, New Mexico, manages the Tribal and Other Trust Funds and the Individual Indian Monies Trust Funds held in trust by the Department. The allocation and distribution of receipts and disbursements by the OTFM to trust beneficiaries is significantly dependent and reliant upon the receipt of timely and accurate information derived from the records of the ownership and lease of Indian land maintained by the BIA and other Departmental agencies (see note 7).
  - **Regional Offices** – The OTFM and the BIA maintain regional offices located throughout the U.S. which provide administrative and operational support for their respective agency and field offices.
  - **Agency and Field Offices** – The OTFM and the BIA maintain agency and field offices located throughout the U.S. which generally are physically located near the tribes and individual Indians served. OTFM and BIA personnel located at most of the agency offices perform various functions related to trust fund activities. Each of the agency and field offices are organized under one of the regional offices.

**(b) Description of the Trust Funds**

Certain of the IIM Trust Funds described below are subject to legal, regulatory, budgetary, court ordered or other restrictions. Approximately 247,000 and 258,000 open accounts, held for the benefit of individual Indian account holder beneficiaries and tribal entities, comprise the IIM Trust Funds as of September 30, 2001 and 2000, respectively. The IIM Trust Funds contain certain special deposit accounts for certain tribal entities.

The IIM Trust Funds are primarily funds on deposit for individual Indians with a beneficial interest in those funds. IIM account holders realize receipts primarily from judgment awards, settlement claims, land use agreements, royalties on natural resource depletion, other proceeds derived directly from trust resources, per capita distributions and investment income.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

**(c) *Investment of Trust Funds***

Authorizing legislation and a substantial body of case law specify how Indian trust funds should be managed and which financial instruments constitute appropriate investments for Indian Trust Funds. The IIM Trust Funds invest in U.S. Federal Government securities, including U.S. Treasury and U.S. Federal Government Agency issues, as well as certain other securities that are guaranteed by the U.S. Federal Government.

**(2) Summary of Significant Accounting Policies**

**(a) *Basis of Accounting***

The OTFM uses the cash basis of accounting with certain modifications for the IIM Trust Funds which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Receipts are recorded when received with the exception of interest earned on invested funds (including discount accretion and premium amortization), and disbursements are recorded when paid. Investments are stated at amortized cost. Accrual adjustments to reflect interest and dividends earned but not received, and to record any applicable accretion of discounts and amortization of premiums over the terms of the investments have been recorded in the accompanying financial statements. Interest income reported in the statements of changes in trust fund balances reflect interest earned, net of any premium amortization or discount accretion recognized during the fiscal year.

**(b) *Cash and Cash Equivalents***

Management considers all highly liquid financial instruments with maturities of three months or less when purchased to be cash equivalents.

**(c) *Investments***

Investment securities at September 30, 2001 and 2000 consist of U.S. Treasury and U.S. Federal Government Agency issues and other securities that are guaranteed by the U.S. Federal Government, mortgage-backed securities, and equity securities. IIM Trust Funds are pooled and invested. Investment securities are recorded at amortized cost, adjusted for the amortization or accretion of premiums or discounts. Premiums and discounts are amortized or accreted over the life of the related investment security as an adjustment to yield using the effective interest method. Dividend and interest income are recognized when earned.

The Trust Funds investments have a concentration of credit risk in U.S. Federal Government securities, as mandated by 25 USC 162.

**(d) *Receipts***

Receipts from various leasing activities, mineral royalties and sales of extracted minerals, timber and forest products, fees and fines, and the granting of easements are generated from a variety of nonmonetary assets that are held in trust by the U.S. Federal Government and managed by the BIA.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

and other Federal Agencies on behalf of individual Indians. Receipts also include payments, claims, and judgment awards to individual Indians from the U.S. Federal Government. Receipts on hand at the regional and agency offices at September 30, 2001 and 2000, if any, awaiting deposit to Treasury are not included in the financial statements.

**(e) Disbursements**

Payments disbursed to and on behalf of individual Indians consist of accumulations of investment income, as well as funds from various income-producing activities such as leasing, royalty receipts, mineral extraction, and timber and forest product sales and per capita payments.

**(f) Use of Estimates**

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets at the date of the financial statements and the reported amounts of increases and decreases in trust fund balances during the reporting period. Actual results could differ from those estimates.

**(g) Reclassifications**

Certain amounts in the prior year financial statements have been reclassified to conform to the current year presentation.

**(3) Cash and Cash Equivalents**

Cash equivalents of approximately \$44 million and \$18 million at September 30, 2001 and 2000, respectively, consist primarily of overnight investments with Treasury.

Cash balances reflected by the OTFM for the Tribal and Other Trust Funds and the IIM Trust Funds exceed the balances reported by Treasury by approximately \$33 million and \$35 million as of September 30, 2001 and 2000, respectively.

**(4) Investments**

The amortized cost, gross unrealized holding gains, gross unrealized holding losses and fair value of investment securities by major security type and class of security at September 30, 2001 and 2000, were as follows:

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

<i>(In thousands)</i>	<u>Amortized cost</u>	<u>Gross unrealized holding gains</u>	<u>Gross unrealized holding losses</u>	<u>Fair value</u>
<b>At September 30, 2001</b>				
U.S. Treasury and Agency securities	\$ 348,616	18,487	—	367,103
Mortgage-backed securities	5,964	604	—	6,568
	<u>\$ 354,580</u>	<u>19,091</u>	<u>—</u>	<u>373,671</u>
<b>At September 30, 2000</b>				
U.S. Treasury and Agency securities	\$ 364,027	4,741	(9,235)	359,533
Equity securities	5,000	—	(25)	4,975
Mortgage-backed securities	6,356	272	—	6,628
	<u>\$ 375,383</u>	<u>5,013</u>	<u>(9,260)</u>	<u>371,136</u>

Maturities of investment securities were as follows at September 30, 2001:

<i>(In thousands)</i>	<u>Amortized cost</u>	<u>Fair value</u>
Due in one year or less	\$ 74,632	74,811
Due after one year through five years	82,074	87,531
Due after five years through ten years	139,190	146,290
Due after ten years	58,684	65,039
	<u>\$ 354,580</u>	<u>373,671</u>

**(5) Commitments and Contingencies**

The Secretary has been designated by the U.S. Congress as the primary U.S. Federal Government trustee with fiduciary responsibility for the monetary and nonmonetary resources held in trust on behalf of American Indian tribes, individual Indians, and other trust funds. In carrying out the management and oversight of the Indian trust assets, the Secretary has a fiduciary responsibility to collect all monies due from outside individuals and organizations for the use of Indian lands and the extraction of natural resources from Indian lands, disburse such monies collected to the appropriate beneficiaries, ensure that

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

trust accounts are properly maintained and invested, and ensure that accurate and complete reports are provided to the account holders in accordance with applicable law.

A class-action lawsuit brought by a group of individual Indians was filed against the U.S. Federal Government alleging breach of trust with respect to the United States' handling of IIM trust fund accounts and various other claims. Neither the OTFM nor the Office of the Solicitor for the Department can presently determine the outcome of these actions nor the total amount, responsibility and funding source of the potential liability. Accordingly, no amounts have been accrued in the accompanying IIM Trust Funds financial statements for potential claims receivable from the U.S. Federal Government.

Any settlement resulting from an adverse outcome of the contingencies described above is generally not expected to be satisfied with trust fund balances.

**(6) Trust Fund Balances**

Trust fund balances are the aggregation of monetary assets held in trust and represent the amounts owed to beneficiaries as of September 30, 2001 and 2000 for which the OTFM has a fiduciary responsibility.

The trust fund balances reflected in the accompanying IIM Trust Funds financial statements include certain cumulative differences between the control account and the subsidiary detail of IIM account holders' balances, with the net total of the control account reflecting the greater balance. As of September 30, 2001 and 2000, the aggregate of all positive fund balances included in the IIM subsidiary detail of account holders' balances exceeded the assets by approximately \$6.7 million and the IIM detailed subsidiary accounts contain certain accounts with negative balances aggregating approximately \$44 million.

The subsidiary detail of IIM account holders' balances contains approximately 20,000 special deposit accounts with balances totaling approximately \$67 million and \$63 million as of September 30, 2001 and 2000, respectively. A portion of the special deposit account monies held in the IIM Trust Funds has not been distributed to the beneficiaries because the ultimate disposition of the funds has not been determined.

A portion of trust fund balances represents prepayments and/or deposits on production type leases for which certain individual Indians and tribes hold an interest (see note 7). Any deposits in excess of production are returned to the depositor. Such excess deposits as of September 30, 2001 and 2000 have not been quantified.

**(7) Related Party Transactions With Other U.S. Federal Government Organizations**

**(a) U.S. Department of the Interior Bureau of Indian Affairs**

The OTFM receives lease payments from the BIA which are collected from users of Indian lands or other nonmonetary assets managed by the Department on behalf of Indian tribes, other trust funds, and individual Indians. The BIA generally forwards the payments to designated collection officers upon receipt. Subsequently, instructions to enable the OTFM to record the receipts directly into the appropriate IIM account(s) are forwarded to the OTFM, either manually or via electronic interface.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

**(b) U.S. Department of the Interior Mineral Management Service**

The OTFM receives royalty payments from the MMS on behalf of Indian tribes and individual Indians holding mineral rights. MMS generally transfers the royalty payments to the OTFM following deposit to the Treasury. For tribally and individually co-owned leases, the royalty payments are forwarded by MMS and subsequently distributed to the proper IIM account through the Royalty Distribution Reporting System maintained by the BIA. MMS and the BLM both perform verification and other monitoring procedures of mineral assets.

Oil and gas companies sometimes make overpayments to MMS and these overpayments may be disbursed by the OTFM to the beneficiaries. The overpayments generally result from payments being made based on estimated mineral production, in order to comply with the Federal Oil and Gas Royalty Management Act of 1982, which requires timely distribution of royalties. Typically, the oil and gas companies recover such overpayments by adjusting future payments. The amounts of such overpayments if any as of September 30, 2001 and 2000, are not readily determinable and have not been quantified in the financial statements.

**(c) Other**

The Treasury holds cash and overnight investments and disburses for the OTFM. The Department's Office of the Solicitor serves as legal counsel for the OST and OTFM.

**(8) Transfers from Tribal and Other Trust Funds**

The OTFM, pursuant to information provided by the BIA, utilizes special deposit accounts maintained within the IIM Trust Funds for both tribal and IIM beneficiaries as suspense accounts whereby funds are temporarily posted when the proper allocation information is not provided when the funds are received. Following determination of the proper allocation by the BIA, the funds are transferred from the special deposit accounts to the appropriate tribal and/or IIM account(s). In addition, certain oil and gas distributions and per capita disbursements authorized by tribes may result in transfers from the Tribal and Other Trust Funds to the IIM Trust Funds. Net transfers to the IIM trust funds from the Tribal and Other Trust Funds totaled approximately \$42 million and \$7 million during the years ended September 30, 2001 and 2000, respectively. These transfers are reflected as receipts in the accompanying statements of changes in trust fund balances. The amount of monies, if any, not yet transferred has not been quantified in the financial statements.

**(9) Subsequent Events**

In November 2001, Secretarial Order 3235 established the Office of Indian Trust Transition to serve as a temporary office in the Office of the Secretary responsible for planning and implementing the process for transferring program functions and responsibilities for Indian trust (including trust reform) from certain Departmental bureaus and offices to a new organization within the Department.

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Notes to Financial Statements

September 30, 2001 and 2000

On December 5, 2001, the U.S. District Court (for the District of Columbia) issued a temporary restraining order requiring the Department to immediately disconnect from the internet all information technology systems that house or provide access to individual Indian trust data as well as all computers within the custody and control of the Department of the Interior that have access to individual Indian trust data. The disconnect of trust related information technology systems has impacted the processing of certain receipts and disbursements of the Trust Funds.



**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS AND  
INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Auditors' Report on Internal Control Structure  
and  
Compliance with Laws and Regulations

September 30, 2001



6565 Americas Parkway, NE #700  
Post Office Box 3939  
Albuquerque, NM 87190

## Independent Auditors' Report

The Special Trustee  
U.S. Department of the Interior Office of the Special  
Trustee for American Indians:

We have audited the statement of assets and trust fund balances for the Tribal and Other Trust Funds as of September 30, 2001 and the related statement of changes in trust fund balances for the year then ended, and the statement of assets and trust fund balances for the Individual Indian Monies Trust Funds as of September 30, 2001 and the related statement of changes in trust fund balances for the year then ended (collectively referred to as the Trust Fund financial statements) managed by the U.S. Department of the Interior Office of the Special Trustee for American Indians Office of Trust Funds Management (OTFM) and have issued our reports thereon dated January 4, 2002. Our reports were qualified because cash balances reflected in the Trust Fund financial statements were materially greater than balances reported by the U.S. Department of the Treasury. In addition, it was not practicable to extend our auditing procedures sufficiently to satisfy ourselves as to the fairness of trust fund balances in the Trust Fund financial statements as of September 30, 2001 due to inadequacies in certain Department of the Interior trust related accounting systems. Trust fund balances enter into the determination of financial position and changes in trust fund balances. Certain parties for whom the OTFM holds monetary assets in trust do not agree with balances recorded by the OTFM; and certain of these parties have filed, or are expected to file, claims against the U.S. Federal Government. Our reports also state that the Trust Fund financial statements are prepared in accordance with a basis of accounting which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America as described in note 2 to the financial statements. The objective of our audit was to express an opinion on the fair presentation of the Trust Fund financial statements. In connection with our audit, we also considered the OTFM's internal control over financial reporting and tested the OTFM's compliance with certain provisions of applicable laws and regulations that could have a direct and material effect on the Trust Fund financial statements.

### SUMMARY

Our consideration of internal control over financial reporting resulted in the following conditions being identified as reportable conditions:

- A. Reliance on Processing of Trust Transactions at the Bureau of Indian Affairs
- B. Financial Reporting – Unresolved Matters From Prior Periods
- C. Improve Controls Over Information Technology Systems

We consider reportable conditions A and B above to be material weaknesses.

The results of our tests of compliance with the laws and regulations described in the responsibilities section of this report disclosed no instances of noncompliance with laws and regulations that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*.

The following sections discuss our opinion on the Trust Fund financial statements, our consideration of the OTFM's internal control over financial reporting, our tests of the OTFM's compliance with certain provisions of applicable laws and regulations, and management's and our responsibilities.

## **INTERNAL CONTROL OVER FINANCIAL REPORTING**

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the OTFM's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements.

Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal control, misstatements, due to error or fraud may nevertheless occur and not be detected.

### ***Overview – Trust Fund Financial Statements***

The accounting systems and internal control procedures used in the processing of Indian trust transactions have suffered historically from a variety of system and procedural internal control weaknesses. In addition, current management is burdened with the ongoing impact of decades of accumulated discrepancies in the accounting records.

The Secretary of the Department of the Interior (the Secretary) has been designated by the U.S. Congress as the primary U.S. Federal Government trustee with fiduciary responsibility for the monetary and nonmonetary resources held in trust on behalf of American Indian tribes, individual Indians, and other trust funds. In carrying out the management and oversight of the Indian trust assets, the Secretary has a fiduciary responsibility to collect all monies due from third parties related to the use of Indian lands and the extraction of natural resources from Indian lands, disburse such monies collected to the appropriate beneficiaries, ensure that trust accounts are properly maintained and invested, and ensure that accurate and complete reports are provided to the trust beneficiaries in accordance with applicable law.

Prior to February 1996, the Secretary delegated authority for management of trust funds, including accounting and financial reporting, to the Assistant Secretary – Indian Affairs, who carried out the management of the trust funds through the Bureau of Indian Affairs (BIA).

On February 9, 1996, in accordance with the authority provided by The American Indian Trust Fund Management Reform Act of 1994 (Pub. L. 103-412) (the Reform Act), Secretarial Order 3197 established the Office of the Special Trustee for American Indians (OST) and delegated all program and administrative authority necessary to carry out the responsibilities of the OST to the Special Trustee for American Indians (Special Trustee) who reports directly to the Secretary. In addition, the OTFM was transferred intact from the BIA to the OST.

Under this legislation, the Special Trustee is responsible for oversight, reform and coordination of the policies, procedures, systems and practices used by various agencies of the Department of the Interior (Department), including but not limited to, the OTFM, the BIA, Minerals Management Services (MMS) and the Bureau of Land Management (BLM), in managing Indian trust assets.

The Reform Act included the following as prospective actions required of the Secretary necessary to properly discharge the trust responsibilities of the United States:

- Providing adequate systems accounting for and reporting trust fund balances;
- Providing adequate controls over receipts and disbursements;
- Providing periodic, timely reconciliation to assure the accuracy of accounts;
- Determining accurate cash balances;
- Preparing and supplying account holders with periodic statements of their account performance and with balances of their account which shall be available on a daily basis;
- Establishing consistent, written policies and procedures for trust fund management and accounting;
- Providing adequate staffing, supervision, and training for trust fund management and accounting;
- Appropriately managing the natural resources located within boundaries of Indian reservations and trust lands;
- Properly accounting for and investing, as well as maximizing, in a manner consistent with the statutory restrictions imposed on the Secretary's investment options, the return on the investment of all trust fund monies;
- Preparing accurate and timely reports to account holders (and others, as required) on a periodic basis regarding all collections, disbursements, investments, and return on investments related to their trust accounts; and
- Maintaining complete, accurate, and timely data regarding the ownership and lease of Indian lands.

Pursuant to the Reform Act, the Special Trustee was to prepare and submit a comprehensive strategic plan to identify all reforms to policies, procedures, practices and systems of the Department, the BIA, MMS, and the BLM together with a timetable for implementing the reforms identified. In April 1997, a Strategic Plan for trust improvement was submitted by the Special Trustee to the Secretary. The Secretary's decision on system improvements and data cleanup efforts was organized into 13 separate but complementary subprojects, which comprise the Trust Management Improvement Project, and the original High Level Implementation Plan (HLIP) which was approved in July 1998. The HLIP provides information on responsible Bureaus and Offices, supporting tasks, critical milestones, work plans, resource estimates, and accountable officials.

In February 2000, a revised and updated HLIP was issued by the Secretary. The following is an excerpt from the revised and updated HLIP published by the Department.

“Concerns about the management of Indian Trust funds have been a longstanding issue. As early as 1928, the General Accounting Office (GAO) – the investigative research arm of Congress – issued reports documenting weak accounting practices and other problems in Bureau of Indian Affairs (BIA) trust fund management.”

Since then, there have been numerous reports highlighting weaknesses in management and accounting practices from such overseeing entities as the Congressional Committees, the Office of Management and Budget (OMB), the Office of the Inspector General, and Department Bureau reviews as well as outside contractor reports.

The 13 subprojects were reduced to 11 in the revised and updated HLIP and those subprojects are in various stages of completion and implementation as of September 30, 2001.

The 11 subprojects in the revised and updated HLIP are as follows:

- OST Trust Administrative Records Cleanup
- Trust Funds Accounting System (TFAS)
- Records Management
- Training
- Internal Controls
- BIA Trust Resource Records Cleanup
- Probate Backlog
- BIA Appraisal Program
- Trust Asset and Accounting Management System (TAAMS)
- MMS System Reengineering
- Policies and Procedures

We noted certain matters involving internal control over financial reporting and its operation that we consider to be reportable conditions. We believe that the following reportable conditions are material weaknesses:

**A. Reliance on Processing of Trust Transactions at the Bureau of Indian Affairs**

***Condition***

Indian trust assets, including the Trust Funds, are managed under the delegated authority of the OST and the BIA. Management of Indian trust assets on behalf of the trust beneficiaries is a process that is dependent upon the processing of trust related transactions within the accounting systems of the Department, including but not limited to, the OTFM, the BIA, MMS, and certain other Departmental agencies. The BIA, MMS, and other Departmental agencies are responsible for managing the natural resources located within the boundaries of Indian reservations and trust lands as well as the processing of data regarding the ownership and lease of Indian lands. The OTFM is responsible for the management of the Trust Funds on behalf of trust beneficiaries. The allocation and distribution of receipts and disbursements by the OTFM to trust beneficiaries is significantly dependent and reliant upon the receipt of timely and accurate information derived from the records of the ownership and lease of Indian land maintained by the BIA and other Departmental agencies.

The independent auditors' report on internal control over financial reporting for the year ended September 30, 2001 at the BIA contained two reportable conditions which were considered material weaknesses. Specifically, material weaknesses related to controls over information technology systems and controls over processing of Indian trust transactions were included in the report. The presence of these reportable conditions directly impacts the OTFM's ability to process monetary trust transactions on behalf of trust beneficiaries and to provide accurate information to account holders due to the interrelationship between the BIA and the OTFM.

The first material weakness relates to controls over information technology systems at the BIA. Specifically, the presence of weaknesses in BIA computer systems raises concerns about the integrity of information being reported on in the financial statements of the Trust Funds. Although the BIA

has taken preliminary steps in establishing a formal security program, the BIA has not implemented information systems security policies or procedures to effectively control and protect information systems, programs and data supporting BIA operations and assets, which includes management of Indian trust assets, and has failed to meet minimum information technology (IT) security requirements. The second material weakness relates to controls over the processing of Indian trust transactions. The BIA performs a critical role in the initial input and subsequent changes to Indian trust accounting data in its various regional and agency offices. In this fiduciary capacity, the BIA performs a variety of functions related to Indian trust transactions. Specifically, weaknesses in the areas of segregation of duties, related party transactions, probate backlog, appraisal compacts, and the timeliness of depositing cash receipts were noted.

#### ***Recommendation***

We recognize that while program and administrative authority necessary to carry out the responsibilities of the OST was delegated to the Special Trustee and that OTFM was transferred intact from the BIA to the OST in February 1996 under Secretarial Order 3197, particular trust functions are performed by non-OTFM staff (i.e., BIA and tribal) over which the OTFM has no management control nor line authority. However, we recommend management work collaboratively with the OST Office of Trust Risk Management to monitor progress towards completion of the various Indian trust reform subprojects being addressed by the BIA to help to ensure the OTFM fulfills its fiduciary responsibility to the trust fund beneficiaries.

#### ***Management's Response***

OTFM recognizes and acknowledges that, as reported, its ability to process (i.e., account for) trust funds receipts and disbursements for trust beneficiaries is significantly dependent and critically reliant upon the financial information derived from trust records that are maintained and provided by BIA and other Department offices. OTFM also shares in the concerns regarding the integrity of trust data it receives from BIA and understands the reportable conditions being reported as material weaknesses in the independent auditors' report on internal control over financial reporting of the BIA. Accordingly, OTFM commits to strive to work collaboratively with Departmental offices to monitor progress towards the completion of the various Indian trust reform subprojects.

### **B. Financial Reporting – Unresolved Matters From Prior Periods**

#### ***Condition***

As of September 30, 2001, several significant financial reporting differences have not been resolved. The presence of these unresolved differences has a material effect on the financial statements of the Trust Funds as of September 30, 2001 and for the year then ended. These matters include the following:

#### ***Cash – Tribal and IIM***

Total cash balances converted from prior general ledgers to the current Trust Funds Accounting System (TFAS) were materially greater than the total balances as reported by the U.S. Treasury (Treasury). The composition of the difference is not known and no reliance has been obtained that either the OTFM balances or the balances as reported by the Treasury is correct. As a result, the unreconciled difference continues to be reflected as a reconciling item in periodic cash reconciliations of activity between TFAS and Treasury. The out of balance condition, which changes as reconciling items are identified and cleared, is approximately \$33 million as of September 30, 2001.

*Investments – Lack of Reliable IIM Balance Available for Investing – IIM*

The TFAS control account for IIM account holders is purported to represent the aggregate net balance of trust funds held on behalf of IIM account holders as reflected in the detailed subsidiary accounts also in TFAS. The balance per the control account does not agree to the sum of the balances per the IIM subsidiary accounts and it cannot be determined which balance, if either, is correct. Consequently, the balance of funds invested for IIM account holders may not be correct. The amount invested for IIM is based on the IIM control account balance in TFAS. As of September 30, 2001, the aggregate sum of all positive balances included in the detailed subsidiary ledger of IIM accounts exceeded the control account by approximately \$6,700,000. Accordingly, IIM account holders with positive balances are being penalized by lower interest earnings. In addition, the IIM detailed subsidiary ledger accounts contain negative account balances totaling approximately \$44,000,000 as of September 30, 2001.

*Trust Fund Balances – Tribal and IIM*

A historical "Undistributed Interest Account" of approximately \$1,800,000 existed at September 30, 1995. The balance as of September 30, 2001 is approximately \$1,680,000.

*Cash – Tribal*

There were thirteen historical cash accounts on the previous trust funds accounting system prior to the conversion to TFAS with negative balances totaling approximately \$742,000. As of September 30, 2001, there are 12 TFAS accounts with balances totaling approximately \$724,000.

*Cash – Failure to Analyze Suspense Accounts – Tribal and IIM*

An analysis of the many historical items that comprise several Treasury suspense and budget clearing accounts has not been completed. The OTFM's current procedures for researching and proposing adjustments to the cash out of balance condition may not consider whether an offset may already exist within one of these account balances. Funds to cover an adjustment may be in a Treasury suspense or budget clearing account because the original transaction may not have been reported to Treasury, and a Statement of Difference was created. If the Statement of Difference was not resolved, the transaction amount was transferred to one of the Treasury suspense or budget clearing accounts. The Treasury suspense and budget clearing account balances at September 30, 2001 were approximately (\$3,378,000), \$5,957,000, and (\$3,310,000).

*Special Deposit Accounts – Inconsistent Practices – IIM*

As of September 30, 2001, there were approximately 20,000 special deposit accounts reflected in the detailed subsidiary ledger accounts in TFAS (IIM accounts) with a balance totaling approximately \$67 million. Per 25 CFR, special deposit accounts are to be used as suspense accounts for which funds are posted when the allocation of the funds is not immediately known upon receipt. The funds are to reside in the suspense accounts temporarily until the proper recipient is identified at which time the funds are to be transferred to the proper account. A significant number of special deposit accounts have remained inactive for the past several years and new accounts continued to be established during the year ended September 30, 2001. During fiscal 2001, we understand management of the OTFM, together with the BIA and a contractor, developed a formal plan to address special deposit accounts. Additionally, a pilot program to identify the source of funds for certain special deposit

accounts was implemented during fiscal 2001. However, a significant number of inactive special deposit accounts continue to require resolution at September 30, 2001.

***Recommendation***

We recommend that management of the OTFM continue to work with appropriate officials within the Department of the Interior to resolve these matters as soon as practicable.

***Management's Response***

OTFM concurs. OTFM recognizes and acknowledges the presence of the noted unresolved differences, as reported. Accordingly, OTFM i) has prepared issue papers, ii) developed and proposed action plans, and iii) submitted the items to designated Departmental personnel. Also, OTFM understands that i) interdepartmental discussions regarding these conditions continue and ii) draft legislation intended to resolve the \$6.7 million difference is circulating for comment.

We noted the following reportable condition, that is not considered to be a material weakness:

**C. Improve Controls Over Information Technology Systems**

***Condition***

Sufficient internal control over information technology (IT) systems and applications is necessary to ensure OTFM fulfills its fiduciary responsibility to trust beneficiaries and that OTFM accomplishes its mission. During our audit, we noted certain matters related to internal control over IT that could be improved which are indicated below.

***IT Policies and Procedures***

Proper documentation for system and application administration is important for the maintenance and operability of the OTFM systems and applications. If system or application malfunction or failures occur, it is imperative that proper and current procedures be in place to administer the system. The OTFM does not have formal policies and procedures related to information technology. Specifically, individual job functions and responsibilities are not formally documented in a procedure format and the system development life cycle for in-house developed systems and applications is not formalized. While operators are often proficient in their duties it is still important that documentation be in place should the system require maintenance when they are not available. Without specific, written instructions for the performance of work in the Division of Trust Fund Systems, OTFM personnel may not be performing their duties correctly or at all if back up personnel are unavailable.

***Security Programs***

Security programs, including security policies and a related implementation plan, for general support systems and major applications are the foundation of an entity's security control structure and a reflection of senior management's commitment to addressing security risks. As outlined in OMB Circular A-130, an effective security program includes a risk assessment process, a certification process, and an effective incident response and monitoring capability. OTFM has not developed and put into place a security program and a security policy which provides a high-level strategy for establishing a sound security framework.

***Segregation of Duties***

OTFM has not ensured proper segregation of duties for certain applications and/or activities through its policies, procedures, and organizational structure to ensure that any one individual cannot control key aspects of computer-related operations or financial transactions.

### *Accreditations*

OTFM has no formal accreditation process to authorize the operation of applications in a secure environment. Specifically, management has not accredited and certified its general support systems and all major applications used to process, store or transmit sensitive information as required by OMB Circular A-130. By not authorizing and accepting the risks associated with these systems to process information, management has not established a key quality control component.

### *Access Controls*

Access controls should provide reasonable assurance that computer resources (data files, application programs, and computer-related facilities and equipment) are protected against unauthorized modification, disclosure, loss, or impairment. The objectives of limiting access are to ensure that (1) users have only the access needed to perform their duties; (2) access to very sensitive resources, such as security software programs, is limited to very few individuals; and (3) employees are restricted from performing incompatible functions or functions beyond their responsibilities. Technical and procedural access controls over OTFM's network have not been configured and/or developed to minimize the risk of unauthorized access.

### *Application Software Development and Change Controls*

Establishing controls over the modification of application software programs help to ensure that only authorized programs and authorized modifications are implemented. Without proper controls, there is a risk that security features could be inadvertently or deliberately omitted or "turned-off," or that processing irregularities could be introduced. OTFM has not formalized the system development life cycle for in-house developed and systems and applications. Additionally, there is no formal change control process for systems and application software developed and maintained by OTFM that would prevent unauthorized programs or modifications to an existing program from being implemented.

### *Service Continuity*

Losing the capability to process, retrieve, and protect information maintained electronically could significantly impact OTFM's ability to accomplish its mission. OTFM's continuity of operations plan does not include comprehensive disaster recovery procedures related to OTFM's IT operations and OTFM has not sufficiently tested the plan to ensure that when unexpected events occur, critical operations continue without interruption or are promptly resumed and critical and sensitive data are protected.

### *Network Security*

The OTFM has not implemented measures to minimize security risks on the network. Network security configuration settings are not sufficiently robust and appropriate mechanisms have not been implemented to prevent and monitor unauthorized access to the network.

### **Recommendation**

We recommend that the OTFM develop an operations manual to cover the daily procedures carried out by the Division of Trust Fund Systems. Formalized policies and procedures should also be developed and incorporated into a comprehensive application security plan to be implemented by the OTFM to fully comply with the requirements of OMB Circular A-130. These policies and procedures should incorporate a formalized system development life cycle for in-house developed

systems and applications. In addition, OTFM should establish and implement policies and procedures necessary to properly accredit and certify all systems used to process, store, or transmit classified or sensitive information. Policies should include an accreditation process to take place every three years. We also recommend OTFM develop and document change control procedures for all the OTFM proprietary applications. The OTFM should also develop detailed disaster recovery procedures for mission critical applications to be incorporated into the existing continuity of operations plan, and the existing plan should be periodically tested and employees trained on its use. The OTFM should also take the steps necessary to improve network security.

#### ***Management's Response***

OTFM recognizes and acknowledges the concerns reported, for improving internal control over information technology (IT) systems. Accordingly, OTFM will i) contract for the development of appropriate IT policies and procedures, ii) implement review procedures for appropriate access controls, and iii) update its Continuity of Operations Plan.

A summary of the status of prior year reportable conditions is included as Exhibit I. We also noted other matters involving internal control over financial reporting and its operation that we have reported to OTFM management in a separate letter dated January 4, 2002.

#### **COMPLIANCE WITH LAWS AND REGULATIONS**

The results of our tests of compliance with the laws and regulations described in the Responsibilities section of this report disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02.

We also noted other matters involving compliance with laws and regulations that, under *Government Auditing Standards* and OMB Bulletin No. 01-02, were not required to be included in this report, that we have reported to OTFM management in a separate letter dated January 4, 2002.

#### **RESPONSIBILITIES**

##### ***Management's Responsibility***

The American Indian Trust Fund Management Reform Act of 1994 (the Reform Act) requires that the Secretary shall cause to be conducted an annual audit on a fiscal year basis of all funds held in trust by the United States for the benefit of an Indian tribe or an individual Indian which are deposited or invested pursuant to the Act of June 24, 1938 (25 U.S.C. 12a). To meet the Reform Act reporting requirements, the OTFM prepares annual Trust Fund financial statements.

Management is responsible for:

- Preparing the financial statements in conformity with accounting principles generally accepted in the United States of America;
- Establishing and maintaining internal controls over financial reporting; and
- Complying with laws and regulations.

In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies.

##### ***Auditors' Responsibility***

Our responsibility is to express an opinion on the fiscal year 2001 financial statements of the Trust Funds managed by the OTFM based on our audit. Except as discussed in the fourth paragraph of our auditors'

reports, we conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Bulletin No. 01-02. Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall financial statement presentation.

We believe that our audit provides a reasonable basis for our opinion.

In planning and performing our fiscal year 2001 audit, we considered the OTFM's internal control over financial reporting by obtaining an understanding of the OTFM's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 01-02 and *Government Auditing Standards*. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982. The objective of our audit was not to provide assurance on internal controls over financial reporting. Consequently, we do not provide an opinion on internal control over financial reporting.

As part of obtaining reasonable assurance about whether the Trust Funds fiscal year 2001 financial statements are free of material misstatement, we performed tests of the OTFM's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 01-02. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws and regulations applicable to the OTFM. Providing an opinion on compliance with laws and regulations was not an objective of our audit, and, accordingly, we do not express such an opinion.

#### **Distribution**

This report is intended for the information and use of the Department of the Interior's management, Department of the Interior's Office of the Inspector General, OMB and the U.S. Congress, and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

January 4, 2002

**U.S. DEPARTMENT OF THE INTERIOR  
OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS  
TRIBAL AND OTHER TRUST FUNDS AND INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE OFFICE OF TRUST FUNDS MANAGEMENT**

Summary of the Status of Prior Year Reportable Conditions

September 30, 2001

Ref	Condition	Status
OTFM-2000-45	Reliance on BIA Ownership Files	Incorporated into reportable condition A (material weakness)
OTFM-1998-42	Trust Systems	Incorporated into reportable condition A (material weakness)
OTFM-1997-32	Missing and/or Incomplete Documents – Tribal and IIM	Not incorporated in report
OTFM-1997-33	Improper Transaction Coding – Tribal and IIM	Not incorporated in report
OTFM-1996-20	Cash – Failure to Analyze Suspense Accounts – Tribal and IIM	Incorporated into reportable condition B (material weakness)
OTFM-1996-22	Investments – Lack of Reliable IIM Balance Available for Investing – IIM	Incorporated into reportable condition B (material weakness)
OTFM-1996-24	Special Deposit Accounts – Lack of Policies and Procedures and Inconsistent Practices – IIM	Incorporated into reportable condition B (material weakness)
OTFM-1996-26	Negative IIM Account Balances Included in Invested Balances - IIM	Incorporated into reportable condition B (material weakness)
OTFM-1995-1	Cash – Tribal and IIM	Incorporated into reportable condition B (material weakness)
OTFM-1995-3	Trust Fund Balances – Tribal and IIM	Incorporated into reportable condition B (material weakness)
OTFM-1995-5	Cash – Tribal	Incorporated into reportable condition B (material weakness)
OTFM-1995-10	Accounts Receivable System at BIA – Tribal and IIM	Incorporated into reportable condition A (material weakness)



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## Mission Statement

The Office of Inspector General conducts and supervises audits and investigations of Department of the Interior and insular area government programs and operations to:

- Promote the economy, efficiency, and effectiveness of programs and operations and
- Prevent and detect fraud, waste, and abuse in programs and operations.

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