



DEPARTMENT  
OF THE  
INTERIOR

The Office of  
Financial  
Management

# Revised Contingent Liability Reporting Guidance

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# CONTINGENT LIABILITY REPORTING GUIDANCE

## Introduction

The Department of the Interior (the Department) and its bureaus and offices (bureaus) are party to litigation, claims, and assessments of which the outcome is uncertain related to the Federal Tort Claims Act, contract disputes, tribal and Indian trust-related matters, personnel and employment-related matters, and various land and resources related claims and adjudications. These matters may involve possible loss resulting in contingent legal liabilities to the Department. This document provides bureaus information and guidance on reviewing and reporting contingent legal liabilities.

The Department's Office of Financial Management (PFM) under the Assistant Secretary – Policy, Management and Budget coordinates the preparation of the Department's financial statements and is liaison between the bureaus, the Office of the Solicitor (SOL), and the financial statement auditors (auditors) for purposes of contingent liability reporting.

## The Evaluation of Legal Contingencies

Generally, attorneys assist the financial management community by applying professional judgment about the outcome of litigation, claims, and assessments that may have a discernible impact on the financial statements. One of the authorities that govern the attorneys' role in the audit process is the Statement of Federal Financial Accounting Standard (SFFAS) Number 5, *Accounting for Liabilities of the Federal Government*. The SFFAS Number 5, as amended, defines a contingency as an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss to an entity. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. It requires Federal agencies to recognize a liability for loss contingencies when: 1) a past event or exchange transaction has occurred; 2) a future outflow or other sacrifice of resources is probable; and 3) the future outflow or sacrifice of resources is measurable.

The SFFAS Number 5, as amended, also defines the likelihood of loss as follows:

- Probable - The future confirming event or events are likely to occur.
- Reasonably Possible - The chance of the future confirming event or events occurring is more than remote but less than probable.
- Remote - The chance of the future event or events occurring is slight.

## The Department's Legal Contingencies

Depending on the circumstances, monetary awards may be paid from agency appropriations, legislation specific to the award, or by the U.S. Department of the Treasury's (Treasury) Judgment Fund. Monetary awards that are significant to the financial statements are usually paid by the Judgment Fund subject to the provisions in its statutory authority. Federal agencies are not required to reimburse the Judgment Fund except for claims arising under the following statutes:

- Contract Disputes Act (CDA); and
- Statutes identified in the No FEAR Act (Notification and Federal Employee Antidiscrimination and Retaliation Act) and its implementing regulations.

## Contingent Liability System

The SOL uses the Contingent Liability System (CLS) to track the legal matters that support the contingent legal liabilities reported in the financial statements. The CLS data is stored in a Structured Query Language database managed by SOL. Attorneys report into CLS through a web interface, and PFM runs reports using a Microsoft Access reporting tool. When a case is entered in CLS, the system assigns a chronological reference number for tracking. Bureaus should cite this four-digit reference number when contacting PFM or SOL.

The Office of the Solicitor's *General Policy and Guidelines for Providing Information to Auditors Relating to Contingent Liabilities* requires attorneys, attorney supervisors, and Associate and Regional Solicitors to ensure the accuracy of all entries in the CLS while preserving attorney-client and attorney work-product privileges. See Appendix I for the SOL policy. Attorneys update matters in accordance with the American Bar Association (ABA) *Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information* ("ABA Statement"), the instructions provided by the CLS manager and the dates on the CLS Schedule. See the CLS Schedule section below for more details.

Access to matters in the CLS in the SOL is segregated by divisions at headquarters and regional and field locations. Only attorneys specifically assigned to a matter or assigned to the same organizational unit as the matter may modify it. Associate and Regional Solicitors who oversee more than one branch or field unit have access to review and modify all matters within their purview.

## CLS Entry Thresholds

Due to the large volume of cases in which the Department or the bureaus are involved, it is not cost-effective to report all cases where the aggregate potential loss of cases with low loss estimates is immaterial to the Department. Therefore, only matters with a potential loss of \$300,000 or more are entered in the system. Note that this CLS entry threshold differs from the reporting thresholds discussed below and is reduced to \$50,000 when a matter relates to the Office of Special Trustee (OST). Active matters not meeting the CLS entry threshold are captured once each year through a data call by the SOL and included in the below-threshold analysis. Entry threshold changes will be posted on the CLS and communicated to attorneys.

## CLS Reporting Thresholds

Reporting thresholds have been built into the CLS reporting tool to reduce the reporting burden. The thresholds apply to the attorneys' upper loss estimate or the claimed amount when no estimate is determined. If a case falls below the reporting threshold, it is excluded from the reports that PFM distributes to the bureaus. The case is now included in the below-threshold

analysis and remains there until the case is closed or until a subsequent change brings it back to the reporting threshold. See the Below-Threshold Analysis section for further information.

The current reporting thresholds are \$50,000 for OST related matters and \$1,000,000 for all other bureaus. Reporting threshold changes will be incorporated into CLS and communicated to the bureaus and to the auditors.

## CLS Schedule

The CLS Schedule delineates the due dates for quarterly reporting, below-threshold analysis, legal representation letters, and management schedule submissions, along with the associated deadlines for attorney updates and the subsequent supervisory review in CLS. The dates are determined by the CLS manager in conjunction with PFM at the beginning of the fiscal year (FY) based on the Office of Management and Budget (OMB) Circular A-136 and the financial reporting due dates. The appropriate due dates are incorporated into the PFM Milestone List. See Appendix II for a sample CLS Schedule. The current schedule for each reporting period is maintained on the CLS and provided to the bureaus.

## CLS Reports

The PFM runs reports from CLS according to the CLS Schedule and provides them to the bureaus for review. Matter summaries consist of PDF reports that follow the Department of Justice (DOJ) specified templates. The "summary" Excel data extract is formatted to create a Management Schedule, and the "detail" Excel data extract gives additional details not included in the DOJ templates (e.g., when certifications took place). Appendix III provides the filenames and descriptions of the reports. The reports with the "changed" designation include only changes from the last report date to the current reporting date. Reports without the "changed" designation are reports covering the current and prior financial reporting periods as of the current reporting date. The reporting threshold governs which cases are contained in the reports.

## Review of CLS Data

Bureaus rely on the attorneys' assessments of likelihood, estimate of loss, and the expected source of funds in CLS for reporting contingent liabilities. Bureaus also rely on attorneys updating matters timely and giving sufficient detail to support their determinations while maintaining attorney client privilege. Updates should reflect the most current case developments that have a bearing on a matter's evaluation. Bureaus should review the individual case details for consistency between the supporting narratives and the likelihood of loss and estimated loss.

Per the ABA Statement, attorneys are responsible for stating whether the outcome is "Probable" or "Remote," and to refrain from expressly opining that an unfavorable outcome is "Reasonably Possible." Therefore, SOL does not assert to the likelihood of loss of "Reasonably Possible." Instead, the likelihood of "**not Probable or Remote**" is used in CLS for cases with neither probable nor remote loss determinations. Departmental and bureau management make the final determination regarding how matters are reported and disclosed in the financial statements;

however, management should use the likelihood of "Reasonably Possible" when the attorney's evaluation of likelihood is neither probable nor remote.

The following are various statuses of the cases with their corresponding designations under "Type of Matter" in the CLS reports:

- Unasserted claims – UCA;
- Pending Administrative claims – PTA;
- Pending Judicial litigation – PTJ; and
- Closed – CLS (not to be confused with Contingent Liability System).

For purposes of contingent liability reporting, an Unasserted claim is one where there has been no manifestation by a potential claimant of an awareness of and present intention to assert a possible claim or assessment. When a potential claimant has manifested to the client bureau an awareness of and present intention to assert a possible claim or assessment, the matter is no longer unasserted even if the claim is baseless, is not properly filed, has little to no supporting documentation, or the statute of limitations continues to run.

Unasserted matters are only entered into CLS when it is probable that a claim will be asserted, it is at least reasonably possible that the outcome will be unfavorable, and that the resulting liability will meet the CLS reporting threshold. Therefore, an unasserted matter may not have a likelihood of "Remote" in CLS. An unasserted matter reported in CLS should be closed if the likelihood of loss drops to "Remote."

If a matter is in a court forum that may not award monetary damages meeting the CLS entry threshold, but it is apparent that the claimant ultimately seeks monetary damages, the matter may be entered in CLS as an unasserted matter based on meeting the other criteria above. Unasserted matters reported in the CLS that have estimated losses should be presented in the financial statements and the note disclosures in the same manner as other pending cases.

Both Pending Administrative claims and Pending Judicial litigation begin with some form of complaint, and both types of proceedings require an answer, or other response, to a complaint. Administrative matters are those taking place before federal (or state) governing bodies (e.g., the Equal Employment Opportunity Commission, U.S. Civilian Board of Contract Appeals). Judicial proceedings are those actions that take place in court, such as a breach of contract suit or other civil actions. These matters are recorded in the financial statements and note disclosures as described in the Recording Contingent Liabilities in the Financial Statements section below.

For relatively new cases, it is not unusual to have a "Probable" likelihood of loss and a zero loss estimate because there may be insufficient information to estimate the amount of loss. However, older matters should have a clearer explanation of factors inhibiting the attorney from providing an estimate when the likelihood remains "Probable."

In reviewing the CLS data, the fact that settlement negotiations are underway may provide the attorneys a reasonable basis upon which to estimate the likelihood of loss. The existence of such negotiations, in and of themselves, does not automatically render the likelihood of loss more

certain. In other words, an offer to settle does not mean that the likelihood of loss should be "Probable." Other factors, such as how likely it is the claimant of the government will accept the settlement terms, needs consideration.

Pending (active) matters that have attained a fully signed settlement agreement or where the court entered the settlement as an order are marked as "Settlement Payment Triggered" in the CLS. These matters will reflect the agreement amount (or range of loss) as the probable loss in CLS reports; however, the settlement amounts are no longer considered contingent and all associated contingent liability balances should be removed from the financial statements and note disclosures. In addition to reducing the related contingent liability, additional accounting entries may be required to record the appropriate cost and/or potential liability associated with a loss settlement. See Appendix VIII – Accounting Treatment for guidance. Payment from the Judgment Fund or appropriations may still be pending at this point.

Matters for which a settlement has been reached are not considered "Closed" in CLS until other required qualifications occur. Though not common, complex matters may involve partial settlements, or multiple plaintiffs who are not party to a settlement. It is important that bureaus read matter summary details to understand if a contingent liability still exists.

Pending matters are "Closed" in the CLS when: 1) conclusively resolved or the time for any appeal has passed; 2) it no longer meets the CLS entry threshold (and will not in the future); 3) it is determined that the matter should be consolidated with another matter in CLS; or 4) it is determined that the matter is a duplicate of another matter in CLS. Attorneys usually do not close a case in CLS until conclusively resolved (i.e., administrative denial letters are sent, settlement agreements are final, final decisions are issued, and court cases are dismissed) and any time for appeal has expired. Official documentation such as a court dismissal is provided to the bureaus and to the auditors for each matter. For closed matters and open matters with fully signed settlement agreements, PFM works with the SOL to provide documentation to the bureaus by the 5<sup>th</sup> business day after PFM provides the CLS reports so the bureaus have adequate support to reduce all related contingent liabilities. Judgment Fund payments may still be pending at this point.

The CLS does not stamp a date of attorney review in the matter summaries when the attorneys merely review the cases in the CLS without making updates. To determine whether the cases have been updated or reviewed, bureaus can refer to the "ChangedAt" column in the "detail" Excel file. Matters are not required to be validated by management in CLS; therefore, bureaus can obtain assurance of management review by using a combination of the "ValidAt" column in the "detail" Excel file and the signed certification by SOL managers confirming that the matters within their Division or Region are current. These high level management certifications are collected before updates are released and Legal Representation Letters are signed.

After reviewing the CLS reports, bureaus should submit questions to PFM using the standard template and information available in the "detail" Excel file. See Appendix IV for a sample template. The PFM works with SOL for timely responses. Follow-up questions may be submitted to PFM if the original responses are not satisfactory to the bureaus. In addition, bureaus should consider SOL responses when reporting the contingent liabilities in the financial

statements. If the bureaus and the attorneys agree that the liabilities should differ from the CLS reports, bureaus should ensure that changes are reflected in the financial statements as well as the Management Schedule. The PFM will work with SOL regarding any updated CLS reports needed to support the liabilities reported in the financial statements. If an agreement cannot be reached between the bureau and SOL, bureau management may present the legal liability according to its judgment and document the basis for the discrepancy between the liability recognized and the CLS reports (e.g., Judgment Fund activity, liability best reported as an Environmental and Disposal Liability).

## **Reporting Contingent Liabilities in the Financial Statements**

Bureaus will report and disclose contingent liabilities in the financial statements. For pending and unasserted matters with a “Probable” likelihood of loss, a contingent liability should be recognized and the range of loss should be disclosed in the note to the financial statements. As discussed in the Reducing Contingent Liabilities section below, if an open matter is marked as “Settlement Payment Triggered,” the related contingent liability should be removed and reclassified as necessary. See Appendix VIII – Accounting Treatment for guidance. If the estimate of loss is a range, the lower range of loss should be recognized as a contingent liability unless another amount within the range is more appropriate. If the likelihood of loss is greater than “Remote,” bureaus should disclose the loss estimate or the range of loss estimate in the note to the financial statements. For cases with the likelihood of loss of “Remote,” no contingent liability is recognized or disclosed.

## **Reducing Contingent Liabilities**

In accordance with the Federal Accounting Standards Advisory Board Interpretation No. 2: *Accounting for Treasury Judgment Fund Transactions, an Interpretation of SFFAS 4 and 5*, the CLS includes a “Settlement Payment Triggered” field to identify when settlement agreements have been fully signed or where the court entered the settlement as an order. These events will drive the reduction of the contingent liability and proper reclassification on the financial statements and footnote disclosures. See Appendix VIII – Accounting Treatment for guidance on the associated accounting treatment.

The contingent liability amount should be reduced for matters marked as “Settlement Payment Triggered” or “Closed.” In the event that an approved payment is identified on the Judgment Fund quarterly report where the contingent liability has not been removed due to the matter in the CLS not being marked as “Settlement Payment Triggered,” the related contingent liability should be removed.

Information provided in the CLS will provide guidance to the bureaus on who the expected source of funding is for the potential loss. Each matters will designate the Source of Funding as either Judgment Fund, Appropriation, or Unknown. If there is more than one source of funds for a particular matter, the source contributing the largest share will be listed, and an explanation of the split will be provided in the narratives. For Judgment Fund and Unknown matters, unless otherwise noted in the claim details that it relates to a CDA, these cases should be considered paid by the Judgment Fund, non-reimbursable for accounting purposes. If the detail identifies

the claim as a CDA, these should be considered paid by the Judgment Fund, reimbursable. The Appropriation designation implies that any loss would be expected to be paid directly by THE DEPARTMENT out of an available appropriation.

For fully signed settlements and closed matters where the Judgment Fund is expected to be the source of payment and it is expected to be non-reimbursable, bureaus should reverse the contingent liabilities and the related expense previously recognized and record an imputed cost and an imputed financing source using trading partner “020” for Treasury. For fully signed settlements and closed matters where the Judgment Fund is expected to be the source of payment and they are reimbursable to Treasury (e.g. CDA), bureaus should set up an expense and payable with trading partner “020” for Treasury until reimbursement is made. For fully signed settlements and closed matters expected to be funded by an available appropriation, the contingent liability should be reversed and an obligation and disbursement should be made accordingly. See Appendix VIII – Accounting Treatment for details. No-FEAR Act claims are normally below threshold and are reimbursed immediately by the Office of Budget (POB). POB then seeks reimbursement from the appropriate bureaus through reimbursable agreements.

Reductions to contingent liabilities are also required for cases that drop off of the current CLS listing due to changes in estimated losses that are below the \$1 million reporting threshold (\$50,000 for OST related).

### **Quarterly Judgment Fund Payment Reports**

When the cases are settled for monetary damages or judgment has been ordered and the Judgment Fund is determined to be the source of funding, DOJ attorneys or the Department’s attorneys will either submit requests for the payments via the Treasury’s Bureau of the Fiscal Service (Fiscal Service) Judgment Fund Internet Claim System (JFICS) or directly to the Fiscal Service Judgment Fund Branch, which administers the Judgment Fund. Reports on the Judgment Fund payments are available in JFICS by “Payment Submitted Date” or by “Payment Sent Date.” Both types of reports include only payments that have been approved for disbursement. The Judgment Fund Branch accrues a liability for requested payments that have not yet been disbursed and a matching receivable for reimbursable activity. For this reason, PFM will generate the reports from JFICS based on the “Submitted Date” to assist in the quarterly reconciliation with Treasury.

The PFM generates the Judgment Fund Agency Payment Report from JFICS quarterly and distributes to the bureaus for reporting. Many of the payments on the report may list “Department of the Interior” as the responsible agency but the liabilities are reported by the individual bureaus and not the Departmental Offices. For significant payments, PFM will research further to identify the appropriate reporting entity within the Department and if any additional agencies share responsibility of the settlement. If additional agencies are identified, bureaus should only recognize the Department’s portion of the loss.

Bureaus should review individual payments to ensure proper accounting. For non-reimbursable Judgment Fund payments related to “Settlement Payment Triggered” or “Closed” cases where the contingent liability has been removed and an imputed cost recorded, no further action is

necessary. For reimbursable Judgment Fund payments, with the exception of No FEAR Act claims, bureaus should confirm that either a payment has been made or a liability is reported with Treasury until reimbursement is made. The No FEAR Act reimbursable claims are normally below threshold and are reimbursed immediately by the Office of Budget (POB). In the event that payment requests have been submitted to the Judgment Fund per the JFICS Agency Payment Report, and there is no imputed cost or liability due to Treasury already recorded per information provided in the CLS reports additional research may be required to confirm the payment belongs to the Department. Due to the below threshold reporting thresholds in the CLS, bureaus may often see payments for less than \$300,000 which have not previously been recorded.

Most Judgment Fund payments are non-reimbursable. However, payments made under certain laws and statutes are reimbursable to the Judgment Fund. Currently, Judgment Fund payments pursuant to the CDA and No FEAR Act are required to be reimbursed.

For Judgment Fund payments made under the No FEAR Act, the Judgment Fund Branch sends the reimbursement notices to POB, and POB reimburses the Judgment Fund on behalf of all bureaus centrally to comply with the Office of Personnel Management and other regulations and to meet the 45-day Treasury requirement for No FEAR Act reimbursements. The POB then seeks reimbursement from the appropriate bureaus through reimbursable agreements. Refer to PFM's Financial Management Memorandum 2010-006, *No FEAR Act Settlement and Award Payments*, for more information.

For Judgment Fund payments pursuant to CDA, the Judgment Fund Branch sends the reimbursement notices with the payment details to PFM. In turn, PFM forwards them to the relevant bureaus. The bureaus have 45 business days to reimburse the Judgment Fund or contact the Judgment Fund Branch to make written arrangements for reimbursement. Quarterly, PFM will confirm that the receivable balances recorded by Treasury's Judgment Fund Branch reconcile with the Department's Judgment Fund payable balances in order to minimize intra-governmental differences.

For further information on the Judgment Fund, see Treasury Financial Manual Volume 1, Part 6, Chapter 3100 at: <http://tfm.fiscal.treasury.gov/v1/p6/c310.html>.

### **Below-Threshold Analysis**

The SOL will perform the below-threshold analysis in conjunction with the first Legal Representation Letter with an update at the end of the fourth quarter to assess the impact on financial reporting. There are two types of cases included in the below-threshold analysis: 1) cases with the four digit reference number that meet the CLS entry threshold (currently \$300,000 and \$50,000 for OST) but are below the reporting threshold (currently \$1,000,000), and 2) cases below the CLS entry threshold. Matters with potential monetary damages not reported in CLS have the "below" designation in the report instead of the four-digit reference numbers. The SOL compiles both sets of data for the below-threshold analysis.

There are two parts to the analysis: the worst-case scenario and the unreported liability. The worst-case analysis takes into account the claimed amount in absence of a loss estimate. The estimated amount in the worst-case analysis will be included in the Legal Representation Letter itself, and the unreported liability will be disclosed in the Department's non-Generally Accepted Accounting Principles (GAAP) analysis. Currently, PFM reports the contingent liabilities that are considered non-GAAP at the consolidated level.

The PFM will analyze the materiality of the unreported contingent liability to assess the impact on the financial statements to determine if the thresholds need to be revised.

### **Legal Representation Letters and the Related Management Schedules**

The SOL prepares the Legal Representation Letter (Legal Letter) in accordance with guidance provided in OMB Circular A-136. The Legal Letter process begins with a request for the Legal Letter from the Assistant Secretary for Policy, Management and Budget to the Solicitor concerning litigation, claims and assessments, with due dates of the Legal Letter responses specified in accordance with the reporting requirements set forth in OMB Circular A-136. See Appendix V for a sample Request for Legal Representation Letters.

The response to the request for the Legal Letter is a memorandum signed by the Solicitor or designated official to the Inspector General and external financial audit partner. The Legal Letter transmits in attachments updated information on the Department's potential financial liabilities related to legal contingencies. The attachments to the Legal Letter are the CLS reports that PFM provides to the bureaus. See Appendix VI for a sample Legal Letter.

The OMB Circular A-136 currently requires an interim and a final Legal Letter that includes updates only. The Department, however, prepares an initial (interim) Legal Letter and two updates, one at the end of the FY and a final update within twenty days of the issuance of the Agency Financial Report (AFR) to better assist bureaus in reporting their legal contingent liabilities.

The OMB prescribed Management Schedule shows how the information contained in the Legal Letter was considered in preparing the financial statements. The schedule should be consistent with the most current information presented in the Legal Letter (and updates) and the financial statements. Any discrepancies such as changes resulting from the discussions with the SOL should be explained in the comment column on the Management Schedule. See Appendix VII for a sample Management Schedule.

The following describes the process for preparing the Management Schedule:

- The PFM prepares the Management Schedule using the data from the CLS summary Excel reports. All pending matters are listed in the initial or interim Management Schedule. The update to the Management Schedule includes active open matters with a change in probability or estimate from the prior schedule, or new matters occurring during the reporting period.

- The PFM requests the bureaus to fill in the disposition section of the Management Schedule, considering the probability and estimates provided by SOL, materiality, input from bureau and program/environmental staff, and responses from the attorneys on the bureau questions. For “Probable” cases, the amount recognized in the financial statement should be entered; for “Probable” cases with “Settlement Payment Triggered,” the liability recorded should be \$0 and an explanation provided; for “Reasonably Possible” cases, the note to the financial statement where the range of loss is disclosed should be entered; and for “Remote” cases, no action is required.
- The PFM finalizes the Department’s Management Schedule and transmits it to the external auditors and the Department’s Office of the Inspector General (OIG).

Per OMB Circular A-136, the Legal Letter updates and the related Management Schedules should be limited to significant changes and new information only, i.e., cases that arise subsequent to initial or interim Legal Letter or changes in the status of cases or the likelihood of loss that were reported in the interim letter, and should not repeat the information from the interim letter that has not changed. For this reason, bureaus cannot crosswalk their contingent liabilities reported in the financial statements to the Management Schedule updates. Bureaus will need to consider the cumulative reports to determine their contingent liabilities.

The PFM submits the Legal Letter and the Management Schedule to the external financial auditor and the OIG. The OIG forwards them to DOJ, Treasury’s Fiscal Service, and the Government Accountability Office according to the established due dates in OMB Circular A-136. Subsequent changes after the issuance of the AFR but before the issuance of the Financial Report of the United States Government are provided by PFM to the OIG for submission to Fiscal Service only.

### **CLS Audit Questions**

Bureaus should work with their auditors on inquiries related to contingent legal liabilities. When the bureau audit teams have questions for the SOL, the questions should be submitted to PFM using the standard template. The PFM will coordinate with the SOL in providing responses, and if necessary, coordinate with the SOL in setting up meetings with the auditors, the attorneys, and bureau representatives. The PFM will keep bureaus informed as they coordinate inquiries with the consolidated audit team.

### **Bureau Management Responsibilities**

It is the bureau management’s responsibility to ensure that the contingent liabilities are reported fairly. Bureau management shall ensure 1) the review of the CLS reports, 2) provide approval of the disposition on the Management Schedule, and 3) ensure that liabilities are accurately presented in the financial statements and the note disclosures. Assistance from PFM and the SOL is available, as needed.

## Appendixes

- Appendix I – *General Policy and Guidelines for Providing Information to Auditors Relating to Contingent Liabilities*
- Appendix II – Sample CLS Schedule
- Appendix III – CLS Filename Definitions
- Appendix IV – Standard Template for bureau and auditor questions
- Appendix V – Sample Request for Legal Representation Letters
- Appendix VI – Sample Legal Representation Letter Response
- Appendix VII – Sample Management Schedule
- Appendix VIII – Accounting Treatment

## Appendix I - General Policy and Guidelines for Providing Information to Auditors Relating to Contingent Liabilities



IN REPLY REFER TO:

### United States Department of the Interior

OFFICE OF THE SOLICITOR  
Washington, D.C. 20240

FEB 24 2012

#### Memorandum

To: All Solicitor's Office Attorneys

From: Deputy Solicitor *Arthur E. Gary*

Subject: GENERAL POLICY AND GUIDELINES FOR PROVIDING INFORMATION TO AUDITORS  
RELATING TO CONTINGENT LIABILITIES

#### I. INTRODUCTION:

A. **General:** It is widely recognized that our legal, political, and economic systems depend to an important extent on public confidence in published financial statements of government agencies. Working through the Office of Inspector General (OIG) and the Department's Office of Financial Management under the Assistant Secretary – Policy, Management & Budget, the Department retains the services of an external accounting firm to perform its annual financial audit in accordance with statutes and Executive Branch directives (referred to herein as "auditors"). The general authorities and requirements for the Department's financial management program are found in the Departmental Manual (DM) at 340 DM 1 and 360 DM 1. These DM chapters illustrate that the primary responsibility for decisions relating to the Department's financial audits belongs to the Department.

As with all audited organizations, the Department must adopt policies and procedures to identify, evaluate and account for litigation, claims and assessments as a significant component of its financial position. To this end, the Department necessarily relies on its attorneys in the Office of the Solicitor to provide important information about such matters. The Solicitor's Office meets its obligations by reporting on contingent liabilities – that is, conditions, situations or circumstances (litigation being key among them) that give rise to potential financial gain or loss.

Much as the accounting profession must adopt and adhere to standards and procedures that will command confidence in the auditing process (noted below), it is not necessary to intrude on the confidentiality of the lawyer-client relationship in order to command such confidence. Accordingly, attorneys must fully understand their respective roles and obligations both as to participation in the audit process and in adhering to their ethical responsibilities to their clients.

This Policy explains the role of the Solicitor's Office attorneys in the Department's annual financial audit, including the mandatory use of the Contingent Liability System (CLS) by Solicitor's Office staff. The CLS is the primary means of tracking the information we require to respond to requests for information relating to the Department's financial statements from internal financial management officials, the OIG,

as well as the Department's external auditors. Development of this policy has been coordinated with the Department's financial management officials and OIG, and reflects a consensus as to the role of the government attorney in the Department's audit process.

**B. Auditors' Duties:** Auditors' duties are to the reader of financial audit reports and are generally oriented towards publication. Under Statement of Federal Financial Accounting Standards (SFFAS) No. 5, as amended, the auditors have to determine whether a material loss contingency is required to be accrued or disclosed as part of the agency's financial statement. Accrual of a loss contingency is required if available information indicates that a liability has been incurred and the amount of loss can be reasonably estimated. Such loss is 'probable' under SFFAS No. 5 if it is "likely to occur." Auditors will also classify liabilities as "remote" (the likelihood is "slight") or "reasonably possible," which is more likely than "remote" but less than "probable." Even if the liability is not accrued, it may have to be disclosed by the auditors (usually as a footnote to the financial statement). It must be disclosed if there's a "reasonable possibility" of loss. [Reference: Commentary to ABA Statement, Comment 5.1]

**C. Attorneys' Duties:** The American Bar Association (ABA) has acknowledged the attorney's role in this process, but recognizes that under the professional obligations that guide attorneys, their duty is to the client and is private in nature. Thus, while attorneys have a duty to assist their clients in responding to public audit requirements in a timely manner, there are limitations on the attorney's role that are imposed by rules and canons of professional responsibility. In the private sector, it falls to the client to comply with public auditing requirements, thus at the client's request the attorney communicates to the auditors information the auditors need to form an opinion regarding the client's financial reports. But in so doing, the attorney is still required to preserve attorney-client and attorney work-product privileges. The tension between these competing obligations is real. As a result, the attorney must recognize the divergent roles of attorney and auditor. To guide attorneys through this tension, the ABA issued a Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information ("ABA Statement"). It has been noted in some scholarly professional articles that government attorneys, unlike their private sector counterparts (who, after all, may be dismissed by their clients) may be seen to have additional requirements to serve the public interest, which can put the attorney at odds with the stated interests of its client representatives (government officials). It is not the place of this Policy to address that argument or its counterarguments. Nevertheless, though there may be unquantifiable variations between the obligations of public and private sector attorneys, it remains incumbent upon government attorneys to understand and comply with professional standards to guard their relationship with the client and the limitations this imposes on the attorney's response to requests for audit information. The Office therefore adopted the ABA Statement as the best guide to attorneys' roles in the financial audit process. In following the ABA Statement, attorneys will protect and preserve their professional responsibilities as well as the confidences of the client.

**D. Relative Duties of Attorneys and Clients:** As a general matter, it is the Department's financial position that is being audited, thus it is the Department that has the primary obligation to provide the auditors with information sufficient to make determinations about accrual and disclosure of liabilities with respect to its financial statements. However, it is the ongoing responsibility of the Department's

lawyers to assist their client in this regard. To this end, SOL and appropriate Bureau and Departmental employees work together to develop information sufficient to assist auditors in forming an opinion about the Department's financial statement. The transmission of this information is accomplished through the CLS, along with informal communications between attorneys, financial management staff, and the auditors. This reporting obligation of attorneys in no way lessens the need to protect client privileges in information relating to potential liabilities.

II. Policy:

A. **ABA Policy:** The Office adopts and hereby incorporates by reference the ABA's Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information ("ABA Statement"), including Commentaries, Supplemental Reports, and updates. The initial ABA Statement (without Commentaries or Supplemental Reports) is attached as Appendix A. Attorneys responsible for reporting information in the CLS are expected to read and adhere to the ABA Statement, including relevant Commentaries, Supplemental Reports, updates and associated materials, and this policy.

The following references have been consulted in the development of this Policy, and the Office will look to these references (and others, as appropriate) for resolving questions relating to the role of the Office in supporting the Department's annual financial audit, as well as to address specific questions relating to the reporting of particular claims and cases:

- American Bar Association materials:
  - ABA Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information, including Commentary and Supplemental Reports
  - ABA Section of Business Law; *Audit Responses in the New Environment*, Nov. 19, 2004
- 2003 Florida Bar Journal, Vol. LXXVII, No. 1
- 340 DM 1 *et seq.*, 360 DM 1 *et seq.*
- Statement of Federal Financial Accounting Standards (SFFAS) No. 5 ("Accounting for Liabilities of the Federal Government") and No. 12 ("Recognition of Contingent Liabilities Arising from Litigation", amending SFFAS No. 5), promulgated by the Federal Accounting Standards Advisory Board
- Other References: Chief Financial Officer's Act of 1990; Government Management Reform Act of 1994; Federal Financial Management Improvement Act of 1996.

B. **ABA Statement of Policy:** Attached as Appendix A

III. GENERAL GUIDELINES FOR RESPONDING TO AUDITORS' REQUESTS FOR INFORMATION

A. **Responses to Auditors Generally:** In providing responses to the auditors on behalf of its clients, SOL collectively must make reasonable efforts to determine all matters involving loss contingencies to which SOL attorneys have devoted substantive legal attention. The CLS, and the concomitant obligation of all SOL attorneys to diligently enter and update information in the CLS regarding their cases in accordance with these and other guidelines and instructions, fulfills that duty. The CLS has been developed in

consultation with the Department's Office of Financial Management, the Office of Inspector General, as well as with the auditors.

The description inserted into the CLS interface or other means of transmission of information by attorneys should not be a rambling, stream-of-consciousness dissertation about the claim. Factual assertions and history of the claim/litigation should be only that minimally necessary to describe the claim and provide sufficient context for the assessment of likelihood of an unfavorable outcome and estimated loss. Specific guidelines for entering information into the CLS are provided in the CLS menus, and are considered authoritative. Attorneys should consult the guidelines in the CLS, and raise any questions to their immediate supervisors.

**B. Attorney-Client Confidences To Be Maintained:** Attorneys must preserve confidential information provided by the client as well as privileged attorney work-product. This bedrock principle informs the way by which attorneys will fulfill their obligation to assist their client to provide the auditors with information relating to the audit. The developing case law regarding waiver of privileges by attorneys' statements to auditors generally but increasingly confirms the presence of cognizable risk of waiver when an attorney communicates to auditors confidential information pertaining to their client's legal position. Therefore, confidential information and strategies should not be included in the CLS entry. The background discussion should be reviewed periodically and in accordance with Office-wide directives and edited by both staff attorneys and their managers to assure that it is up to date and contains no more information than is necessary.

**C. Limitations on Estimating Loss Contingencies:** (Reference: Paragraph 5 of ABA Statement; Comment 5.2 to ABA Statement; First Report of the Committee on Audit Inquiry Responses Regarding Initial Implementation of the Statement of Policy)

The tension between the responsibilities of auditors and those of attorneys is most pronounced when the need arises to estimate the likelihood and amount of potential loss contingencies. SFFAS No. 5 limits reporting of liabilities in financial audits to three categories: "remote," "reasonably probable," and "probable." [Lawyers, in contrast, are responsible for stating whether the outcome is "remote", "probable" or "unable to form such a judgment.] ***Note that these definitions differ from those applicable to attorneys, who are governed by the more stringent thresholds in the ABA Statement.*** If the lawyer cannot advise that an unfavorable outcome is "remote" or "probable," he is to state that he is unable to form such a judgment. ***Attorneys should refrain from expressing a judgment as to outcomes of claims and cases except in those relatively few clear cases where it appears to the lawyer that an unfavorable outcome is either "probable" or "remote," as those terms are defined in the ABA Statement.***

According to Comment 5.2, attorneys should estimate the likelihood of an unfavorable outcome as follows:

- ***"Probable"***: An unfavorable outcome is normally "probable" if, but only if, investigation, preparation (including the development of factual data and legal research) and progress of the

matter have reached a stage where a judgment can be made, taking all relevant factors into account which may affect the outcome, *that it is extremely doubtful that the client will prevail.*

- **"Remote":** The prospect for an unfavorable outcome appears, at the time, to be slight; i.e., *it is extremely doubtful that the client will not prevail.* Normally, this would entail the ability to make an unqualified judgment, taking into account all relevant factors which may affect the outcome, that the client may confidently expect to prevail on a motion for summary judgment on all issues to the clarity of the fact and the law.

***Lawyers should refrain from expressly opining that an unfavorable outcome is "reasonably possible."***

The CLS interface no longer includes this category. In such cases, the lawyer should provide a general statement that "the litigation is being defended vigorously and the client has meritorious defenses." The attorney may be able to provide additional information to assist the auditor to make this determination, but when discussing the response with auditors the attorney must avoid giving oral opinions about the likelihood of an unfavorable outcome.

While the fact that settlement negotiations are underway may provide a reliable basis upon which to estimate the likelihood of a liability, the existence of such negotiations, in and of themselves, does not render the likelihood of liability more certain. Attorneys must continue to use sound judgment with respect to the likelihood of settlement.

**D. Estimating Loss Amounts:** Attorneys should estimate the amount (or range) of potential loss only when the unfavorable outcome is not "remote," but then only if the attorney believes that the probability of inaccuracy of the estimate of the range or amount is slight. The same formulation of probability should be used with respect to the determination of estimated loss amounts as should be used with respect to estimating the outcome of the matter. As with estimating the outcome, attorneys might be able to provide the auditor with information concerning loss contingencies through detailed communications (oral or written, such as email), subject, of course to the principles set forth in the ABA Statement and these guidelines.

**E. Providing Information on Unasserted Claims:** Attorneys should provide information on the existence of possible unasserted claims only where:

- Assertion of a claim is probable (more likely than not);
- Assuming a claim is asserted, there is a reasonable possibility the outcome will be unfavorable;  
AND
- The resulting liability will be material to the financial condition of the client or meets DOI reporting thresholds

Attorneys' obligations with respect to unasserted possible claims primarily encompass providing notice as to the existence of possible matters and assisting the agency as necessary to make a determination whether and to what extent it must be disclosed as part of the audit. As with asserted claims and cases, attorneys' have the same obligation to predict the likelihood where it appears to the attorney that an unfavorable outcome is either probable or remote. Likewise, the attorney should predict the amount of the liability only where the probability of inaccuracy of the estimate of the amount or range of potential

loss is slight. See Second Report of the ABA Committee on Audit Inquiry Responses Regarding Initial Implementation (August 1976) for additional guidance on unasserted claims.

### III. VERIFYING CLS INFORMATION

**A. Periodic Review & Certification of CLS Entries:** Because information in CLS flows forward automatically to the OIG, the bureau and Departmental financial management personnel, as well as the auditors, it is especially important that all attorneys and supervisors ensure that the information entered into CLS is accurate and updated. Supervisors and managers are responsible for taking appropriate steps periodically to assure the accuracy of all entries from their organizational unit. Additionally, as the preliminary and final legal representation letters are prepared in the third and fourth quarter of each fiscal year, all attorneys and supervisors will be required to certify in writing that they have complied with all official requests to update their CLS entries, including reviewing and updating their CLS entries, as appropriate.

**B. Coordination with Bureau / Departmental Financial Management Staff & Auditors:** All attorneys and supervisors are expected to cooperate with requests from bureau and Departmental financial management staff and/or auditors to respond to questions relating to information in the CLS. The Division of Administration will coordinate these requests. Supervisors and managers are expected to participate in such calls to assure that the cases and matters are accurately reported and that any changes to CLS entries in response to such communications properly reflect attorneys' responsibilities under the ABA Statement.

### IV. LEGAL REPRESENTATION LETTERS AND UPDATES

The work of the Solicitor's Office in reporting contingent liabilities is formally reflected in the Legal Representation Letters provided to the OIG. The Solicitor's Office also plays a key role in the Management Representation Letter signed by the Secretary as part of the annual financial audit. All legal representation letters, including updates, shall be signed by a senior managing attorney such as the Solicitor, a Deputy Solicitor, or the Associate Solicitor for General Law. Similarly, only these officials may provide final surname review of the Secretary's Management Representation Letter. The official signing the Legal Representation Letter and reviewing the Management Representation Letter necessarily must rely on the information provided by all Solicitor's Office attorneys without being able to independently verify all such information. Compliance with the process established by this Policy assures that the Solicitor's Office can competently perform its important role in the audit process.

### V. CONCLUSION

This policy is effective immediately and shall be incorporated into the Solicitor's Manual as soon as practicable.

## **APPENDIX A: ORIGINAL ABA STATEMENT OF POLICY**

[WITHOUT COMMENTARY OR SUPPLEMENTAL REPORTS]

**NOTE:** IT IS EACH ATTORNEY'S RESPONSIBILITY TO READ AND UNDERSTAND THE COMMENTARY AND SUPPLEMENTAL REPORTS INSOFAR AS IT APPLIES TO THE ATTORNEY'S ROLE AND RESPONSIBILITIES IN THE AUDIT PROCESS.

### AMERICAN BAR ASSOCIATION

Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information<sup>1</sup>

#### **Preamble**

The public interest in protecting the confidentiality of lawyer-client communications is fundamental. The American legal, political and economic systems depend heavily upon voluntary compliance with the law and upon ready access to a respected body of professionals able to interpret and advise on the law. The expanding complexity of our laws and governmental regulations increases the need for prompt, specific and unhampered lawyer-client communication. The benefits of such communication and early consultation underlie the strict statutory and ethical obligations of the lawyer to preserve the confidences and secrets of the client, as well as the long recognized testimonial privilege for lawyer-client communication.

Both the Code of Professional Responsibility and the cases applying the evidentiary privilege recognize that the privilege against disclosure can be knowingly and voluntarily waived by the client. It is equally clear that disclosure to a third party may result in loss of the "confidentiality" essential to maintain the privilege. Disclosure to a third party of the lawyer-client communication on a particular subject may also destroy the privilege as to other communications on that subject. Thus, the mere disclosure by the lawyer to the outside auditor, with due client consent, of the substance of communications between the lawyer and client may significantly impair the client's ability in other contexts to maintain the confidentiality of such communications.

Under the circumstances a policy of audit procedure which requires clients to give consent and authorize lawyers to respond to general inquiries and disclose information to auditors concerning matters which have been communicated in confidence is essentially destructive of free and open communication and early consultation between lawyer and client. The institution of such a policy would inevitably discourage management from discussing potential legal problems with counsel for fear that such discussion might become public and precipitate a loss to or possible liability of the business enterprise and its stockholders that might otherwise never materialize.

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<sup>1</sup> 1 Previously published in *The Business Lawyer*, Vol. 31, No. 3 (April 1976). Editor's note: The Board of Governors of the American Bar Association on December 8, 1975, approved the following ABA Statement of Policy. (The Statement had been approved in principle by the Section Council in Montreal in August 1975 and, as revised, in early December 1975.) A Statement on Auditing Standards, which coordinates with the approach set forth in the revised ABA Statement, was approved on January 7, 1976, by the AICPA Auditing Standards Executive Committee. A copy of the ABA Statement of Policy is hereinafter set forth.

It is also recognized that our legal, political and economic systems depend to an important extent on public confidence in published financial statements. To meet this need the accounting profession must adopt and adhere to standards and procedures that will command confidence in the auditing process. It is not, however, believed necessary or sound public policy to intrude upon the confidentiality of the lawyer-client relationship in order to command such confidence. On the contrary, the objective of fair disclosure in financial statements is more likely to be better served by maintaining the integrity of the confidential relationship between lawyer and client, thereby strengthening corporate management's confidence in counsel and encouraging its readiness to seek advice of counsel and to act in accordance with counsel's advice.

Consistent with the foregoing public policy considerations, it is believed appropriate to distinguish between, on the one hand, litigation which is pending or which a third party has manifested to the client a present intention to commence and, on the other hand, other contingencies of a legal nature or having legal aspects. As regards the former category, unquestionably the lawyer representing the client in a litigation matter may be the best source for a description of the claim or claims asserted, the client's position (e.g. denial, contest, etc.), and the client's possible exposure in the litigation (to the extent the lawyer is in a position to do so). As to the latter category, it is submitted that, for the reasons set forth above, it is not in the public interest for the lawyer to be required to respond to general inquiries from auditors concerning possible claims.

It is recognized that the disclosure requirements for enterprises subject to the reporting requirements of the Federal securities laws are a major concern of managements and counsel, as well as auditors. It is submitted that compliance therewith is best assured when clients are afforded maximum encouragement, by protecting lawyer-client confidentiality, freely to consult counsel. Likewise, lawyers must be keenly conscious of the importance of their clients being completely advised in these matters.

#### **Statement of Policy**

NOW, THEREFORE, BE IT RESOLVED that it is desirable and in the public interest that this Association adopt the following Statement of Policy regarding the appropriate scope of the lawyer's response to the auditor's request, made by the client at the request of the auditor, for information concerning matters referred to the lawyer during the course of his representation of the client:

**(1) Client Consent to Response.** The lawyer may properly respond to the auditor's requests for information concerning loss contingencies (the term and concept established by Statement of Financial Accounting Standards No. 5, promulgated by the Financial Accounting Standards Board in March 1975 and discussed in Paragraph 5.1 of the accompanying Commentary), to the extent hereinafter set forth, subject to the following:

(a) Assuming that the client's initial letter requesting the lawyer to provide information to the auditor is signed by an agent of the client having apparent authority to make such a request, the lawyer may provide to the auditor information requested, without further consent, unless such information discloses a confidence or a secret or requires an evaluation of a claim.

(b) In the normal case, the initial request letter does not provide the necessary consent to the disclosure of a confidence or secret or to the evaluation of a claim since that consent may only be given after full disclosure to the client of the legal consequences of such action.

(c) Lawyers should bear in mind, in evaluating claims, that an adverse party may assert that any evaluation of potential liability is an admission.

(d) In securing the client's consent to the disclosure of confidences or secrets, or the evaluation of claims, the lawyer may wish to have a draft of his letter reviewed and approved by the client before releasing it to the auditor; in such cases, additional explanation would in all probability be necessary so that the legal consequences of the consent are fully disclosed to the client.

**(2) Limitation on Scope of Response.** It is appropriate for the lawyer to set forth in his response, by way of limitation, the scope of his engagement by the client. It is also appropriate for the lawyer to indicate the date as of which information is furnished and to disclaim any undertaking to advise the auditor of changes which may thereafter be brought to the lawyer's attention. Unless the lawyer's response indicates otherwise, (a) it is properly limited to matters which have been given substantive attention by the lawyer in the form of legal consultation and, where appropriate, legal representation since the beginning of the period or periods being reported upon, and (b) if a law firm or a law department, the auditor may assume that the firm or department has endeavored, to the extent believed necessary by the firm or department, to determine from lawyers currently in the firm or department who have performed services for the client since the beginning of the fiscal period under audit whether such services involved substantive attention in the form of legal consultation concerning those loss contingencies referred to in Paragraph 5(a) below but, beyond that, no review has been made of any of the client's transactions or other matters for the purpose of identifying loss contingencies to be described in the response.<sup>2</sup>

**(3) Response May Be Limited to Material Items.** In response to an auditor's request for disclosure of loss contingencies of a client, it is appropriate for the lawyer's response to indicate that the response is limited to items which are considered individually or collectively material to the presentation of the client's financial statements.

**(4) Limited Responses.** Where the lawyer is limiting his response in accordance with this Statement of Policy, his response should so indicate (see Paragraph 8). If in any other respect the lawyer is not undertaking to respond to or comment on particular aspects of the inquiry when responding to the auditor, he should consider advising the auditor that his response is limited, in order to avoid any inference that the lawyer has responded to all aspects; otherwise, he may be assuming a responsibility which he does not intend.

**(5) Loss Contingencies.** When properly requested by the client, it is appropriate for the lawyer to furnish to the auditor information concerning the following matters if the lawyer has been engaged by the client to represent or advise the client professionally with respect thereto and he has devoted substantive attention to them in the form of legal representation or consultation:

(a) Overtly threatened or pending litigation, whether or not specified by the client;

(b) A contractually assumed obligation which the client has specifically identified and upon which the client has specifically requested, in the inquiry letter or a supplement thereto, comment to the auditor;

(c) An unasserted possible claim or assessment which the client has specifically identified and upon which the client has specifically requested, in the inquiry letter or a supplement thereto, comment to the auditor.

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<sup>2</sup> As contemplated by Paragraph 8 of this Statement of Policy, this sentence is intended to be the subject of incorporation by reference as therein provided.

With respect to clause (a), overtly threatened litigation means that a potential claimant has manifested to the client an awareness of and present intention to assert a possible claim or assessment unless the likelihood of litigation (or of settlement when litigation would normally be avoided) is considered remote. With respect to clause (c), where there has been no manifestation by a potential claimant of an awareness of and present intention to assert a possible claim or assessment, consistent with the considerations and concerns outlined in the Preamble and Paragraph 1 hereof, the client should request the lawyer to furnish information to the auditor only if the client has determined that it is probable that a possible claim will be asserted, that there is a reasonable possibility that the outcome (assuming such assertion) will be unfavorable, and that the resulting liability would be material to the financial condition of the client. Examples of such situations might (depending in each case upon the particular circumstances) include the following: (i) a catastrophe, accident or other similar physical occurrence in which the client's involvement is open and notorious, or (ii) an investigation by a government agency where enforcement proceedings have been instituted or where the likelihood that they will not be instituted is remote, under circumstances where assertion of one or more private claims for redress would normally be expected, or (iii) a public disclosure by the client acknowledging (and thus focusing attention upon) the existence of one or more probable claims arising out of an event or circumstance. In assessing whether or not the assertion of a possible claim is probable, it is expected that the client would normally employ, by reason of the inherent uncertainties involved and insufficiency of available data, concepts parallel to those used by the lawyer (discussed below) in assessing whether or not an unfavorable outcome is probable; thus, assertion of a possible claim would be considered probable only when the prospects of its being asserted seem reasonably certain (i.e., supported by extrinsic evidence strong enough to establish a presumption that it will happen) and the prospects of non-assertion seems slight.

It would not be appropriate, however, for the lawyer to be requested to furnish information in response to an inquiry letter or supplement thereto if it appears that (a) the client has been required to specify unasserted possible claims without regard to the standard suggested in the preceding paragraph, or (b) the client has been required to specify all or substantially all unasserted possible claims as to which legal advice may have been obtained, since, in either case, such a request would be in substance a general inquiry and would be inconsistent with the intent of this Statement of Policy.

The information that lawyers may properly give to the auditor concerning the foregoing matters would include (to the extent appropriate) an identification of the proceedings or matter, the stage of proceedings, the claim(s) asserted, and the position taken by the client.

In view of the inherent uncertainties, the lawyer should normally refrain from expressing judgments as to outcome except in those relatively few clear cases where it appears to the lawyer that an unfavorable outcome is either "probable" or "remote;" for purposes of any such judgment it is appropriate to use the following meanings:

- (i) Probable—(an unfavorable outcome for the client is probable if the prospects of the claimant not succeeding are judged to be extremely doubtful and the prospects for success by the client in its defense are judged to be slight.
- (ii) Remote—(an unfavorable outcome is remote if the prospects for the client not succeeding in its defense are judged to be extremely doubtful and the prospects of success by the claimant are judged to be slight.

If, in the opinion of the lawyer, considerations within the province of his professional judgment bear on a particular loss contingency to the degree necessary to make an informed judgment, he may in

appropriate circumstances communicate to the auditor his view that an unfavorable outcome is "probable" or "remote," applying the above meanings. No inference should be drawn, from the absence of such a judgment, that the client will not prevail.

The lawyer also may be asked to estimate, in dollar terms, the potential amount of loss or range of loss in the event that an unfavorable outcome is not viewed to be "remote." In such a case, the amount or range of potential loss will normally be as inherently impossible to ascertain, with any degree of certainty, as the outcome of the litigation. Therefore, it is appropriate for the lawyer to provide an estimate of the amount or range or potential loss (if the outcome should be unfavorable) only if he believes that the probability of inaccuracy of the estimate of the amount or range of potential loss is slight.

The considerations bearing upon the difficulty in estimating loss (or range of loss) where pending litigation is concerned are obviously even more compelling in the case of unasserted possible claims. In most cases, the lawyer will not be able to provide any such estimate to the auditor.

As indicated in Paragraph 4 hereof, the auditor may assume that all loss contingencies specified by the client in the manner specified in clauses (b) and (c) above have received comment in the response, unless otherwise therein indicated. The lawyer should not be asked, nor need the lawyer undertake, to furnish information to the auditor concerning loss contingencies except as contemplated by this Paragraph 5.

**(6) Lawyer's Professional Responsibility.** Independent of the scope of his response to the auditor's request for information, the lawyer, depending upon the nature of the matters as to which he is engaged, may have as part of his professional responsibility to his client an obligation to advise the client concerning the need for or advisability of public disclosure of a wide range of events and circumstances. The lawyer has an obligation not knowingly to participate in any violation by the client of the disclosure requirements of the securities laws. The lawyer also may be required under the Code of Professional Responsibility to resign his engagement if his advice concerning disclosures is disregarded by the client. The auditor may properly assume that whenever, in the course of performing legal services for the client with respect to a matter recognized to involve an unasserted possible claim or assessment which may call for financial statement disclosure, the lawyer has formed a professional conclusion that the client must disclose or consider disclosure concerning such possible claim or assessment, the lawyer, as a matter of professional responsibility to the client, will so advise the client and will consult with the client concerning the question of such disclosure and the applicable requirements<sup>3</sup> of FAS 5.

**(7) Limitation on Use of Response.** Unless otherwise stated in the lawyer's response, it shall be solely for the auditor's information in connection with his audit of the financial condition of the client and is not to be quoted in whole or in part or otherwise referred to in any financial statements of the client or related documents, nor is it to be filed with any governmental agency or other person, without the lawyer's prior written consent.<sup>4</sup> Notwithstanding such limitation, the response can properly be furnished

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<sup>3</sup> Under FAS 5, when there has been no manifestation by a potential claimant of an awareness of a possible claim or assessment, disclosure of an unasserted possible claim is required only if the enterprise concludes that (i) it is probable that a claim will be asserted, (ii) there is a reasonable possibility, if the claim is in fact asserted, that the outcome will be unfavorable, and (iii) the liability resulting from such unfavorable outcome would be material to its financial condition.

<sup>4</sup> As contemplated by Paragraph 8 of this Statement of Policy, this sentence is intended to be the subject of incorporation by reference as therein provided.

to others in compliance with court process or when necessary in order to defend the auditor against a challenge of the audit by the client or a regulatory agency, provided that the lawyer is given written notice of the circumstances at least twenty days before the response is so to be furnished to others, or as long in advance as possible if the situation does not permit such period of notice.<sup>5</sup>

**(8) General.** This Statement of Policy, together with the accompanying Commentary (which is an integral part hereof), has been developed for the general guidance of the legal profession. In a particular case, the lawyer may elect to supplement or modify the approach hereby set forth. If desired, this Statement of Policy may be incorporated by reference in the lawyer's response by the following statement: "This response is limited by, and in accordance with, the ABA Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information (December 1975); without limiting the generality of the foregoing, the limitations set forth in such Statement on the scope and use of this response (Paragraphs 2 and 7) are specifically incorporated herein by reference, and any description herein of any 'loss contingencies' is qualified in its entirety by Paragraph 5 of the Statement and the accompanying Commentary (which is an integral part of the Statement)."

[The accompanying Commentary is an integral part of this Statement of Policy.]

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<sup>5</sup> As contemplated by Paragraph 8 of this Statement of Policy, this sentence is intended to be the subject of incorporation by reference as therein provided.

## Appendix II - Sample CLS Schedule

CLS Schedule FY 2015											
											12/4/2014
Quarterly Report to Bureaus	Update Notice	atty entry deadline	Supv. Review	Certify Complete	Dates Covered		PFM runs report		Provide to Bureaus	Closed docs	Remarks
<b>1st Q'tr CLS Data</b>	12/1	12/9	12/10	12/11	11/6/14	- 12/11/14	12/12		12/12	12/19	Attorneys now include FY15 new matters
<b>2nd Q'tr CLS Data</b>	3/3	3/15	3/16	3/18	12/12/14	- 3/18/15	3/19		3/19	3/26	
<b>3rd Q'tr CLS Data</b>	6/2	6/15	6/16	6/18	3/19/15	- 6/18/15	6/19		6/19	6/26	Heavy bureau review
Legal Letter & Management Schedule Milestones	Update Notice	atty entry deadline	Supv. Review	Certify Complete	Dates Covered		PFM runs report	Letter Dated	Provide to Auditors	Closed docs	Remarks
<b>CLS below threshold report</b>	6/24	7/7	7/8		10/1/14	- 6/30/15			7/29		Analysis of matters with potential monetary damages not entered into CLS.
<b>Legal Letter</b>	7/8	7/21	7/22	7/24	10/1/14	- 7/24/15	7/27	7/29	7/29	8/5	Auditor review in early August
<b>Management Schedule</b>					"	- "			8/5		Schedule of all open matters
<b>1st Update - Legal Letter</b>	9/15	9/28	9/29	10/1	7/25/15	- 10/1/15	10/2	10/6	10/6	10/13	Changes to likelihood & estimate/range should be tied to events, court decisions
<b>below threshold update</b>					"	- "			"		Only reflects changes in CLS
<b>Management Schedule</b>					"	- "			10/13		Significant changes from earlier schedule
<b>2nd Update - Legal Letter</b>	10/20	11/2	11/3	11/4	10/2/15	- 11/4/15	11/5	11/9	11/9	11/12	Within 10-20 days of AFR issuance. Changes to likelihood & estimate/range should be limited and tied to events, court decisions.
<b>Management Schedule</b>					"	- "			11/12		Significant changes from earlier schedule

## Appendix III - CLS Filename Definitions

The following is a list of file name definitions for the CLS reports:

- **Summary-xx-xx-xx** (pdf and Excel)  
Summary report from the beginning of the previous FY through the period end date shown on the legal request letter (i.e., 10/01/13 – 09/30/15).
- **Summary-closed-FY20XX** (pdf and Excel)  
Summary report of cases closed during the current FY. The date range is the beginning of the FY through the period end date shown on the legal request letter (i.e., 10/01/13 – 9/30/15).
- **Summary-changed-xx-xx-xx** (pdf and Excel)  
Summary report of cases that have been updated or added since the previous pull date. The date range on this is the day after the previous pull date to the period end date shown on the legal request letter (i.e., 06/19/15 – 09/30/15).
- **Data-xx-xx-xx** (Excel only)  
Excel spreadsheet containing details of all cases in all three statuses – Pending (PTA & PTJ), Unasserted (UCA) and Closed (CLS) from the beginning of the previous FY through the period end date shown on the legal letter (i.e., 10/01/13 – 9/30/15).
- **Detail1-xx-xx-xx** (pdf)  
Detail report of all cases in pending status from the beginning of the previous FY through the period end date shown on the legal request letter (i.e., 10/01/13 – 09/30/15).
- **Detail2-xx-xx-xx** (pdf)  
Detail report of all cases in unasserted status from the beginning of the previous FY through the period end date shown on the legal request letter (i.e., 10/01/13-09/30/15).
- **Detail-closed-xx-xx-xx** (pdf)  
Detail report of all cases in closed status from the beginning of the previous FY through the period end date shown on the legal request letter (i.e., 10/01/13 – 09/30/15).
- **Detail1-changed-xx-xx-xx** (pdf)  
Detail report of all cases in pending status that have changed since the previous pull date. The date range on this is the day after the previous pull date to the period end date shown on the legal request letter (i.e., 06/19/11 – 09/30/15).

- **Detail2-changed-xx-xx-xx** (pdf)  
Detail report of all cases in unasserted status that have changed since the previous pull date. The date range is the day after the previous pull date to the period end date shown on the legal request letter (i.e. 06/19/11 – 09/30/15).
- **Detail-closed-changed-xx-xx-xx** (pdf )  
Detail report of all cases in closed status that have changed since the previous pull date. The date range is the day after the previous pull date to the period end date shown on the legal request letter (i.e. 06/19/11 – 09/30/15).

(NOTE: For files related to EDL, the file names include the prefix EDL and are in pdf only.)



## Appendix V - FY 2015 Request for Legal Representation Letters



### United States Department of the Interior

OFFICE OF THE SECRETARY  
Washington, DC 20240

**JUL 01 2015**

#### Memorandum

To: Solicitor

From: Kristen J. Sarri *Amy Holley for*  
Principal Deputy Assistant Secretary – Policy, Management and Budget

Subject: Request for Legal Representation Letters for Audited Financial Statements

Pursuant to 31 U.S.C. § 3515, KPMG LLP will conduct, under contract, an audit of the consolidated financial statements of the U.S. Department of the Interior (Interior) (herein after referred to as the Department) as of September 30, 2015, and for the year then ended.

In performing audits of Government entities, auditors comply with *Government Auditing Standards* issued by the Comptroller General of the United States (the *Yellow Book*). For financial statement audits, the *Yellow Book* incorporates the fieldwork and reporting standards of the American Institute of Certified Public Accountants (AIPCA) and the *Statements on Auditing Standards* that interpret them.

Consistent with the guidance contained in AU 337, *Inquiry of a Client's Lawyer Concerning Litigation, Claims, & Assessments*, of the AICPA's *Codification of Statements on Auditing Standards*, and consistent with procedures contained in Office of Management and Budget (OMB) Bulletin No.14-02, as amended, *Audit Requirements for Federal Financial Statements*, KPMG LLP has inquired about litigation, claims, and assessments to obtain evidence as to the financial accounting and reporting of such matters in the consolidated financial statements. The purpose of this memorandum is to request your assistance in responding to that inquiry by preparing four legal representation letters.

In accordance with Statement of Federal Financial Accounting Standards (SFFAS) Number 5, *Accounting for Liabilities of the Federal Government*, as amended by SFFAS No. 12, *Recognition of Contingent Liabilities Arising from Litigation*, and Interpretation of Federal Financial Accounting Standards No. 2, *Accounting for Treasury Judgment Fund Transactions*, the Department reports certain information in the consolidated financial statements and notes concerning contingent liabilities arising out of litigation, claims, and assessments. Please provide to the Office of Inspector General (OIG) and KPMG LLP, with a copy to the Office of Financial Management (PFM), information involving matters with respect to which your office has been engaged and has devoted substantive attention on behalf of the Department and its bureaus/office(s) in the form of legal consultation or representation. Please include any litigation, claims, assessments, and unasserted claims and assessments (hereinafter "matters") to which your office has been engaged and devoted substantive attention on behalf of the Department, its bureaus/office(s), officers, and employees in the form of legal consultation or

representation. Include matters even where you believe the Judgment Fund or some financing source other than the Department's budgetary resources will pay any potential loss. Under Generally Accepted Accounting Principles, such amounts may need to be included as liabilities or disclosed in the Department's consolidated financial statements. Please report all new matters, pending matters that were previously reported in legal representation letters and those that were reported in the Fiscal Year (FY) 2014 but have been closed in FY 2015. Include matters being handled by the Department of Justice (DOJ) on behalf of the Department. All matters not previously reported should be marked "original." Matters similar in nature may be aggregated where appropriate.

Please furnish the following for matters to OIG, PFM, and KPMG LLP that will exist as of September 30, 2015:

- (1) An initial response by **July 29, 2015**, including matters that existed as of July 24, 2015;
- (2) An update by **October 6, 2015**, that only includes any additions, changes, and deletions from July 25, 2015 through October 1, 2015; and
- (3) An update by **November 9, 2015**, that only includes any additions, changes, and deletions from October 2, 2015 through November 4, 2015.

Please furnish the following for matters to OIG and PFM that will exist as of September 30, 2015: (1) A FY 2015 subsequent events final update by **February 1, 2016**, that only includes any additions, changes, and deletions from November 5, 2015 through January 31, 2016.

The American Bar Association's Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information (December 1975) provides relevant guidance for the Office of the Solicitor's (SOL) legal representation letters. Regarding cases where DOJ attorneys are handling legal matters on behalf of the Department, additional guidance can be found in Federal Financial Accounting and Auditing Standards Technical Release No. 1, *Audit Legal Letter Guidance*, dated March 1, 1998.

The SOL's legal representation letters should follow the guidance in OMB Bulletin No.14-02, as amended, and they should provide descriptions of legal contingencies on standard forms depending on the type of matter involved - i.e., pending, unasserted, or closed (see Attachments 1, 2, and 3). The SOL should complete a separate form for each matter or group of related cases, and attach the forms to the four legal representation letters (preliminary and three update letters). In addition, SOL should promptly submit advance copies of updated forms to PFM for cases in which significant developments change the likelihood of unfavorable outcome or the estimate of loss.

Please provide your data in the attached standard formats. Note that the applicable dollar threshold for reporting (specified below) should be entered at the top of each form in the designated field. Also, please complete the appropriate field to indicate either an original submission or an update, and provide the date. You should include the notation "potential environmental cleanup liability" in field 2 *Nature of Matter* for all matters which may involve possible environmental cleanup liabilities. Also, please combine related matters where appropriate, group matters by bureau/office(s), and sequence them in descending order by

amount of potential liability. You should place matters for which the amount of potential loss cannot be estimated at the end of the sequence.

It is important that the legal representation letters include an explanation for each change in either the evaluation of likelihood of unfavorable outcome or the estimate of potential loss (i.e., a change from the previously reported status). Similarly, please provide a brief explanation where the estimate of potential loss is not entered. These explanations should be included under *Progress of the Case to Date* for pending or threatened litigation and under *Nature of the Matter* for unasserted claims and assessments.

For purposes of this request, please include any matter individually or in the aggregate where similar/related matters are grouped involving amounts of \$1,000,000 or more for Indian Affairs, the Bureau of Land Management, the Bureau of Reclamation, the U.S. Fish and Wildlife Service, the Bureau of Ocean Energy Management, the Bureau of Safety and Environmental Enforcement, the National Park Service, the Office of Surface Mining, the U.S. Geological Survey, and the Departmental Offices, and include any matter individually or in the aggregate where similar/related matters are grouped involving amounts of \$50,000 or more for the Office of the Special Trustee for American Indians.

A. Pending or Threatened Litigation

Please provide the following information regarding pending or threatened litigation:

1. Case Name;
2. Nature of Matter (including a description of the proceedings, the claim(s) asserted, the damages sought, the objectives sought by the plaintiff (if any) other than monetary, or other damages (such as performance or discontinued performance of certain actions), and where appropriate, a notation for “*Potential environmental cleanup liability*”);
3. Progress of the Case to Date;
4. The Government’s Response or Planned Response (e.g., to contest the case vigorously, or to seek an out-of-court settlement);
5. An Evaluation of the Likelihood of Unfavorable Outcome (e.g., categorized as probable (likely to occur), or as not probable or remote, or remote (the chance of an unfavorable outcome is slight));
6. An Estimate of the Amount or Range of Potential Loss (for losses considered to be probable or not probable or remote) and Expected Source of Funds for Payment (if an amount or range cannot be estimated, state the reasons);
7. The Name and Phone Number of the Agency and DOJ Attorneys Handling the Case; and
8. The Sequence Number.

For threatened litigation, please indicate “not yet filed” as progress to date.

B. Unasserted Claims and Assessments

Please provide the following information regarding unasserted claims and assessments involving matters that you consider probable of assertion, and which, if asserted, have a reasonable possibility of an unfavorable outcome:

1. Name of Matter;
2. Nature of Matter (including, where appropriate, a notation for “*Potential environmental cleanup liability*”);
3. The Government’s Planned Response;
4. An Evaluation of the Likelihood of Unfavorable Outcome (e.g., categorized as probable (likely to occur), or as not probable or remote, or remote (the chance of an unfavorable outcome is slight));
5. An Estimate of the Amount or Range of Potential Loss and Expected Source of Funds for Payment;
6. The Name and Phone Number of the Agency and DOJ Attorneys Handling the Case (Matter); and
7. The Sequence Number.

C. No-Longer-Pending Cases That Were Reported in the Prior Legal Representation Letter

Please provide the following information regarding litigation reported in the prior legal representation letter that is no longer pending:

1. Name of Matter;
2. Sequence Number;
3. Resolution of Matter; and
4. The Name and Phone Number of the Agency and DOJ Attorneys.

Please provide documentation for the outcome of each matter that is closed in FY 2015. Documentation for each matter should have the bureau/office(s) and the Sequence Number of the matter written on the top of the first page to facilitate record keeping.

With respect to a matter recognized to involve an unasserted claim or assessment that may call for financial statement disclosure, please specifically confirm in the legal representation letter that my understanding of the following is correct: whenever, in the course of performing legal services for the Department, you have formed a professional conclusion that the Department should disclose or consider disclosure concerning such possible claim or assessment. And, as a matter of professional responsibility to the Department, please: (1) advise me of your conclusion; and (2) consult with me concerning the question of such disclosure and the applicable requirements of SFFAS No. 5, as amended.

Matters Individually Not Greater Than Threshold Amounts

Please provide the maximum aggregate amount (i.e., the total) of loss contingencies for matters that individually are less than or equal to the threshold amounts identified above. Claimed

amounts, if any, may be used for these lower-dollar matters. Where there are no firm claimed amounts or you consider them unreasonable, the maximum potential loss amounts should be estimated. Based on input from your divisions and field offices, the total as of October 1, 2014, was approximately \$66 million. As with the previous year, please state the total of loss contingencies that are individually less than or equal to the threshold amounts in your legal representation letters.

#### Matters That May Involve Another Governmental Entity

Please separately identify any pending or threatened litigation and unasserted claims with respect to which you have been engaged and to which SOL has devoted substantive attention on behalf of the Department in the form of legal consultation or representation for which you believe another governmental entity may be responsible for any potential liability.

Please specifically identify the nature of and reasons for limitations on your response to this request.

#### Quarterly Information

In addition to the four legal representation letters discussed above, finance offices require information about contingent liabilities from litigation, claims, and assessments in their preparation of quarterly financial statements. Unlike the fiscal year-end requirements, this information need not be submitted as part of a formal legal representation letter. After the fiscal year-end information is provided with the legal representation letters, please resume electronically submitting to PFM quarterly information on the standard forms one week before each fiscal quarter ends. Submission of the information one week before the quarter ends will enable environmental and finance office personnel to resolve apparent differences in liability likelihood or estimates regarding matters identified as having potential environmental cleanup liability.

#### Other Matters

Please separately identify any pending or threatened litigation and unasserted claims with respect to which you have been engaged but for which SOL has not yet devoted substantive attention on behalf of the Department.

#### Confirmation of Matters Communicated to the OIG and Department Management

Please confirm in your legal representation letters that all information brought to your attention indicating the occurrence of a possible non-compliance with laws and regulations, including illegal acts committed by the Department or any of its agents or employees, has been reported to the OIG and, as appropriate, to Department management.

Submission of the Information

You should submit the legal representation letters, with information and updates about contingent liabilities for litigation, claims, and assessments to: Ms. Mary Kendall, Deputy Inspector General, via e-mail at [Mary\\_Kendall@doioig.gov](mailto:Mary_Kendall@doioig.gov); Mr. Doug Glenn Deputy Chief Financial Officer and Director, PFM, via e-mail at [Douglas\\_Glenn@ios.doi.gov](mailto:Douglas_Glenn@ios.doi.gov); and to Ms. Elizabeth Hacquard, KPMG LLP, via e-mail at [EHacquard@kpmg.com](mailto:EHacquard@kpmg.com). Please submit these documents electronically, in PDF format, including required signatures. The OIG is required to submit these documents to DOJ, the U.S. Department of the Treasury's Financial Management Service, and the U.S. Government Accountability Office.

If you have any questions, please contact Douglas Glenn at (202) 513-0362 or via e-mail at [Douglas\\_Glenn@ios.doi.gov](mailto:Douglas_Glenn@ios.doi.gov).

Attachments

## Appendix VI - Sample Legal Representation Letter Response



### United States Department of the Interior

OFFICE OF THE SOLICITOR  
Washington, D.C. 20240

IN REPLY REFER TO:

July 30, 2014

#### Memorandum

To: Mary Kendall  
Deputy Inspector General

Elizabeth L. Hacquard  
KPMG LLP

Through: Douglas A. Glenn   
Director, Office of Financial Management

From: Edward T. Keable   
Deputy Solicitor

Subject: Legal Representation Response in connection with the FY 2014 Financial Statement Audit of the Department of the Interior

I am responding to the June 2, 2014, memorandum from Assistant Secretary Suh in connection with the audit of the Department of the Interior's (Department's) fiscal year 2014 financial statements and the applicable reporting requirement in OMB's July 22, 2004 memo. As Deputy Solicitor, I have the delegated authority to respond to the June 2, 2014, memorandum.

This memorandum transmits, in an attachment, updated information about the Department's potential financial liabilities from pending or threatened litigation, claims, and assessments. The attachment contains the reports on pending litigation and unasserted claims, and it reflects the status of cases and matters pending as of July 29, 2014. The attachment includes the following reports in files named as indicated:

1. A summary of matters (i.e., pending, unasserted, and closed cases and claims) with data added, deleted, or changed from 10/1/12 through 7/25/14 [summary-7-25-14.pdf]
2. A summary of matters closed in FY 2014 [summary-closed-FY2014.pdf]
3. Files of detail reports on each matter with data added, deleted, or changed from 10/1/12 through 7/25/14 [detail 1/2/-closed-7-25-14.pdf]
4. A summary of matters marked as potential environmental and disposal liability (EDL) items with data from 10/1/12 through 7/25/14 [edl-summary-7-25-14.pdf]
5. Files of detail reports on each matter marked as potential EDL items with data from 10/1/12 through 7/25/14 [edl-detail 1/2/-closed-7-25-14.pdf]
6. Contingent Liability System (CLS) raw data spreadsheet [data-7-25-14.xls]
7. Files of detail reports on each matter with data added, deleted, or changed from 7/26/14 through 7/29/14 [detail1-changed-7-29-14.pdf]

These files contain information that may be exempt from FOIA release, and the data should not be released outside the Executive Branch (except to the auditors and GAO) without SOL approval.

As requested, we have included updated matters individually involving amounts of \$1,000,000 or more for the Bureau of Indian Affairs, the Bureau of Land Management, the Bureau of Ocean Energy Management, the Bureau of Safety and Environmental Enforcement, the Bureau of Reclamation, the Departmental Offices, the Fish and Wildlife Service, the National Park Service, the Office of Surface Mining, and the United States Geological Survey, and amounts of \$50,000 or more for the Office of the Special Trustee for American Indians.

The response includes matters pertaining to tribal trust funds and Individual Indian Monies (IIM) Trust funds managed by the Office of Trust Funds Management, a part of the Department's Office of the Special Trustee for American Indians.

The Solicitor of the Department, assisted by her staff (collectively, the Office of the Solicitor), has general supervision over the Department's legal affairs. The Office of the Solicitor has reviewed litigation and claims, asserted or threatened, involving the Department and has consulted with Department of Justice legal counsel with respect thereto when deemed appropriate. Though the Office of the Solicitor represents the Department on a regular basis, our engagement is limited to specific matters on which we have been consulted. There may exist matters of a legal nature which could have a bearing on the financial position of a bureau or the Department with respect to which we have not been consulted.

Subject to the foregoing and the last substantive paragraph of this memorandum, I advise you that, since October 1, 2013, neither the Solicitor nor any of the lawyers over whom she exercises general legal supervision have given substantial attention to, or represented any of the bureaus in connection with: (1) loss contingencies over \$1,000,000 [over \$50,000 for Office of the Special Trustee for American Indians], or (2) loss contingencies that are less than or equal to the above amounts but in the aggregate exceed \$64 million, coming within the scope of clause (a) of Paragraph 5 of the American Bar Association *Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information* (December 1975) (ABA Statement of Policy) except pending or threatened litigation which is expressly made a part hereof. With respect to matters which have been specifically identified as contemplated by clauses (b) or (c) of Paragraph 5 of the ABA Statement of Policy, I advise you, subject to that paragraph, of the unasserted claims and assessments identified in the attachment.

The information set forth herein is as of July 29, 2014, except as otherwise noted, and I disclaim any undertaking to advise you of changes which thereafter may be brought to the Solicitor's attention or the attention of the lawyers over whom she exercises general legal supervision. This response is limited by, and in accordance with, the ABA Statement of Policy. Without limiting the generality of the foregoing, the limitations set forth in the ABA Statement of Policy on the scope and use of this response (Paragraphs 2 and 7) are specifically incorporated herein by reference. Any description herein of any "loss contingencies" is qualified in its entirety by Paragraph 5 of the ABA Statement of Policy and the accompanying commentary, which is an integral part of the ABA Statement of Policy.

I confirm that whenever, in the course of performing legal services for the Department or its bureaus with respect to a matter recognized to involve an unasserted possible claim or assessment that may call for financial statement disclosure, the Office of the Solicitor has formed a professional conclusion that the Department or bureau must disclose or consider disclosure concerning such possible claim or assessment, and the Solicitor or her staff will so advise the Department or bureau. Under these circumstances, we will consult with its management concerning the question of such disclosure and the applicable requirements of Statement of Federal Financial Accounting Standard (SFFAS) No. 5, "Accounting for Liabilities of the Federal Government," as amended.

We confirm that all information brought to our attention indicating the occurrence of a probable/likely illegal act committed by the Department, or any of its agents or employees, has been reported to the OIG and as appropriate, to the Department of the Interior management.

If you have any questions regarding this letter, please contact Jason Earwood at (202) 208-6115.

Attachment



## Appendix VIII - Accounting Treatment

### Recording the Contingent Liability

Bureaus should process the following entries, which are based on the expected source of funding, to record contingent liabilities for open unasserted or pending matters with probable amounts in the CLS that are not marked as “Settlement Payment Triggered”.

#### *HOW TO DETERMINE THE EXPECTED SOURCE OF FUNDING:*

*Information provided in the CLS will provide guidance to the bureaus on the expected source of funding for the potential loss. Each matter will designate the Source of Funding as Judgment Fund, Appropriation, or Unknown. For Judgment Fund and Unknown matters, unless otherwise noted in the claim detail that it falls under the Contract Disputes Act (CDA), these cases should be classified as Judgment Fund, non-reimbursable for accounting treatment purposes. If the detail identifies the claim as a CDA, these matters should be classified as Judgment Fund, reimbursable. The Appropriation designation implies that any loss would be expected to be paid directly by the Department out of an available appropriation. In the event that the expected source of funding changes throughout the life of the matter, bureaus should update the accounting entries accordingly.*

To record contingent liabilities where the expected source of funding is the Treasury Judgment Fund (JF) NOT requiring reimbursement:

Debit 6790 Expenses Not Requiring Budgetary Resources – Non Federal  
Credit 2920 Contingent Liability - Non Federal

To record contingent liabilities where the expected source of funding is the Treasury Judgment Fund that WILL require reimbursement or is expected to be paid by future DEPARTMENT appropriations:

Debit 6800 Future Funded Expenses - Non Federal  
Credit 2920 Contingent Liability - Non Federal

#### Summary Chart:

EVENT	Source of Funding					
	Non-Reimbursable JF		Reimbursable JF		Appropriations	
	Debit	Credit	Debit	Credit	Debit	Credit
<b>Record Contingent Liability</b>	6790	2920	6800	2920	6800	2920

## **Reversing Contingent Liabilities & Recording Settlements (where applicable)**

Bureaus should process the following entries when probable matters are marked as “Settlement Payment Triggered” or “Closed” in the CLS.

### **STEP 1 – Reverse Contingent Liability**

To reverse contingent liabilities previously recorded where the expected source of funding is the Treasury Judgment Fund, NOT requiring reimbursement:

Debit 2920 Contingent Liability - Non Federal  
Credit 6790 Expenses Not Requiring Budgetary Resources - Non Federal

### **OR**

To reverse contingent liabilities where the expected source of funding is the Treasury Judgment Fund, requiring reimbursement or agency appropriations:

Debit 2920 Contingent Liability - Non Federal  
Credit 6800 Future Funded Expense - Non Federal

### **STEP 2 – Record Settlement (if applicable)**

For matters marked as “Settlement Payment Triggered” or “Closed” with a loss amount in the CLS and supporting documentation provided by the Office of the Solicitor, record the following as imputed costs where the expected source of funding is the Treasury Judgment Fund, NOT requiring reimbursement:

Debit 6730 Imputed Costs – Trading Partner 020/3101  
Credit 5780 Imputed Financing Sources - Trading Partner 020/3101

*(Treasury records a cost accrual for any settlements submitted to the Judgment Fund that have not yet been paid.)*

### **OR**

For matters marked as “Settlement Payment Triggered” or “Closed” with a loss amount in the CLS, record the following where the expected source of funding is the Treasury Judgment Fund, requiring reimbursement:

Debit 6800 Future Funded Expense - Trading Partner 020 /3101  
Credit 2990J Other Liabilities Without Related Budgetary Obligations (JF) -  
Trading Partner 020/3101

*(Treasury records a cost accrual for any settlements submitted to the JF that have not yet been paid, along with a matching receivable for claims where reimbursement is required. Quarterly, the Department will reconcile Treasury’s SGL 1310 with the Department’s SGL 2990J).*

**OR**

For matters marked as “Settlement Payment Triggered” or “Closed” with a loss amount in the CLS, record normal spending transactions for settlements expected to be directly funded with Department appropriations.

*(Note: If a loss is expected to be paid by direct appropriations, however funding is not yet available, bureaus may record a future funded expense and other liability until the funded cost accrual is recorded to ensure financial statements and note disclosures are accurately stated.)*

**Judgment Fund Payments**

The Judgment Fund Agency Payment Report generated from Treasury’s JFICS system will be distributed quarterly to the bureaus by PFM. No action is required for payments identified in this report unless the related contingent liability has not been previously removed based on information provided in the distributed CLS reports. If there are differences in amounts or changes in final source of funding (refer to Citation Code Description) compared to what was previously recorded in the financial statements and note disclosures, please update the transactions accordingly to reflect the final information provided in the JFICS Agency Payment Report.

*(The Office of the Solicitor will update the CLS to match the settlement and closed case documentation which should minimize differences.)*

**Summary Chart:**

EVENT	Source of Funding					
	Non-Reimbursable JF		Reimbursable JF		Appropriations	
	Debit	Credit	Debit	Credit	Debit	Credit
<b>Reverse Contingent Liability</b>	2920	6790	2920	6800	2920	6800
<b>Record Settlement (if applicable)</b>	6730	5780	6800	2990J	**	**
<b>JF Paid</b>	N/A	N/A	N/A	N/A	N/A	N/A

\*\* Normal expenditure accounting (obligations/operating costs/payables/cash)

**NOTE: No-FEAR Act claims are normally below threshold and are reimbursed immediately by POB. The POB then seeks reimbursement from the appropriate bureaus through reimbursable agreements. (See PFM’s Financial Management Memorandum 2010-006 - No FEAR Act Settlement and Award Payments for more details.)**