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A Management Control Audit on the General Land Office and Veterans Land Board

November 1996

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Key Points of Report

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Overall Conclusion

The General Land Office and Veterans Land Board have management control systems which provide reasonable assurance that their goals and objectives are met. A need exists, however, to enhance funds management planning and to improve planning and monitoring for grant and contract administration. The Veterans Land Board needs to formally address long-range planning issues associated with the $990.6 million land loan program and the $964 million housing loan programs. Review of the $3 million Coastal Oil-Spill Simulation System and the $1.3 million Funds Management Information System indicates a need to improve planning and monitoring processes for grant and contract administration.

Key Facts and Findings

- The Veterans Land Board (Board) needs to formally address long-range issues pertaining to the future of the land and housing programs. Although the Board has indicated that its goal is to eventually make land loans without issuing bonds, no formal plan outlines how this will be achieved. Possible legal restrictions on the use of funds and alternative uses of the $330 million in assets in the land program need to be evaluated. Plans to address both the anticipated downsizing of the veterans housing programs and the continuing role of the administrator to service outstanding loans would help to ensure continuity for participants in these programs.

- Ownership of the Coastal Oil-Spill Simulation System and responsibility for operating costs were not finalized prior to construction start-up. A $1.5 million matching grant for the General Land Office's share of the project was paid in advance of construction, and contractual provisions to monitor expenditures were lacking.

- Development of the Funds Management Information System is two years behind schedule. The delay has caused management to rely on less sophisticated tools to plan and manage the Veterans Land Board and Coastal Protection funds.

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This audit was conducted in accordance with Government Code, §§ 321.0132 and 321.0133.

Executive Summary

The General Land Office and Veterans Land Board have systems of management controls which provide reasonable assurance that their goals and objectives are met. Several opportunities were identified to enhance aspects of existing planning and management functions. Long-term planning issues pertaining to the management of the Veterans Land Board need to be formally addressed to ensure continuity for program participants. A review of grant and contract administration indicates a need to improve planning and monitoring functions associated with the Coastal Oil-Spill Simulation System and Funds Management Information System projects. Efforts to improve the accumulation of cost information could be enhanced by clarifying the objectives and testing the assumptions of a pilot cost allocation methodology. Controls over a recently implemented timekeeping system, which provides the input data for the proposed cost allocation methodology, need to be improved and standardized to ensure data accuracy and reliability.

Formalize Long-Range Plans for Management of Veterans Land Board Programs

The Veterans Land Board (Board) needs to formally address long range planning issues associated with the $990.6 million land loan program and the $964 million housing loan programs. The Board has indicated that its goal is to eventually maintain the land program without issuing bonds. However, the Board has not established formal, comprehensive plans that detail how this objective will be realized. Legal issues pertaining to the Board's authority to make land loans without issuing debt need to be clarified. Various options regarding the best economic use of the $330 million of assets in the land program also need to be addressed.

The Board needs to develop a formal plan to address the expected downsizing of the housing program due to the impact of the federal Tax Reform Act of 1984 (Act). It is anticipated that the Act will gradually reduce the number of veterans who can receive housing loans from tax-free bonds through the year 2006. After 2006, few if any veterans will benefit from the lower mortgage interest rates provided by tax exempt bonds. In addition, contingency plans to address the possibility of bringing master servicing in-house would provide additional assurance of continuity for program participants.

Improve Planning and Monitoring of Grants and Contracts

Plans to build the Coastal Oil-Spill Simulation System did not resolve the issue of long-term facility ownership and costs for operations and maintenance before construction started. A $1.5 million matching grant payment to build the facility was made prior to construction start-up and before the project operating agreement was finalized. Lost interest on the advance grant payment cost the State approximately $46,000. In addition, the terms of the agreement lack adequate provisions to monitor project expenditures or assure that funding commitments by the General Land Office's partner in the project are met.

The $1.3 million Funds Management Information System is approximately two years behind schedule. This has caused management to rely on less sophisticated tools to plan and manage the Veterans Land Board and Coastal Protection funds. In lieu of an operational system, the agency also incurs costs for consultants to perform analyses and projections to manage debt and investments associated with Veterans Land Board programs. Alternatives to future information systems development contracts might include making payment contingent upon user acceptance of clearly defined deliverables and guidelines for terminating contracts in the event of cost overruns or missed deliverables.

Define and Allocate Costs for Program and Support Departments

The General Land Office and Veterans Land Board have made a commendable effort to improve the accumulation of cost information. These efforts could be further enhanced by clarifying the purposes and decision areas the cost information will support. Improved controls over the recently implemented timekeeping system would enhance the accuracy and reliability of this data, particularly with respect to assigning support personnel costs to direct service program areas. The pilot cost allocation methodology could be improved by reviewing and testing assumptions pertaining to the assignment of costs for direct and indirect employees' time.

Human Resource Management Issues Are Being Addressed

Management is taking steps to address human resource issues identified by the Internal Audit Division. These issues centered upon career ladders, policies and procedures for merit pay increases and promotions, performance evaluations, and management training.

The General Land Office has been successful in diversifying its workforce. As of September 30, 1995, minorities comprised 44 percent of the agency, while the statewide average of minorities in the labor force is 35 percent.

Address Noncompliance and Workload Issues Associated with Senate Bill 43 Requirements

Noncompliance by some state agencies to verify their real property inventories impedes the ability of the General Land Office to evaluate the best use of state real property holdings. Eight out of 26 state agencies failed to return a form to verify the accuracy of current inventories of real property holdings for fiscal year 1995. In addition, a sample of five reporting agencies' property transactions conducted in fiscal year 1996 revealed that 5 of 22 transactions had not met the 60-day reporting requirement for land conveyances. While the General Land Office has no authority to enforce compliance with the State Real Property Inventory reporting requirements, greater use of mechanisms available under current law may be sufficient to compel noncompliant agencies to report.

Statutorily mandated cycles for evaluating other agencies' real property creates significant spikes in workloads, making planning and scheduling difficult. The Asset Management Division is required to evaluate real property holdings once every four years and in the year before an agency is scheduled for abolition under the Texas Sunset Act. Uneven workloads make it difficult for the General Land Office to evaluate agencies' properties and perform other necessary real estate appraisals in a timely manner. The General Land Office should work with the Sunset Advisory Commission to develop a plan to reduce or eliminate spikes in workloads arising from Senate Bill 43 requirements.

Integrate Initiatives to Assess Customer Satisfaction with the Strategic Planning Process

The General Land Office and Veterans Land Board have a proactive, comprehensive strategic planning process. Integrating recent initiatives to assess customer satisfaction would enhance an already well-developed process. Extending and formalizing customer feedback mechanisms would enhance the strategic planning internal/external assessment and performance measurement systems. Review of existing customer feedback systems indicates an opportunity to expand and formalize these processes for ongoing improvement.

Review Policies and Procedures for Value-Added Controls

Budget amendment procedures appear to require more sign-offs than necessary for routine approvals. In some cases, however, approval procedures involving large dollar amounts or significant control areas are not consistently followed. In addition, document routing and processing procedures in some areas could be streamlined to reduce overall cycle time.

Additional layers of review for routine approvals have limited value from a control perspective, and may create gaps or omissions when senior management's review and approval is both important and necessary. By clearly defining and delegating authority for more routine and low risk approvals, upper management could free more of its time for more important tasks.

Management's Response to the Executive Summary

The General Land Office and Veterans Land Board appreciates the State Auditors Office's observations and recommendations provided throughout this review. The General Land Office and Veterans Land Board are committed to continual improvement of services for the citizens of Texas. We appreciate the State Auditors Office's recognition of our efforts. We will work to implement all suggestions that will help us fulfill our mission: to serve the people of Texas by preserving their history, protecting their environment, expanding economic opportunity, and maximizing state revenue through innovative, prudent stewardship of state resources.

Specific long-range plans for the Veterans Land Board programs have been documented; the Coastal Oil-Spill Simulation System and Funds Management Information System projects are progressing successfully; and the new timekeeping system and cost allocation methodology have been refined after the first year testing period. Explicit responses to recommendations are included in the detail section of this report.

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Section 1:

Formalize Long-Range Plans for Management of Veterans Land Board Programs

The Veterans Land Board (Board) needs to formally address long-range planning issues associated with the $990.6 million land loan program and the $964 million housing loan programs. The Veterans Land Board has indicated that its goal is to eventually maintain the land program without issuing bonds. However, the Board has not established formal, comprehensive plans that detail how this will be accomplished. Various options regarding the best economic use of the land program assets also need to be considered.

The Board should develop a formal plan to address the expected downsizing of the housing program due to the impact of the federal Tax Reform Act of 1984 (Act). The Act will gradually reduce the number of veterans who can receive housing program loans from tax-free bonds through the year 2006. After 2006, few if any veterans will be able to benefit from the lower mortgage interest rates provided by tax exempt bonds.

Section 1-A:

Veterans Land Program

The Veterans Land Program is funded through general obligation bonds. The program is self-sustaining and has not required general revenue to meet its obligations. As of August 31, 1995, there were $660.1 million in bonds outstanding and $655.9 million in land loan contracts outstanding. The number of loan contracts was 48,501. Assets in excess of liabilities, including bonds payable, in the Veterans Land Program increased from $220.6 million to $330.5 million between fiscal year 1985 and fiscal year 1995. The buildup in funds is due primarily to income exceeding expenses for operating the program.

While the Veterans Land Board plans to eventually make loans without issuing debt, it is not clear whether there is statutory authority to do so under current law. Section 161.178 of the Natural Resources Code states that funds accrued in excess of what is needed to retire the bonds shall be deposited to the credit of the General Revenue Fund. It appears that the Veterans Land Board may need legislative approval in order to establish a program that could make loans without issuing bonds.

Although the Veterans Land Board has indicated that a long-term goal of the program is to make loans without having to issue bonds, at present there is no formal plan to address the specific time frame as to when this might be feasible. In addition, the continued buildup of funds to establish a revolving loan program needs to be weighed against other possible uses of the fund such as early retirement of bonds, refinancing of bonds, or lower interest rates on loans. One barrier to fuller exploration of alternative uses of the land program's funds is the unavailability of the Funds Management Information System (FMIS) discussed in Section 2. Veterans Land Board management anticipates that when the FMIS is fully operational, it will have the tools to analyze cash flows and perform other projections to evaluate both alternative uses of the funds and the timing and amount of funds necessary to make a revolving loan program feasible.

Recommendations:

- The Veterans Land Board should obtain a legal opinion to determine whether the land program can be maintained with assets in the program as opposed to the use of bond fund money.
- The Veterans Land Board should formulate a plan which projects both time lines and the amount of funds that would be necessary to make loans without issuing bonds. The plan should also address possible alternatives for the best economic use of land program assets such as retiring bonds, refinancing bonds, or reducing interest rates charged on loans.

Management's Responses:

The primary goal of the Veterans Land Board (VLB) is to provide below-market-rate loans to veterans as a reward for service to their country. The VLB always attempts to provide the lowest loan rates possible, while ensuring that the bond funds remain self-sustaining. Additionally, federal tax law limits the earnings on the loans by prescribing the maximum allowable spread for the loan rate in excess of the bond rate. The board has been particularly successful in providing low rate loans with such special programs as zero percent home loans, and three and four percent land loans. Since the VLB is one of the oldest bond issuers in the state, and because Texas veterans have historically repaid their debts at a much higher level than the general population, the funds are very strong. No taxpayers' money has ever been required to repay bond indebtedness, and for at least the last thirteen years, no taxpayers' money has been used to pay the expenses of administering the program.

The VLB will obtain a legal opinion from bond counsel on whether the land program can be maintained with assets of the program as opposed to the continual use of bond funds. The VLB will document their plan for eventually making loans without issuing bonds, and address the possible alternatives for using land program assets. Further, the VLB has indicated their desire to recycle bond funds in order to provide lower interest rates on land loans to Texas veterans. It should be noted that opportunities to recycle must be reviewed on a series-by-series basis. This analysis will occur semiannually. Multiple factors must be examined before the determination to recycle within a series can be reached. The policy of the board describes the variables that must be considered. It is anticipated that the board will take formal action on this policy at a meeting this fall.

Section 1-B:
Veterans Housing Programs

Under the provisions of the federal Tax Reform Act of 1984, only taxable bond funds can be used for veterans who entered the service after January 1, 1977, or who were discharged over 30 years ago. The number of veterans eligible for the loans with lower interest rates will diminish as the pool of qualified applicants shrinks. The higher interest rates available for veterans from proceeds of taxable bonds will result in a severe decrease in demand for loans. Although the Veterans Land Board anticipates a dramatic curtailment in demand for housing and home improvement loans after the year 2006, a need to service outstanding loans will continue to exist.

Even as the housing and home improvement loan programs phase out over the next ten years, the administrator for the programs will continue to play a crucial role in servicing outstanding loans. The Veterans Land Board has an agreement with First Nationwide Mortgage Corporation to perform master mortgage servicing through the year 2017. Unlike the land program, for which the Veterans Land Board originates and services all land contracts, approximately 96 percent of home mortgage loans are originated and serviced by participating lenders and 100 percent are master serviced by the administrator. The Veterans Land Board pays $61 annually for each loan serviced. As of August 31, 1995, there were $575.3 million in home mortgages outstanding and $18.5 million of home improvement loans outstanding. There were 17,599 home mortgage loans and 1,690 home improvement loans.

First Nationwide Mortgage Corporation entered into a contract to service loans for the Veterans Land Board in October 1995 after it purchased the mortgage servicing operation from Lomas Mortgage USA, Inc. Although the Veterans Land Board expressed satisfaction with the overall performance of both Lomas and First Nationwide, the Board could face a dilemma if the administrator were unable to perform. The Board indicates that there has been little interest by other mortgage companies in performing the service. This would most likely require the Board to bring the entire home mortgage servicing operation in-house.

<u>Recommendations</u>:

- The Veterans Land Board should develop a long-range plan to address the future of the housing and home improvement programs. The plan should address the anticipated reduction in demand for housing and home improvement loans, and at what point the Board might consider serving these loans in-house.

- The Veterans Land Board should develop a contingency plan for how to service existing loans in the event that the contract with the administrator is terminated.

Management's Responses:

A written, long-range plan to address the future of the housing and home improvement programs has been completed. Because of the complexity and number of factors affecting the program, including federal tax law and ever-changing financial markets, the board will use a combination of strategies during the next ten years to achieve maximum benefits for Texas veterans who need favorable financing to purchase homes. This will require the board and staff continually monitor the markets and evaluate circumstances affecting the programs to take advantage of any opportunity to benefit veterans.

A formal contingency plan has been completed. It addresses the VLB preparedness for continuing the master servicing function of the housing and home improvement loan programs in the event the current master servicer becomes unable to perform the function. (The current contract does not allow for the administrator to withdraw from the contract.) The contingency plan is to bring master servicing in-house for an evaluation period, then determine whether the function should be re-offered to the private sector for the long term.

Section 2:

Improve Planning and Monitoring of Grants and Contracts

Although the General Land Office and Veterans Land Board have established procedures for formulating, paying, and monitoring grants and contracts, issues in two complex projects were noted. Problems in the planning, funding, and monitoring process of the $3 million Coastal Oil-Spill Simulation System were identified. The $1.3 million Funds Management Information System is two years behind schedule. This impairs planning and management for the Veterans Land Board and Coastal Protection funds.

Section 2-A:

Coastal Oil-Spill Simulation System

Several problems were identified in the General Land Office's agreement with the Marine Spill Response Corporation (MSRC) to build the Coastal Oil-Spill Simulation System (COSS) in Corpus Christi. These issues pertain to project planning, funding, and monitoring. Although the completed project will provide a unique facility in which to conduct research on new remediation techniques to clean up oil spills, long-term ownership and responsibility for maintenance and operating costs were not defined prior to construction start-up. A lump-sum, $1.5 million matching grant payment for the General Land Office's share of the construction phase of the project was made months before any construction activity commenced. In addition, the terms of the grant contain no clear, specific provisions to monitor the appropriateness and reasonableness of expenditures, or to ensure that funding commitments by MSRC[1] are met.

Although the COSS is proceeding as a research and development project, it also entails construction of a capital facility. This is an important distinction due to its impact on issues of facility ownership and the timing of funding payments. The early phases of the project, which included building a prototype and design work, clearly entailed research and development related to new techniques for testing remediation of oil spills. These expenditures were appropriately treated as research and development costs since a facility of this nature had never before been designed or constructed. After the completion of the prototype and design phases, however, the scope and cost of the project was definable. At this point, according to Financial Accounting Standards Board definitions, the project clearly moved from research and development into construction of a capital facility. Because the entire project–including the construction phase–was treated as a grant for research and development, the General Land Office did not finalize important planning steps to address the long-term ownership of the facility and costs associated with operations and maintenance.

The original agreement to build the facility included a partnership between the General Land Office, MSRC, and Texas A&M University - Corpus Christi (then Corpus Christi State University). This agreement, which included the prototype for the current construction, was executed in March 1993. Under the original agreement, Texas A&M University - Corpus Christi (University) would own and operate the prototype facility. The General Land Office states that participation in the final engineering and construction phase was terminated because the University would require approximately $1 million to oversee construction of the project. In addition, since the University would have to treat the COSS as a capital project for construction, it would add an additional year to completion time to go through its capital expenditure committee. These additional costs and delays were the primary reasons for the University's departure from the project.

After the University's withdrawal from the project in the spring of 1994, the agreement between the General Land Office and MSRC was amended. Under the terms of the amended agreement, MSRC will oversee construction and own the COSS facility until construction is complete. Upon completion, ownership of the facility will then revert to the General Land Office. The funding contributions for the project are shared equally between the General Land Office and MSRC. Each party agreed to contribute $150,000 for the architectural and engineering design phase and $1.5 million for the construction phase. The General Land Office, however, is committed to fund costs in excess of these amounts, subject to its prior approval.

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[1]MSRC is a national, private, nonprofit organization. Funding for MSRC is provided by the Marine Preservation Association (MPA). MPA is a nonprofit membership corporation organized to promote the interests of the petroleum/energy industries, which includes addressing the problems caused by oil spills in coastal waters.

Although the General Land Office has indicated that it would like to transfer ownership and management of the COSS to a university to conduct research and development, at present no such agreement is in place. The facility is scheduled for completion in December 1996. After installation and testing, it should be operational by approximately March 1997. The General Land Office estimates management costs for operations to be between $325,000 and $350,000 per year. If the facility fails to generate sufficient revenues to cover expenses, operating costs will be paid from the General Land Office's appropriations for research and development.

Recommendations:

- The General Land Office should secure an agreement for ownership and management of the COSS facility as soon as possible.

- The General Land Office should ensure that planning for any future research and development initiatives that entail construction of plant and equipment distinguish between capital expenditures and research and development. Issues of facility ownership and responsibility for operating costs should be finalized prior to the commitment and expenditure of funds.

Management's Responses:

The GLO concluded very successful negotiations for contracting the operation of the Coastal Oil-Spill Simulation System (COSS) facility in August 1996. An agreement was negotiated with Texas A&M University (TAMU)/Kingsville and the Texas Engineering Experiment Station (TEES). The GLO, through an interagency contract, will provide TAMU/Kingsville with $297,490 per year to operate and maintain the COSS; TEES will contribute $85,000 per year to those operating costs. This net cost of $212,490 is well below the $325,000 GLO estimated it would cost for annual operation and maintenance. Negotiating with TAMU/Kingsville and other entities over a two-year period, rather than signing an agreement before the project was started, saved the state significantly. The GLO will become the owner of COSS upon the completion of construction.

The COSS will be a world-class research center, drawing scientists from around the world to study ways to clean up toxic waste, especially oil spills. The facility will consist of nine wave tanks capable of simulating waves, tides, and various shoreline environments including beaches, tidal flats, and marshes. Petroleum products can then be introduced into these controlled environments and innovative remediation technologies can be tested.

The GLO understands that ownership, operation, and maintenance of a one-of-a-kind facility, such as COSS, are critical. The ownership, operation, and associated costs of the COSS have been part of the planning process since the initiation of the project and were explored concurrently with the design and construction of the facility. Over the last two years, the GLO contacted and discussed the operation of the COSS with several entities. Negotiation with these entities culminated in the agreement with

TAMU/Kingsville described above. If future research and development initiatives involving construction are undertaken, issues of operation and ownership will be addressed prior to commitment and expenditure of funds.

A second issue pertaining to the COSS project concerns the nature of the grant payment for the General Land Office's share of the project costs. Although the General Land Office has authority to make research and development grants under the Oil Spill Prevention and Response Act, the timing and structure of the grant made to MSRC unnecessarily cost the State approximately $46,000. Alternative grant terms could have accomplished the objectives of the project at a reduced cost.

Actual construction on the COSS facility did not begin until April 1996. The General Land Office authorized payment of $1.5 million to MSRC on August 31, 1995, approximately seven months before construction start-up. In contrast, according to a representative of the MSRC, the companies financing the MSRC's share of the project contribute funds only on a "pay-as-you-go basis." Lost interest on state funds for the seven months between payment and construction start-up, calculated on average state Treasury interest rates for the period in question, come to approximately $46,000. This does not include any interest that may accrue on unexpended funds held by the recipient over the duration of construction.

The funds for the project were paid almost one month before the operating agreement was finalized. The warrant for $1.5 million was issued by the Comptroller of Public Accounts on September 19, 1995, pursuant to a three page letter of agreement, dated August 28, 1995. While this letter stipulates that the funds may be used only for the COSS, it also notes that no other terms or conditions are required for the transfer or receipt of the funds. The amended agreement governing the project between the General Land Office and MSRC was not finalized until October 16, 1995. The amended agreement details the project description, statement of work, lease agreement with Corpus Christi Power and Light (where the facility is to be built), and the General Land Office's continuing obligations for the project. Although the August 28 grant letter appears to be a binding agreement, the funds were paid without the more detailed final operating agreement in place.

<u>Recommendations</u>:

- The General Land Office should review alternative procedures for contracting and grant administration. Alternative procedures could include provisions for collecting interest on funds held but not yet expended by grantees, or a schedule of payments, particularly for projects entailing capital expenditures.

- The General Land Office should establish procedures to ensure that funds are not expended without a finalized contract or agreement in place.

Management's Responses:

After reviewing various alternatives for the most cost-effective method to build the COSS, the GLO determined that a direct grant to the Marine Spill Response Corporation (MSRC) would achieve the goal of speedy construction at the lowest overall cost to the state. To ensure the state received the MSRC's $1.5 million match plus their in-kind services, GLO provided the state's half of the funding at the beginning of the project.

The MSRC, the premier research and development organization for oil spill response since its inception as industry's response to the Valdez spill, has in-house expertise in construction, contracting and management, and design engineering. Having MSRC provide these services substantially lowered the costs of the COSS. Further, the ability of MSRC to act more expeditiously in the private sector made it cheaper to utilize MSRC for all phases of the design and construction. The GLO recognized that it was cheaper to allow MSRC to perform the tasks they could do more efficiently.

In future projects, GLO will consider all alternatives for funding, including collecting interest of funds held but not yet expended by grantees, to ensure the best use of state funds. The GLO will also ensure that detailed agreements, as well as overall agreements, are completed and in place before funds are expended.

The third area of concern pertaining to the COSS project is the lack of provisions in the agreement to monitor project expenditures. Although the original project agreement which included Texas A&M University - Corpus Christi had clear provisions for financial reporting, the amended agreement between the General Land Office and MSRC lacked such provisions. The original project agreement included a provision for monthly status reports showing "actual spending compared to budget, actual funding paid compared to project funding commitments." Under the agreement now in effect, no financial reporting requirements pertain to MSRC unless MSRC terminates its participation prior to completion of the project. As noted previously, the General Land Office merely stipulates that the funds be used only for the COSS project, and that no terms or conditions are necessary. Thus, the General Land Office lacks a defined process to assure either that the terms of the agreement are adhered to by MSRC, or that MSRC contributes its full share of the project costs.

When contacted by the State Auditor's Office, MSRC stated that due to a recent downsizing, it lacked sufficient staff to provide expenditure information, although its files were available for General Land Office review. It was also noted that the General Land Office lacked key documents to monitor the project. For example, the final bid proposal that was awarded in February 1996 to construct the facility was not in the General Land Office's possession and had to be requested from MSRC.

Recommendations:

- The General Land Office should actively monitor construction of the COSS facility to ensure that state expenditures for the project are allowable and reasonable. In addition, the General Land Office should also monitor to ensure that project funding commitments by MSRC are met.

- The General Land Office should review policies and procedures pertaining to grants and/or contracts to determine whether provisions are adequate to ensure that funds are expended for reasonable and allowable costs. Examples of such provisions might include: requirements for records retention and regular expenditure reports, provisions regarding contractor cost accounting requirements, clear definitions of allowable and unallowable expenditures, provisions for contractor reimbursement of unallowable expenditures, and the right to audit all expenditures.

Management's Responses:

The GLO has an active role in monitoring the construction of COSS. The GLO attends monthly construction meetings, receives weekly construction status reports, and receives monthly expenditure reports. The GLO has also hired an engineering firm to act as on-site construction manager to monitor the contractor's performance. The GLO has access to all MSRC's records related to COSS. The latest reports show the project is on time and on budget. Through these various monitoring tools, the GLO believes that all expenditures for the project are allowable and reasonable, and that the funding commitments by MSRC are being met.

MSRC has been the GLO's partner on various successful research and development projects over the last four years. Throughout these experiences, MSRC has proved to be a valuable partner in reaching the common goal of improved spill response and improved technology.

As is agency practice, the GLO will have our contract specialists in the legal division review all grants and contracts to ensure that necessary provisions are included that require funds are expended for reasonable and allowable costs.

Section 2-B:
Funds Management Information System

The Funds Management Information System (FMIS) project is more than two years behind schedule and has exceeded expenditures for contracted services. The FMIS, developed under contract with KPMG Peat Marwick, was originally scheduled for completion by August 31, 1993. Although managers for the project anticipated having the system operational by August 31, 1996, some key staff members expressed doubt as to whether a fully operational system will be completed by this date. While FMIS is within total projected costs through the end of fiscal year 1996, no funds are budgeted for the project in fiscal year 1997 if the completion date is not met.

The FMIS is intended to provide automated tools to assist the Funds Management Division of the General Land Office to manage the debt and investments associated with the Veterans Land Board bond funds. The Funds Management Division manages over $1 billion of outstanding debt issued to support the land and housing programs of the Veterans Land Board. It also manages approximately $500 million of investments associated with these programs, in addition to investments for the Coastal Protection Fund. The FMIS will provide the Funds Management Division with tools to:

- Monitor compliance with federal arbitrage and arbitrage rebate regulations
- Facilitate effective management of the Board's investment portfolio
- Facilitate effective management of the debt service associated with bonds issued by the Board

When fully operational, FMIS should assist the Funds Management Division with obtaining funds from capital markets at the lowest possible cost, restructure existing debt service, and select the best securities available to satisfy the debt service stream at the lowest possible cost.

Although the contracted amount for KPMG Peat Marwick for system development is $738,496, the total scheduled payments for KPMG Peat Marwick's role in the project through the end of fiscal year 1996 is $860,968. This represents an overage of $122,472. This is possible because the contract allows for monthly billings for hours worked instead of basing payment on user-accepted modules. The total system development costs, including the in-house costs for the General Land Office, will total over $1.3 million if the system is fully operational by the end of fiscal year 1996.

Although work on the project began in April 1990, the extended time frame for development has required multiple changes to the system requirements. As technology advanced during the development, the General Land Office continued to modify the system to take advantage of expanded hardware and software capabilities. These modifications necessitated changes in the original design specifications that in turn extended the project development cycle. The hardware and software specifications developed by KPMG Peat Marwick in the original Requirements Definition became obsolete as the project progressed. The lack of a clear understanding of agency and contractor roles appears to have contributed to delays in completion of the project. In addition, turnover of key personnel at the General Land Office and KPMG Peat Marwick during the extended time line of the project contributed to communication problems and disagreements over the scope of the contractor's responsibilities.

In the absence of an operational system, the Funds Management Division incurs costs for professional services to obtain information that FMIS could have helped to provide. For example, the General Land Office's Biennial Operating Plan notes in its impact analysis that the FMIS would reduce financial advisors fees by $50,000 annually. In addition, the lack of analysis tools may have cost the agency in foregone interest savings. Not having other tools and projection capabilities that FMIS could provide also hinders key fund management planning functions, as discussed in Section 1.

Without proper planning and monitoring procedures, there is a risk that systems may not be implemented on time, as required, or within contracted amounts. Implementation delays may require reallocation of funds and personnel needed for other projects, impacting other areas of the agency. Delays in implementation may also significantly impair operations or incur avoidable costs.

Recommendations:

- The General Land Office and Veterans Land Board should consider structuring system development contracts to make payment contingent upon the agency's acceptance of clearly defined deliverables.
- The General Land Office and Veterans Land Board should ensure that the monitoring of system development includes procedures to follow in case of cost overruns and/or missed delivery dates, including guidelines for when to terminate a contractor or consultant.

Management's Responses:

Although the development of the Funds Management Information System (FMIS) has been difficult and lengthy, staff of the General Land Office/Veterans Land Board (GLO/VLB) and KPMG Peat Marwick (KPMG) have worked diligently to complete the project. When finished, FMIS will be one of the most sophisticated information systems in the country available for use in the management of debt, investments and arbitrage/rebate. When the project was first designed, the level of difficulty associated with progressing from conceptual design to actual implementation was underestimated by all parties. Further, due to the long development period, there have been staff changes, both at the GLO/VLB and KPMG, federal tax law changes, and technological advances. These factors contributed to a delay in the completion date and increased costs for the project. The cashflow module is completed and in the testing phase, and the arbitrage/rebate module will be completed in October 1996.

The GLO/VLB carefully monitored the FMIS project. The initial contract with KPMG included a provision that requires the GLO/VLB to retain ten percent of the cost of the contract until the project is complete. These funds have been retained and will not be released until the GLO/VLB is fully satisfied with the system. It should be noted that KPMG received the final payment under the contract, less the retained ten percent, in December 1995. They continue to work diligently to complete the project.

As recommended, the GLO/VLB will structure future system development projects to be fixed priced contracts with payments released upon the final acceptance of the deliverables, if this structure will be advantageous to the agency.

The agency will also develop guidelines for resolving cost overruns and missed delivery dates, possibly including penalties for missed delivery dates. These guidelines will include criteria for terminating a contractor or consultant.

The GLO/VLB acknowledges that the FMIS project has not progressed as planned; however, the project is nearing its final stages of development. When fully operational, the system will be state-of-the-art and permit the GLO/VLB to manage the bond and investment functions more efficiently and effectively. The system will be a significant asset to the state.

Section 3:

Define and Allocate Costs for Program and Support Departments

The General Land Office and Veterans Land Board have made a commendable effort to link their new automated timekeeping system with a pilot cost allocation methodology. However, the purposes for which the cost information will be used need to be more comprehensively defined prior to implementing the entire system. While the objectives of a cost information system need to be tailored to the unique needs of the agency, several immediate improvements to the tools management has already set in place are possible pending more precise definition of these higher-level issues.

As the automated Timekeeper database provides the inputs for the pilot cost allocation methodology, improved controls over data entered into this system will help to ensure the reliability of this information. Similarly, the accuracy of the pilot cost allocation methodology could be enhanced by testing assumptions pertaining to the assignment of direct and indirect costs to individual program areas.

Section 3-A:

Define the Objectives of the Cost Allocation Methodology

As the operating environment for the General Land Office and Veterans Land Board has become more complex with the addition of new programs and responsibilities, better cost information is increasingly important for effective management. While cost information can be used for a number of purposes, it is particularly important to consider whether the methodology will be used to satisfy requirements other than just financial reporting. It is instructive to note the Federal Accounting Standards Advisory Board's word of caution in designing cost information systems: "If cost information is not useful to the program manager, its value is in serious question, both for improving basic program operations and for broader evaluation or accountability purposes."[2] Thus, it is important to consider the needs of both internal and external users and the decisions they make.

More comprehensive cost information would permit greater accuracy in tracking expenditures for programs financed from restricted funds such as the Veterans Land Board and the Oil Spill Prevention and Response Division. More accurate cost information would also enable the agency to better evaluate the cost effectiveness of

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[2] Federal Accounting Standards Advisory Board; "Managerial Cost Accounting Standards for the Federal Government;" *Statement of Recommended Accounting Standards; Exposure Draft*; October 7, 1994; page 3.

alternatives to current service provision, such as contracting out all or parts of selected functions. The level of effort and amount of detail associated with the accumulation of cost information could vary significantly depending upon the purposes and decision areas it will be used to support.

Recommendation:

The General Land Office and Veterans Land Board should clearly define the objectives for gathering cost information. Some of the objectives that might be considered include: planning, controlling, and improving operations; budget formulation; federal cost reimbursement; privatization; and compliance and accountability issues.

Management's Response:

A task force has reviewed and more clearly defined the objectives of the cost allocation system. The refined objectives of the Cost Allocation Program are included in the Timekeeper Policies and Procedures Update effective September, 1996. The cost information will be used to determine the indirect cost charges for federal grants and other funding sources. It will also be used for budget preparations and management controls.

Section 3-B:

Improve and Standardize Controls Over the Timekeeper System

Opportunities exist to improve the timeliness and reliability of the timekeeping system which was implemented agencywide in September 1995. Several inconsistencies pertaining to how employees charge their time and how supervisors monitor staff compliance were noted.

One particularly significant concern is the inconsistent use of the Allocation Cost Account codes. Allocation Cost Account codes are important because they tie the work performed by approximately 258 staff in four support divisions to the direct service program areas.[3] Heavy use of Allocation Cost Account codes which charge time to the support department itself rather than to the program area served defeats one of the primary benefits of the timekeeping system, which is to link costs incurred (employee time) to the program area served. From September 1995 through April 1996, support staff charged time to their departments rather than program areas in the following amounts:

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[3]The 258 staff work in Information Systems, Field Operations, Central Administration, and Human Resources and Special Programs. Thirty-nine staff are in the Legal Services department, which uses a separate, previously existing timekeeping system to track their time.

- Information Systems 41 percent
- Field Operations 35 percent
- Central Administration 34 percent
- Human Resources/Special Programs 51 percent

For the support departments cited above, time charged to an employee's own departmental support code is appropriate when the activity performed cannot be linked to a single direct program area or grant. However, we identified numerous instances where the work performed was clearly identifiable with an agency strategy and direct service program area. While some staff appear to charge most or all of their time to divisional support codes for purposes of expediency, in many cases there appears to be a lack of understanding on which codes to use.

Recommendations:

- The General Land Office and Veterans Land Board should review charges to departmental support Allocation Cost Account codes to identify and quantify instances where direct charges to program areas should have occurred.

- The General Land Office and Veterans Land Board should communicate to supervisors who approve employees' entries to the Timekeeper database that part of their approval includes a review of the appropriateness of the Allocation Cost Account codes for the activity recorded.

- The General Land Office and Veterans Land Board should communicate to and train staff on the need for accurate use of Allocation Cost Account codes.

Management's Responses:

Timekeeper data, in the first year of inception (fiscal year 1996) has been analyzed for needed improvements. Changes to the Timekeeper Policies and Procedures will be implemented for the new fiscal year, effective September 1996. The changes include: automatic linking of Allocation Cost Accounts (ACA's) to certain activities, limiting time charged to administrative duties, reducing the number of activities an employee can choose, and emphasizing supervisory review of ACA's for reasonableness. Automatically selecting the ACA based on the activity will reduce coding errors. The other changes will provide more accurate and useful management information. These changes to the policies and procedures have been documented and communicated to staff to ensure the reliability of the system's information.

A second concern pertaining to the timekeeping system is the lack of consistent, timely, and complete data entry. Although the Timekeeper policies and procedures manual states that supervisors will approve users time on a weekly basis, not all staff members adhere to a weekly schedule for data entry and approval. In addition, some employees either do not enter time at all or fail to enter enough hours in a month to be considered a full-time equivalent (FTE) employee.

The lack of timely, complete entry of employee hours diminishes both the reliability and usefulness of the Timekeeper database, and incurs additional time and expense to monitor and correct missing or incomplete entries. Discussions with management and staff indicate a degree of cultural resistance to tracking and recording time, particularly since timekeeping system use is a relatively new requirement.

Recommendation:

The General Land Office and Veterans Land Board should consider standardizing a requirement for weekly data entry into Timekeeper for all staff.

Management's Response:

Changes to the procedures effective September 1996 include a requirement for weekly data entry by all employees.

A third concern pertaining to the timekeeping system is inconsistent follow-up to ensure that exceptions to timekeeping system policies are promptly corrected. Compliance with timekeeping system policies is monitored through exception reports which are produced each month by Central Administration. Although exception reports are run monthly, they are not cumulative and do not reflect exceptions from prior months that may not have been corrected.

Recommendation:

The General Land Office and Veterans Land Board should report exceptions on a cumulative basis to identify instances of noncompliance. The General Land Office and Veterans Land Board should also institute controls to ensure that problems noted in Timekeeper exception reports are corrected in a timely fashion.

Management's Response:

Changes to the procedures effective September 1996 also include a new weekly exception report of employees missing time for the week and a new cumulative monthly follow-up report. Supervisors will be required to review and take action on the exception reports.

Section 3-C:

Test Assumptions Pertaining to Allocations of Direct and Indirect Employee Time

Careful review of Timekeeper data should improve the accuracy of how direct and indirect personnel costs are assigned to program areas under the pilot cost allocation methodology. Timekeeper data should be used to validate whether staff function as direct or indirect employees of program areas. In addition, depending upon the level of precision desired, additional tools to augment the timekeeping system may be necessary to identify and assign costs incurred on behalf of different program areas by indirect employees.

Although Field Operations appraisers worked primarily for the Veterans Land Board in the past, the workload generated by the Asset Management Division has steadily increased with the addition of appraisals of other state agencies' properties pursuant to Senate Bill 43 and numerous special projects. Over the first eight months of fiscal year 1996, the workload distribution for the 34 in-house staff appraisers was 50 percent Veterans Land Board and 49 percent Asset Management Division. Under the pilot cost allocation methodology, however, all of the costs incurred by appraisal staff would be assigned to the Veterans Land Board due to their designation as direct employees of the Board.[4] Such an allocation would not accurately reflect the costs incurred by the Asset Management Division for appraisal services.

Recommendation:

The General Land Office and Veterans Land Board should review hours charged to Timekeeper database to validate assumptions as to which employees are actually direct or indirect.

Management's Response:

At the time the cost allocation methodology was developed, there was no universal data, collected agency-wide, to help determine which employees were direct or indirect. Fiscal year 1996, the first complete year of Timekeeper data, will provide more comprehensive, consistent information to make this determination for future cost allocations.

The second issue pertaining to the pilot cost allocation methodology is whether Timekeeper-based allocations will accurately reflect the level of effort of indirect staff

[4] "A 'direct' employee is defined as a staff member whose time can be directly attributed to a specific strategy/program; an 'indirect' employee is one whose time is directly attributed to a number of strategies/programs, or possibly all strategies and program areas." *Timekeeper Policies and Procedures*, General Land Office, August 17, 1995.

who perform work for multiple programs on a continuous basis. If there are significant differences in the activity drivers associated with different programs, a high level allocation of costs based upon the relative percentages of direct time charges to the program areas may understate or overstate the actual costs. For example, some programs may have extremely heavy travel requirements on an ongoing basis, while staff for other programs may rarely travel. In such a case, the administrative costs for processing travel vouchers for the former program area will significantly exceed the costs for the latter program area. Similarly, programs with heavy financial or accounts receivable requirements may incur a large amount of indirect administrative support time in comparison to other programs.

The pilot allocation methodology, however, essentially assumes a level playing field with respect to the activities which drive these costs. However, the costs of capturing such distinctions through the timekeeping system by having employees perform extremely detailed tracking of time on a daily basis might outweigh the benefits. Depending upon the ultimate objectives of the allocation methodology, the agency might consider the relative cost/benefit of capturing such distinctions through mechanisms other than extremely detailed timekeeping entries.

Recommendation:

Contingent upon the ultimate objectives of the allocation methodology, the General Land Office and Veterans Land Board should consider alternative management tools to capture time for indirect support functions with multiple internal customers. One such tool is a time motion study to identify the impact of different activity drivers associated with different programs. Other alternatives to extremely detailed tracking of individual employee time would include estimates of time associated with specific activities to distinguish the impact of activity drivers associated with different programs.

Management's Response:

The GLO realized at the beginning of the project that it was not cost effective to require detailed tracking of individual employee time for certain routine functions. For this reason, estimates of time associated with certain activities based on test periods are used by some division/sections, for example the accounts payable function. The GLO will review other functions and apply this practice when appropriate.

Section 4:

Human Resource Management Issues Are Being Addressed

Prior to the State Auditor's management control audit of the General Land Office and Veterans Land Board, a number of human resource management issues were identified by the General Land Office's Internal Audit Division (Report No. 096-1). These issues centered upon career ladders, policies and procedures for merit pay increases and promotions, performance evaluations, and management training. At the end of fieldwork for this audit, the General Land Office was in various stages of resolving these issues. An overview of the issues identified and the current status of efforts to resolve them are outlined below.

The General Land Office is reviewing all functional job descriptions in conjunction with a career ladder program. This review was approximately 20 percent complete as of March 1996. The review of functional job descriptions is expected to be complete by the end of fiscal year 1997.

A new employee handbook including policy and procedures for merit pay increases and promotions was scheduled for completion in July 1996. The revision of the handbook was undertaken in part to ensure consistency for processing merits, promotions, reclassifications, performance evaluations, and disciplinary actions. Prior to this revision the General Land Office's Internal Audit Division had noted that the Personnel Division lacked written criteria or procedures that must be met or exceeded for an employee to be eligible for salary actions involving either promotions or greater than one-step merit increases.

A new performance appraisal system is scheduled for completion by the end of fiscal year 1996. The revision of the performance appraisal system aligns with efforts to improve criteria for salary actions noted above. Training for management on the performance appraisal system and the employee handbook is anticipated for early fiscal year 1997. Additional management training for other areas including interviewing skills and sexual harassment is also anticipated for early fiscal year 1997.

In addition to reviewing the status of the issues noted above, we also examined a number of other human resource management areas and found them to be functioning appropriately. The General Land Office has been successful in its efforts to diversify its workforce. As of September 30, 1995, minorities comprised 44 percent of the agency, while the statewide average of minorities in the labor force is 35 percent.

Section 5:

Address Noncompliance and Workload Issues Associated With Senate Bill 43 Requirements

Under Senate Bill 43, the General Land Office Asset Management Division is charged with maintaining an inventory of real property owned by non-university state agencies. Noncompliance with the State Real Property Inventory reporting requirements by some agencies impedes the ability of the General Land Office to evaluate the highest and best use of the State's real property. In addition, the schedule for appraising and evaluating properties creates spikes in workloads and poses significant planning and scheduling difficulties.

Section 5-A:

Address Noncompliance With State Real Property Inventory Requirements

Noncompliance by some state agencies to verify their real property inventories impedes the ability of the General Land Office to evaluate the highest and best use of state real property holdings. Eight out of 26 state agencies[5] failed to return a form that verifies the accuracy of current inventories of real property holdings for fiscal year 1995. In addition, a sample of property transactions conducted in fiscal year 1996 revealed that 23 percent had not met the 60-day reporting requirement for land conveyances.

All state agencies that are required to report real property under section 31.151 *et seq* of the Natural Resources Code must complete and return a Master File Report Verification Form to the General Land Office. The General Land Office then certifies the form to indicate that the inventory is complete and accurate. The 1995 General Appropriations Act requires agencies to include the certified verification forms in their Annual Financial Reports.

The General Land Office's guidelines for the State Real Property Inventory requires agencies to report land transactions within 60 days and capital improvements within 30 days. A sample of five reporting agencies' activities in fiscal year 1996 revealed that 5 of 22 transactions did not meet these requirements.

While noncompliance with reporting requirements can impede the General Land Office's ability to evaluate agencies' real property, there is a need for some flexibility in reporting. For example, if an agency is in the middle of a construction project, reporting capital improvements at the end of the fiscal year might require numerous revisions to information reported to the General Land Office. This would create rework for both the General Land Office and the reporting agency.

Although the General Land Office holds regular workshops to inform the property managers of the reporting requirements, it has no authority to enforce compliance. Under article IX, section 77 of the 1995 General Appropriations Act, agencies are not allowed to expend funds after 90 days of the end of the fiscal year if they do not include in their Annual Financial Reports a section consisting of the Master File Report Verification Form certified by the General Land Office. Part 7 of the Act specifies that one of the items that shall be included in the reports is the Master File Report Verification Form certified by the General Land Office. The Act further stipulates that the Comptroller of Public Accounts shall approve all reports as to form

[5] The eight agencies in noncompliance for fiscal year 1995 were: General Services Commission, Adjutant General Department, Texas Department of Public Safety, Texas Department of Transportation, Texas Department of Mental Health and Mental Retardation-Central Office, Texas School for the Blind, Texas Historical Commission, and Texas State Preservation Board. The General Services Commission, Texas Department of Public Safety, and Texas Historical Commission were also in noncompliance in fiscal year 1994.

and content. These provisions should provide a mechanism to compel agencies to comply with the reporting requirements.

Recommendation:

The General Land Office should consider greater use of mechanisms available under current law to compel compliance with the State Real Property Inventory Requirements. One such option would be to report agencies considered to be in substantial noncompliance to the Comptroller of Public Accounts in order to enforce the applicable sections of the General Appropriations Act.

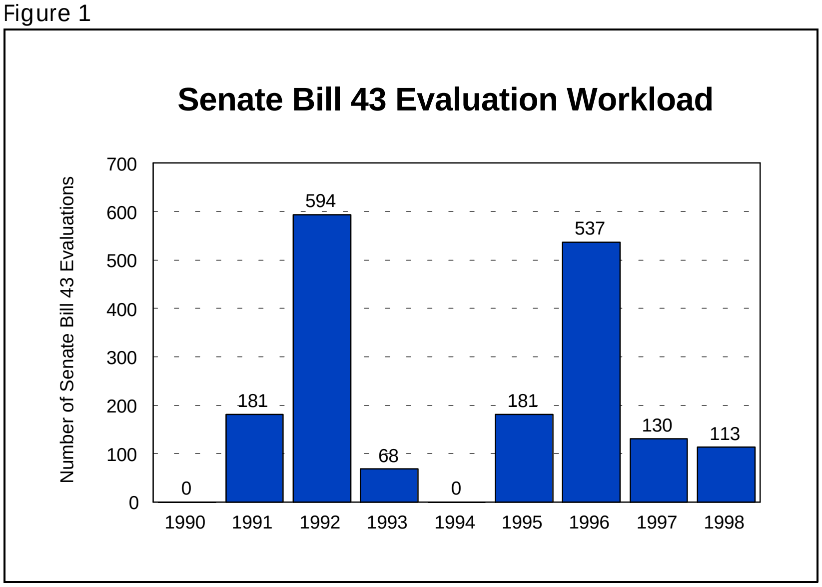
Management's Response:

The GLO will develop criteria and procedures for determining agencies in substantial noncompliance with the State Real Property Inventory Requirements. If efforts through multiple notifications to encourage these agencies to comply are unsuccessful, these agencies will be reported to the Comptrollers Office beginning in fiscal year 1997. Other mechanisms will be developed, if feasible, by the Legal Services Division.

Section 5-B:

Address Senate Bill 43 Workload Issues

Figure 1



Statutorily mandated cycles to evaluate other state agencies' real property holdings create significant variation in workloads for the General Land Office Asset Management Division and Field Operations appraisal work teams. Pursuant to Senate Bill 43, the Asset Management Division must evaluate the highest and best use of state agencies' real property not less than once every four years and in the year before an agency is scheduled for abolition under the Texas Sunset Act. As depicted in Figure 1, the required evaluation cycles create significant spikes in workloads, particularly when agencies with a large number of property holdings are scheduled for evaluation in the same year.

Although the General Land Office has been able to meet required deadlines for evaluating state agency properties, spikes in workloads pose significant planning and scheduling difficulties for both the Asset Management Division and Field Operations. Uneven workloads strain the ability of the Asset Management Division to meet reporting deadlines; they also impact the capacity of Field Operations to meet other real estate appraisal needs of the General Land Office and Veterans Land Board. This has resulted in significant overtime for Field Operations appraisers, as well as an increasing number of Veterans Land Board appraisals being contracted out. While Field Operations was able to complete the 537 Senate Bill 43 appraisals required for fiscal year 1996, this was accomplished during a period in which lower private sector interest rates resulted in relatively low demand for Veterans Land Board housing and home improvement loans. If a spike in Senate Bill 43 evaluation workloads coincides with a period of high demand for Veterans Land Board loans, it would be difficult for Field Operations to complete all necessary appraisals within required time frames.

Recommendation:

The Asset Management Division should work with the Sunset Advisory Commission to develop a plan to reduce or eliminate spikes in workloads arising from Senate Bill 43 property evaluation requirements.

Management's Response:

The GLO will work with the Sunset Commission and the Legislature to develop a plan for creating a more even workload for evaluating properties as required by Senate Bill 43.

Section 6:

Integrate Initiatives to Assess Customer Satisfaction With the Strategic Planning Process

The General Land Office and Veterans Land Board have a proactive, comprehensive strategic planning process. Linking recent initiatives to assess customer satisfaction with strategic planning would improve an already well-developed process. Data on customer satisfaction would be particularly useful for the agency's internal/external assessment and performance measurement systems. Review of existing customer feedback systems indicates an opportunity to expand and formalize these processes for ongoing improvement.

The General Land Office and Veterans Land Board have a comprehensive internal/external assessment of environmental factors affecting the agencies. In addition, each division has well-developed action plans that tie to the strategic plan goals, objectives, and strategies. However, current efforts to assess customer satisfaction are less formal and vary from one division to another.

In reviewing program areas and support divisions, it appears that two have formal mechanisms to assess customer satisfaction, five have some feedback procedures in place, and two lack a mechanism to obtain customer feedback from a departmental perspective. In the latter case, it is primarily left up to individuals to obtain feedback on performance.

Customer satisfaction is a key element for continually assessing and improving overall agency performance. A well-developed, proactive assessment of customer satisfaction can provide an essential feedback loop for both strategic and operational planning. Feedback from customers, both external and internal, can also provide key data that can be used to prevent minor problems from becoming major ones.

Recommendation:

The General Land Office and Veterans Land Board should build upon recent initiatives to formally obtain customer feedback on its key business processes. Customer satisfaction measurements should also link to and provide the inputs to key elements of the strategic planning processes of internal/external assessment and performance measurement.

Management's Response:

The GLO/VLB appreciates the SAO's acknowledgment of our strategic planning process. Management is currently studying the best way to implement customer feedback mechanisms to cover all key business processes. The GLO/VLB will customize the mechanisms to fit the varied internal and external GLO/VLB users. The feedback received will be used in the planning process and for performance measurement.

Section 7:

Review Policies and Procedures for Value-Added Controls

Budget amendment procedures appear to require more sign-offs than necessary for more routine approvals. Policies for some more routine procedures require an unnecessary number of approvals. In some cases, however, approval procedures involving large dollar amounts or significant control areas were not consistently followed. In addition, document routing and processing procedures in some areas could be streamlined to reduce overall cycle time.

Section 7-A:

Budget Approval Process

Internal controls over the budget amendment process can require up to five approvals depending on the dollar amount involved. Generally, budget amendments require the signatures of the director, the program services officer, the deputy commissioner, the budget director, and the senior deputy commissioner (only if the amount is over

$1,000). This appears to be an unnecessary number of reviews, especially for more routine approvals.

While there appears to be an excessive number of approvals for more routine budget amendments, these procedures are not always consistently followed. Testing for compliance with budget amendment policies and procedures for fiscal year 1995 in one division revealed that the required signatures were missing on 21 out of 48 (43.8 percent) amendments, while another division lacked the required approvals in 71 out of 231 (30.7 percent) cases. One amendment for over $435,000 lacked the required senior deputy's approval. Also noted was an amendment for two salary increases totaling $7,266 which had only the budget director's signature.

The budget amendment process is intended to ensure that funds are authorized only for necessary and appropriate expenditures. However, additional layers of approval for routine transfers of funds add little value from a control perspective, and may tend to create gaps or omissions when senior management review and approval is both important and necessary. By clearly defining and delegating authority for more routine and low-risk approvals, upper management could free more of its time for more important tasks. This could also improve cycle time for standard decision-making.

Recommendations:

- The General Land Office and Veterans Land Board should review processes to identify procedures which could be eliminated or consolidated without sacrificing the effectiveness of internal controls.
- The General Land Office and Veterans Land Board should ensure that budget amendment procedures are followed.

Management's Responses:

In April 1996, the GLO "Request for Leave" form was changed from daily to weekly, and the number of approval signatures was reduced from three to one. By FY98 the GLO plans to automate several more forms for electronic routing. During this process, controls and levels of approval necessary will be reviewed. This automation will have built-in internal controls which will allow for the reduction of the number of approvals on each form. The GLO/VLB will review budget amendment policies and procedures to eliminate unnecessary reviews and ensure procedures are followed.

Section 7-B:
Work Flow Streamlining

Similar to the approval process, streamlining document processing and routing would increase efficiency and reduce cycle time. Given the diverse nature of the General Land Office's and Veterans Land Board's operating environment, there are a number of work processes that cross organizational boundaries. Improvements to work flow sequences could reduce overall processing time by eliminating non-value-added work steps.

One illustration of opportunities to improve cycle time is the procedure for the Permanent School Fund acquisition/disposition document routing. This process, which originates in the Asset Management Division's inventory section, includes the functions of permitting, surveying, and dispositions; as well as action taken by the Energy Resources Division. While each work area has important tasks to ensure the accuracy of Permanent School Fund land inventory records, each task is performed sequentially. The documents are then returned to the inventory section before being rerouted to the next section. It appears that some of these tasks could be performed in parallel as opposed to sequential processing to reduce queuing time between work areas.

While an in-depth review of cycle time efficiency was not performed during this audit, analysis of key business processes associated with state land inventories and other areas could yield significant improvement opportunities. In addition, since a number of these processes are undergoing or are scheduled to undergo automation enhancements, streamlining existing manual or paper driven processes would ideally occur prior to automation of these procedures.

Recommendation:

The General Land Office and Veterans Land Board should consider reviewing the cycle time efficiency of key business processes, especially those which entail "hand-offs" between sections and divisions. This effort could easily integrate with the agency's Quality Progression Process program, which provides training to staff on process analysis techniques.

Management's Response:

The GLO will continue to review key business processes to improve efficiency and reduce cycle time. As recommended, special consideration will be given to reviewing processes prior to automation.

Appendix 1:

Objective, Scope, and Methodology

Objective

The audit objective was to evaluate the management control systems of the General Land Office and Veterans Land Board. We determined that the control systems are providing reasonable assurance that the objectives of the General Land Office and Veterans Land Board will be met. We also identified strengths and opportunities for improvement and reviewed the management of resources.

Management controls are the policies, procedures, and processes used to carry out an organization's objectives. They should provide reasonable assurance that:

- Goals are met.
- Assets are safeguarded and efficiently used.
- Reliable data is reported.
- Laws and applicable regulations are complied with.

Management controls, no matter how well designed and operated, can only provide reasonable assurance that objectives will be achieved. Breakdowns can occur because of human error, circumvention of control by collusion, and the ability of management to override control systems.

Scope

The scope of this audit included consideration of the General Land Office and Veterans Land Board's overall management control systems: policy management, information management, performance management, and resource management.

Consideration of the General Land Office and Veterans Land Board's policy management system included a review of:

- Processes used to formulate, monitor, and evaluate strategic and operational plans
- Processes used to formulate, monitor, and revise budgets
- Processes used to prioritize and adjust workloads
- Processes and controls over the management of human resources
- Processes used to formulate and monitor policies and procedures

Consideration of the General Land Office and Veterans Land Board's information management systems included a review of:

- Processes for identifying, collecting, classifying, evaluating, maintaining, and updating information
- Existing management reports

- Timeliness, accuracy, and availability of information
- Security of information

Consideration of the General Land Office and Veterans Land Board's performance management systems included a review of:

- Processes used to identify, track, report on, and use performance measures
- Processes used to evaluate programs and to ensure quality products and services

Consideration of the General Land Office and Veterans Land Board's resource management systems included a review of:

- Processes used to control cash
- Revenue collection and identification
- Processes used to control loans and contracts, receivables, and inventories
- Processes for contracted oil spill clean-up services
- Controls over general computer equipment and computer applications

Methodology

Information collected to accomplish our objectives included the following:

- Agency policy, procedure, financial, and planning documents
- Staff and management interviews, surveys, and questionnaires
- Download of General Land Office Timekeeper database and expenditure database

Procedures, tests, and analysis performed included the following:

- Trend analysis of Veterans Land Board account balances, interest rates, delinquencies, and foreclosures
- Sampling to test controls over cash balances, receipts, and disbursements; loans and contracts; real property inventories; and surface land permitting
- Sampling to test compliance with internal policies and procedures
- Review of controls over automated information systems

Criteria used included the following:

- Applicable constitutional amendments, statutes, and bond covenants
- General Land Office and Veterans Land Board policies and procedures
- Financial Accounting Standards Board definitions
- General and specific criteria developed by the State Auditor's Office Inventory of Accountability Systems Project
- State Auditor's Office Project Manual System: The Methodology

- State Auditor’s Office Project Procedures Manual
- Other standards and criteria developed through secondary research sources

Other Information

Fieldwork was conducted from February 15, 1996, to June 15, 1996. The audit was conducted in accordance with applicable professional standards, including:

- Generally Accepted Government Auditing Standards
- Generally Accepted Auditing Standards

Review of the General Land Office and Veterans Land Board’s investments practices was performed and will be reported under Phase II of the State Auditor’s Office Review of Investment Practices audit.

The audit work was performed by the following members of the State Auditor's Office staff:

- John Young, MPA, (Project Manager)
- David Boedeker, CPA
- Dana Brown
- Sharon Lin, MPA
- Robert Shultz, CISA
- Charles R. Hrncir, CPA (Audit Manager)
- Deborah Kerr, Ph.D. (Audit Director)

Appendix 2.1

General Land Office and Veterans Land Board Profile

Mission

The mission of the General Land Office is to serve the schoolchildren, veterans, and all people of Texas by:

- Preserving their history
- Protecting their environment
- Expanding economic development
- Maximizing state revenue through innovative administration and prudent stewardship of state lands and resources

The goals of the General Land Office and Veterans Land Board are to:

- Enhance state assets and revenues by managing state-owned land
- Provide low interest loans to Texas veterans
- Improve and protect the Texas environment and promote the use of resources

Background

The General Land Office was established in 1836 to determine land ownership following Texas' independence from Mexico. The General Land Office is the management agency for over 20 million acres of state lands and associated mineral rights. Its responsibilities include oil, gas, and other resource development; improvement and protection of the environment; and support for the Texas Veterans Land Board programs. The Veterans Land Board was created in 1946 to make loans to Texas veterans for land purchases. In 1983, the Constitution was amended to permit the Veterans Land Board to make loans to veterans to purchase or improve homes in Texas.

The Oil Spill Prevention and Response Act of 1991 designated the General Land Office as the lead state agency for preventing and responding to oil spills in coastal waters. The General Land Office serves as the lead agency for the Coastal Coordination Council. The Coastal Coordination Council was created by the Legislature in 1991 to improve coordination of federal, state, and local governments in order to improve protection of the coast. The General Land Office is also responsible for a number of environmental initiatives, including sustainable energy, adopt-a-beach, alternative fuels, recycling, and border issues.

Operations

The Commissioner of the General Land Office is a state official elected by the voters of Texas to a four-year term. The Commissioner also serves as the Chair of the Veterans Land Board and other boards that are responsible for leasing state-owned lands. Two of the more important of these boards are the School Land Board and the Board for Lease of University Lands.

The General Land Office is organized into ten areas of responsibility. These are: Asset Management, Central Administration and Fiscal Management, Energy Resources, Field Operations, Human Resources and Special Programs, Information Systems, Legal Services, Oil Spill Prevention and Response, Resource Management, and the Veterans Land Board.

Appendix 2.2

Financial Information

For fiscal year 1996, the General Land Office and Veterans Land Board had legislative appropriations of $38,898,033. Of this amount, $12,228,825 was general revenue. General Revenue Fund consolidated receipts totaled $12,158,593. Other funds, including $9,290,499 from Veterans Land Program Administration Fund No. 522 and $3,220,252 in federal funds, totaled $14,341,788. There were 680.5 authorized FTEs for the General Land Office and Veterans Land Board in fiscal year 1996.

Financial information pertaining to the Veterans Land Board land, housing, and home improvement loan programs for fiscal year 1995 is detailed below.

Figure 2

Financial Information Pertaining to Loan Programs as of August 31, 1995

Land Loan Programs

Assets	Liabilities	Net Fund Balance	Bonds Payable	Net After Bonds Payable and Liabilities	Total Debt Service Requirements
$ 990,602,464	$ 20,298	$ 990,582,166	$ 660,080,075	$ 330,502,091	$1,134,180,398†

Housing and Home Improvement Loan Programs

Assets	Liabilities	Net Fund Balance	Bonds Payable	Net After Bonds Payable and Liabilities	Total Debt Service Requirements
$ 964,071,649	$ 5,466,451	$ 958,605,198	$ 808,680,074	$ 149,925,124	$1,728,125,075‡

Land, Housing, and Home Improvement Loan Programs Combined

Assets	Liabilities	Net Fund Balance	Bonds Payable	Net After Bonds Payable and Liabilities	Total Debt Service Requirements
$ 1,954,674,113	$ 5,486,749	$ 1,949,187,364	$ 1,468,760,149	$ 480,427,215	$ 2,862,305,473

Source: 1995 Annual Financial Report for the General Land Office and Veterans Land Board

†As of August 31, 1996, this amount includes principal and interest due through final bond maturity date.

‡As of August 31, 1995, this amount includes principal and interest due through final bond maturity date.

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