



# **Alaska Region Timber Sales Program Region 10**

**2018-FCOB-002**

**USDA Forest Service**

**Chief Financial Officer Organization**

**Audit & Assurance**

**Financial Compliance & Oversight Branch**

**August 18, 2020**



**File Code:** 1430; 2400

**Date:** August 18, 2020

**Subject:** Final Report – Alaska Region Timber Sales Program

**To:** Chris French, Deputy Chief, National Forest System  
David Schmid, Regional Forester, Alaska Region  
Earl Stewart, Forest Supervisor, Tongass National Forest

This letter is to notify you that the USDA Forest Service Financial Compliance & Oversight Branch has completed the final report for the audit over the Alaska Region timber sales program. The report is for your information and use and is for official use only.

We considered comments provided when preparing the final report. Comments to the draft report left no unresolved issues. Therefore, we do not require any additional comments. We will continue to monitor the implementation of the recommendations through August 2021 and may reach out to your staff in the future.

We appreciate the courtesies extended to the staff. If there are any questions, please contact me at [anthony.m.torres@usda.gov](mailto:anthony.m.torres@usda.gov) or (505) 563-7252.

Sincerely,

Digitally signed by  
ANTHONY TORRES  
Date: 2020.08.18 18:05:12  
-06'00'

ANTHONY M. TORRES  
Branch Chief, Financial Compliance & Oversight

Cc: Antoine Dixon, Michael Clanton, Erica Banegas, Juan Sedillo, Valarie Sanchez



# Contents

<b>Objective</b> .....	<b>2</b>
<b>Background</b> .....	<b>2</b>
<b>Summary</b> .....	<b>3</b>
<b>Big Thorne Stewardship Contract</b> .....	<b>3</b>
Cruise Plan.....	3
Appraisal .....	4
Designation by Prescription .....	6
<b>Kosciusko Good Neighbor Authority Agreement</b> .....	<b>8</b>
Potential Conflict of Interest.....	8
Cruising Software .....	10
Appraisal .....	11
Restoration Services .....	11
Financial Review .....	12
Unallowable Costs .....	12
Financial Reporting.....	12
Labor Cost Matching.....	13
<b>Conclusion</b> .....	<b>13</b>
<b>Recommendations</b> .....	<b>14</b>
<b>Management Comments</b> .....	<b>15</b>
<b>Our Response</b> .....	<b>15</b>
<b>Scope</b> .....	<b>16</b>
<b>Methodology</b> .....	<b>16</b>
<b>Report Release Instructions</b> .....	<b>17</b>

## Alaska Region Timber Sales Program

**PREPARED FOR:** USDA Forest Service, National Forest System  
1400 Independence Ave SW  
Washington, DC 20250  
ATTN: Chris French, Deputy Chief

USDA Forest Service, Alaska Region (R10)  
P.O. Box 21628  
Juneau, AK 99802-1628  
ATTN: David Schmid, Regional Forester

USDA Forest Service, Tongass National Forest  
648 Mission Street  
Ketchikan, AK 99901-6591  
ATTN: Earl Stewart, Forest Supervisor

**PREPARED BY:** USDA Forest Service  
Washington Office  
Chief Financial Officer Organization, Audit & Assurance  
Financial Compliance & Oversight Branch

**SUBJECT:** Final Report – Alaska Region Timber Sales Program Audit

**ADDRESS:** USDA Forest Service  
101B Sun Avenue NE  
Albuquerque, NM 87109



## OBJECTIVE

To determine whether the timber sale program was sufficiently managed by the USDA Forest Service Alaska Region and Tongass National Forest personnel.

## BACKGROUND

The USDA Forest Service (Forest Service) manages about 191 million acres of public land within 156 national forests. Located in Southeast Alaska is the Tongass National Forest (Tongass)<sup>1</sup>. The Tongass encompasses 16.7 million acres, of which 3.5% or 593 thousand acres was identified for timber production. Most of Southeast Alaska is undeveloped. The region is sparsely populated with an estimated 74,280 people living in more than 30 towns with only 4 of those towns having populations greater than 2,500. The communities of Southeast Alaska depend on the Tongass in various ways, including employment in wood products, commercial fishing, fish processing, recreation, tourism, mining, and mineral development.

The Tongass is managed by the Forest Supervisor through eight ranger districts and the Tongass headquarters (the Supervisor's Office (SO)). The Regional Forester, supported by staff in the Regional Office (RO), provides policy direction and oversight for national forests in the Alaska region. The Chief Financial Officer Organization, Financial Compliance & Oversight Branch audit team was requested to specifically review two timber sales prepared, awarded and administered by Tongass and State of Alaska (State) staff that also included RO oversight.

- **Big Thorne Stewardship Contract:** Awarded on September 30, 2014 to Viking Lumber Company, Inc. This included approximately 98 million board feet (MMBF) of proposed timber. The timber sale was located on Prince of Wales Island, within the boundaries of the Thorne Bay Ranger District of the Tongass.
- **Kosciusko Good Neighbor Authority (GNA) Agreement:** Awarded on May 8, 2017 to the State and the timber sale contract was awarded in September 2017 to Alcan Timber, Inc. This included approximately 30 MMBF of proposed timber. The timber sale was located on Kosciusko Island near Edna Bay. This Agreement was the first of its type within the region. The GNA was awarded to the State to manage the timber sale with Forest Service oversight. In addition, the State is required to perform restoration projects with the proceeds of the sale.

---

<sup>1</sup> Tongass – Most work on the Tongass is carried out by personnel on ranger districts rather than in the Forest Supervisor's headquarters (SO). In the report, unless the SO is specifically acknowledged, "Tongass" or "Forest" is referenced.

Forest Service timber sale activities have long been controversial because of concerns over ecological and financial costs associated with harvesting timber. In particular, the Forest Service has received multiple concerns with the Region's management of the timber sales program. For example, a 2016 timber program review that was conducted by Forest Service personnel from the Washington Office identified several areas for improvement in the administration of the region's timber program, which were documented in an Action Plan. The 2016 review identified specific concerns with cruising and appraisal of the Big Thorne Stewardship Contract that resulted in the Regional Forester requesting a subsequent independent review in 2017. This review identified additional findings. Due to continued public interest and the need for an additional independent review, the Washington Office Associate Deputy Chief, National Forest Systems, requested an audit of the Big Thorne Stewardship Contract and the Kosciusko GNA agreement.

## **SUMMARY**

The timber sales program was not sufficiently managed. Specifically, the timber sale cruising, appraisal, sale preparation, and contracting program for the Big Thorne Stewardship Contract and Kosciusko Good Neighbor Authority Agreement were not always managed in accordance with the terms of the agreements and Forest Service policy. As a result, timber sale methodology and calculation errors created an approximate \$2 million contract modification adjustment for the Big Thorne Stewardship Contract to reconcile inaccuracies. Similarly, the Kosciusko Good Neighbor Authority Agreement administration and oversight were not sufficient to prevent a potential conflict of interest, inaccurate or missing information and financial management discrepancies.

## **BIG THORNE STEWARDSHIP CONTRACT**

The RO and Tongass personnel were not aligned in decisions that affected the Big Thorne Stewardship Contract. This included methodology and calculation variances between the offices that contributed to an inefficient timber program and ultimately, potential litigation from the contractor awarded this timber sale. This should be of significant concern to the Forest Service as the stewardship contracts require potential buyers to bid on the timber sale. If the timber sale numbers are not accurate, the Forest Service may encounter skeptical contractors in future timber sales contracts.

## **Cruise Plan**

The Tongass personnel cruised the timber sale site without an approved cruise plan. According to a Forest Service official, the process was not strictly followed because to do so would mean not meeting the deadline to complete the sale. FSM 2400, Chapter 2440, Section 2442.2, states each timber sale is required to



have an approved cruise plan *before* cruising has started for every timber sale expected to have a value in excess of \$5,000. However, cruising for the Big Thorne sale was completed two months before the approved plan was signed. Specifically, the cruise was completed on June 25, 2013 while the cruise plan was approved on August 21, 2013.

In addition, the Tongass personnel made errors that resulted in an overstatement of the cruised timber volume. For example, they cruised all trees on every plot and post stratified or combined all cruises into one. Forest Service Handbook (FSH) 2409.12, 41.4.5, states that post stratifying is not allowed because stratification after the field samples are taken does not permit optimum allocation of samples by strata and introduces bias in the estimate.

Moreover, we were informed that the cruising software did not have enough space to handle the large file developed from cruising the Big Thorne sale. The Tongass personnel decided to divide the cruise into five separate cruises, run them separately through the cruising software, and combine the final results. This inaccurate cruising methodology resulted in more volume than could actually be accounted. Although the RO questioned the results, the Tongass personnel did not have enough time to figure out what was wrong or determine how to correct the issue.

Also, the FSH was not followed to develop the final cruise which should have accounted for hidden defects, percent recoverable in utility, and cull and breakage factors. According to a 2017 prior review, the cruise plan developed in 2013 followed the FSH. However, the plan was not followed in implementing the final 2013 cruise. For example, the hidden defect percentage for Hemlock should have been 26%, but was recorded in the final cruise as 19%. Overall, the prior review identified approximately 12 MMBF less sawtimber and utility volume due to using the incorrect FSH figures.

As a result, not processing the cruise in accordance with the FSH and cruising without an approved cruise plan allowed errors to occur which affected the accuracy of the data and remaining timber sale processes that used the cruise data for support, including the appraisal.

## Appraisal

We identified the need for enhanced appraisal controls. According to FSH 2409.22, Chapter 100.120, prior to advertisement, any timber sale greater than or equal to 1 MMBF must have an Appraisal of Record approved by the Regional Office Forest Management. The audit team recognized that the Big Thorne timber sale was offered twice. The 2013 timber sale was "pulled" from the award process at the last minute because of a National Environmental Policy Act (NEPA) deficiency. Once the NEPA deficiency was corrected, the sale was reoffered in 2014. In addition, the appraisal responsibility for the Big Thorne



changed from the RO to the Tongass SO. The SO appraisal was ultimately used in the contract award.

Historically, an Appraisal Specialist worked with different Ranger Districts to develop draft appraisals. Once a draft appraisal was completed by the Appraisal Specialist, it was sent to the RO for final approval. The RO would review and approve the draft appraisal and subsequently issue an AOR. However, the Appraisal Specialist retired from the Forest Service in 2014. That same year, a SO official questioned the use of the existing appraisal process. For example, the official expressed concern that Profit and Risk (P&R) calculations for all timber sales should not be the same. The P&R weighted average factors for consideration include market fluctuations, capital investment requirements, uncertain timber supply, probable lawsuits, defective timber, and difficult logging.

Due to the P&R set by the RO, which is required in FSM 2420.43, the SO official asserted that it was difficult to use the same P&R for all timber sales. Specifically, a timber sale cannot be advertised if it has a negative timber sale value to the Forest Service. Further, the SO official stated that if the P&R is set too high, it is impossible to have a timber sale with a positive value. As a result, the SO wanted to calculate a lower P&R for the Big Thorne sale, but did not have the authority to change the P&R set by the RO.

Therefore, the SO created a draft *Leader's Intent* document. The purpose of the draft *Leader's Intent* was to increase transparency, credibility and accountability for timber sales and stewardship contract residual value appraisals. The document specifically requested an amendment to, "Forest Service Handbook 2409.22 by 01 July 2014 to clarify that the Forest Supervisor/District Ranger is responsible for developing the AOR. Line Officers will document rationale for all costs used in the AOR. R10 Director of Timber Management may review AOR's to ensure approved methodology and deducted cost ranges are used."

The RO, at the request of the Tongass Forest Supervisor, arranged for a Washington Office Functional Assistance Trip (FAT) to review several aspects of the Region's timber sale appraisal program. One of these aspects was to determine which office should issue the AOR. The FAT occurred in August 2014 and the report was issued in December 2014. The report recommended that the Tongass SO issue the final AOR, but with a review from the RO to ensure appraisals complied with policies and procedures.

The Tongass submitted the draft *Leader's Intent* document to the Regional Forester in 2014. The RO subsequently issued an interim direction that stated the draft *Leader's Intent* document would not be finalized "until we have resolved the procedural and foundational components for the R10 Forest Management Handbook and Supplement updates." The procedural and foundational components that the Regional Forester set forth were never completed and the recommendations of the draft *Leader's Intent* were never included into the FSH. Instead, in response to concerns about sale specific factors affecting P&R, the RO developed a P&R estimator that was based on sale-specific risk factors. The



P&R estimator allowed the appraiser the flexibility of calculating P&R by either not making a change, or increasing or decreasing the risk factors by one percent based on sale specific criteria.

The Tongass appraiser subsequently used the P&R estimator for the 2014 appraisal and their results came out lower than the RO's 2013 AOR. Three of 10 P&R risk factors were adjusted down by the SO; specifically, the Designation by Prescription (D x Pre), current competition on large timber sales, and blowdown/salvage/high defect P&R risk factors. However, the adjustment down did not account for all variables. For example, the Big Thorne sale has a 31.8% scaling defect. According to a prior review, this should have led to an upward P&R adjustment. Ultimately, the RO recognized that the P&R estimator was not being used as intended.

Table 1 illustrates the 2013 and 2014 P&R variances by tree species, including the Sitka Spruce (SS), Western Hemlock (HEM), Alaskan Yellow Cedar (AYC), and Western Red Cedar (WRC), and the weighted average P&Rs for the two years.

**Table 1. Comparison of 2013 and 2014 P&R Percentages**

Effective P&R						
Fiscal Year	Tree Species				Weighted Average	Issued AOR
	SS	HEM	AYC	WRC		
2013	13.97%	12.53%	12.28%	13.22%	12.91%	RO
2014	11.82%	11.28%	10.71%	12.28%	11.54%	SO

The lowered P&R incorrectly resulted in a higher appraisal value for the Big Thorne sale, making it possible for a positive value and ultimately helped the Tongass and Region obtain its annual timber sale goal.

Further, the Tongass appraiser determined the contractor's haul time to be less in their AOR when compared to the RO AOR. Specifically, the SO calculated the haul time to be a half hour less, which affected the final appraisal because it did not include the wait time at the mill. Our analysis on the haul time came within one tenth of the time calculated in the 2013 AOR. The omission of the half hour of delay time in the 2014 AOR was ultimately validated and corrected as a result of the 2017 independent review. Subsequent contract modification was approved to correct both volume and value inconsistencies.

### Designation by Prescription

The Tongass implementation of D x Pre for the Big Thorne sale was not fully understood or implemented; however, the Tongass did subsequently make improvements. D x Pre is a method of designating trees for removal by describing the desired end result of the treatment. For example, the Big Thorne timber sale used D x Pre to harvest either 50 percent or 25 percent of the basal

area of different tree species in designated units to achieve specified silviculture goals. The quantity of products removed is determined post-harvest for payment purposes. According to FSM 2400, Chapter 2440, Section 2441.04c.1, it is the responsibility of the Forest Supervisor to “Ensure the District Ranger has available staff or access to qualified employees with the necessary skills and certifications to administer timber sales and stewardship contracts designating timber by description or by prescription.”

In D x Pre, the contractor selects the trees to be cut or left to meet objectives contained in the silvicultural prescriptions. This type of tree designation requires close on-the-ground monitoring by the Forest Service and is best suited with sales where the timber is uniform.

While the Big Thorne timber sale site was not uniform, the Regional Forester submitted a letter to the Forest Supervisor approving the use of D x Pre in July 2013. This was the largest sale to use D x Pre in the Region. Within the letter, the Regional Forester emphasized oversight needed to implement D x Pre.

For example, the Tongass was required to:

- Analyze stands to determine the ones where D x Pre would be the optimum designation method, and the stands where marking trees is not necessary to meet stand objectives.
- Commit additional contract administration personnel to properly implement the prescription and achieve desired stand conditions.
- Implement more frequent inspections, as compared to a regular timber sale to assure attainment of the objectives and requirements of the prescription.

According to the 2016 WO review, multiple findings were identified regarding the Tongass’ use of D x Pre. For example, the purchaser tended to remove less than what was prescribed by species, in favor of removing larger diameter and more valuable species groups, such as western red cedar and spruce. Also, there were concerns that the inspection process was not well-defined and the sale administration team relied heavily on contractor self-inspections.

However, during our review we identified the sale administration team was working towards ensuring the inspection process is effective by maintaining a record of every tree that is being cut by the purchaser in the Big Thorne. This record was based on the basal area of each species of trees within each plot. A spreadsheet was being maintained that includes each tree’s number, diameter, and the individual’s initials of the person who cut the tree written on the tree stump.

During a harvest inspection, a sample was taken to ensure the information of each tree had been recorded. From 2015 to 2018, based on inspection reports we received, there was approximately 511 inspections performed. The inspections have not identified losses in accountability on any tree harvested for sale. An experienced SO official stated that the contractor is cutting according to



prescription and the contractor is cutting every decent hemlock in the Forest. Some units have almost nothing but hemlock; these units are being significantly logged.

Additionally, we were informed that the less desirable species HEM was not being cut, as opposed to the more valuable species. However, during our site visit to the purchasers scaling yard, we observed HEM that was cut from the Big Thorne sale. We also observed HEM being harvested at the helicopter drop off location at the Big Thorne site. Lastly, we verified that HEM was cut substantially compared to the other species, based on our review of the scaling reports. Table 2 illustrates the amount of HEM scaled compared to the other species.

**Table 2: FY 2015 – 2017 Scaled Volume by Species**

Species	Volume by MMBF
Hemlock	39
Red Cedar	19
Sitka Spruce	19
Yellow Cedar	6
Total	83

D x Pre caused stress for multiple Tongass employees. According to an SO official, D x Pre has not been used since the Big Thorne sale, although it is an acceptable method to use and offers some benefits for the Forest Service to issue a sale. For example, according to some Forest employees, it is the safest, least time consuming, and least expensive harvest method that can be used. It is also a very good method to accomplish silvicultural objectives.

However, it appears D x Pre was not effectively implemented for the Big Thorne sale due to the urgency to meet the Forest Service timber sale goal. Going forward, improvements will be needed when implementing D x Pre.

## **KOSCIUSKO GOOD NEIGHBOR AUTHORITY AGREEMENT**

Use of GNA is relatively new to the Forest Service. Further, this was the first time this authority was used in the Alaska Region for a timber sale. We found that the Kosciusko GNA Agreement administration and oversight were not sufficient to prevent a potential conflict of interest, inaccurate or missing information and financial management discrepancies.

### **Potential Conflict of Interest**

We found that the State did not sufficiently address a potential conflict of interest from occurring in this agreement. According to 2 CFR 200.318, the non-Federal

entity (in this case, the State) must maintain written standards of conduct covering conflicts of interest and governing the actions of its employees engaged in the selection, award and administration of contracts. No employee, officer, or agent may participate in the selection, award, or administration of a contract supported by a Federal award if he or she has a real or apparent conflict of interest. Such a conflict of interest would arise when the employee, officer, or agent, any member of his or her immediate family, his or her partner, or an organization which employs or is about to employ any of the parties indicated herein, has a financial or other interest in or a tangible personal benefit from a firm considered for a contract.

The State had an ethics officer along with ethics policies and standards. State staff also take ethics training and are required annually to complete an ethics notice and/or determination for potential conflicts. Although the State has ethics policies and standards in place, they did not address past employees or contractors.

We identified that the contractor who was involved in supporting the pre-award phase of the GNA timber sale by developing the feasibility and final appraisal for the State was also awarded the contract to perform the timber sale layout for Alcan Timber Inc., the purchaser of the timber sale. In July 2017, before agreeing to develop the final appraisal, the contractor sent an email to the State requesting written acknowledgement that his involvement with working on the appraisal would not produce a conflict of interest or prevent future involvement in the timber sale after it is sold.

We acknowledge the State's Ethics official offered conditions when conducting future work with a successful purchaser. Specifically, the official stated, the contractor "should not solicit employment by bidding parties or form an agreement for services until the contract has been awarded."

However, prior to the Ethics officer's response, the contractor referenced the purchaser as someone the contractor communicated with in the development of the February 2017 feasibility appraisal. Further, after the Ethics officer's statement, the purchaser's September 2017 proposal referenced the contractor to perform the timber sale layout for their company. Later that month, the purchaser was awarded the contract.

We attempted to obtain the contract from the purchaser and the contractor to determine whether the agreement was signed before the award of the Kosciusko sale, but *both parties declined* to provide the document to us. In meetings with State and Forest Service officials, they mentioned to us that there were not many experienced contractors to do the timber sale layout work or appraisal.

Based on the above details and the withholding of information, the risk of a conflict of interest was high. Further, despite the State acting on the potential conflict of interest, existing State ethics internal controls were not sufficient to adequately address the Federal conflict of interest requirements. As a result of inadequate controls, a person with privileged details of the Kosciusko sale had



the ability to gain financially by potentially agreeing to work for the purchaser prior to the sale being awarded.

## **Cruising Software**

We verified a concern presented to us that the cruising software used for the Kosciusko sale was not calculating the correct timber volume. According to the Forest Service agreement, the State was responsible for the cruise development, implementation, and volume determination. The cruising software used by the State was called Kruzer. We verified that the software did not calculate cruised board feet accurately. By comparing the cruising report measurements to the Log Scaling Handbook, we found 1,143 out of 2,443, or 47% of the total sampled logs, were inaccurately calculated by the software. Specifically, we identified that all logs over 9 inches in diameter, with the exception of 12-inch diameter logs, were under calculated ranging from 10 to 40 board feet. At a minimum, 12,300 board feet were not included in the total volume calculation.

Since we only reviewed the logs that were sampled to develop the extrapolated total cruised volume, the actual board feet not included should be higher. According to a SO official, they identified this issue once they received the cruise report. However, once the individual reported their concern to the State, the request for proposal was already out for bid and a State official stated it was too late to make any changes.

Kruzer was never used before for a timber sale by either the State or the SO. The State primarily uses a software called Atterbury SuperACE, which was agreed upon by both State and Forest Service officials as being reliable. According to the State, Kruzer was recommended by the Tongass Advisory Committee and used to inventory young growth timber for the Forest Service Tongass Young Growth Inventory Project. According to a State official, since their team was familiar with using Kruzer for the prior agreement and due to time constraints, they continued to use it for the Kosciusko sale. But, according to the State, there was a vigorous discussion with the SO regarding the software to use. According to the State, they agreed to use Kruzer in the spirit of learning to work together with the Forest Service to create a team environment.

The State acknowledged an issue with Kruzer as a result of conducting an independent review of the software. The independent verifier evaluated the software and also verified that the software was not estimating timber volume correctly.

According to both the State and RO, Kruzer was not used on a subsequent GNA timber sale offer as a result of challenges discovered.

Both the State and the Forest Service did not ensure the cruising software was reliable and could accurately calculate timber volume. As a result, potential bidders and the winning purchaser did not have accurate information on how much timber was available for bidding.

## Appraisal

Initially, we found that the appraisal and request for proposals did not match the cruised timber volume, as required by the Forest Service Kosciusko agreement timber sale contract checklist, Appendix E. However, after further communication with the State and analysis we agree that the Agreement allows the State to adjust appraisal volumes since they were able to provide documentation that shows how they calculated the difference in timber volumes.

Although the Agreement allowed the State to adjust the appraisal volume, we found that the adjusted volume didn't reflect the allowable 8" merchantable end log diameter that's stated in the contract with the purchaser. Specifically, Table 3 illustrates the timber volume total variances documented in the cruise, appraisal, request for proposals, and contract along with the end log diameter used.

**Table 3: Comparison of Timber Volume Totals**

Document	End Log Diameter	Volume Total by MMBF
Cruise	5"	32
Appraisal	6"	30
Request for Proposals	6"	30
Contract	8"	27*

\*Volume not included in contract since it's a scaled timber sale, but according to State calculations 8" end diameter logs would equal approximately 27 MMBF.

Since the State appraised and advertised the timber sale volume using the 6" end log diameter, the contract with the purchaser was inaccurate. The State did not have any further comment based on the discrepancy. Due to not effectively reviewing the contract before issuing it, the State did not ensure the correct end log diameter was documented in the contract.

## Restoration Services

Specific restoration services were not included within the initial Kosciusko GNA supplemental agreement with the State, but corrective actions occurred during the time of this audit. According to the Farm Bill that authorizes GNA use, it encourages the Forest Service to enter into GNA agreements with State governments to carry out authorized forest, rangeland, and watershed restoration services on and off of National Forest System lands.



Although the Kosciusko GNA supplemental agreement states that it is a cooperative effort between the Forest Service and State to perform restoration services, it does not specifically identify what services should be performed, as required in the GNA Master agreement. According to a Forest Service official, this was the first GNA agreement developed through the RO. Further, the Forest Service official stated the error was one of the lessons learned from using this type of agreement. Further, they mentioned that restoration services were always intended to be included in the agreement, but later when services were identified.

To address this issue, the Forest Service conducted a field visit to the Kosciusko Island in April 2018 to determine potential restoration services. Restoration services identified included trout creek stream restoration, buggy creek bridges for aquatic organism passage, and buggy creek road hardened crossings. These restoration services cost estimates ranged from \$10,000 to \$400,000.

According to an SO official, they are developing a modification to the agreement to specifically state what restoration services will be performed. As a result of not including specific restoration services in the initial supplemental agreement, it gave the public the impression that no restoration would be performed, and risked offering insufficient time to conduct restoration services, since they were not identified at the start of the agreement.

## Financial Review

### Unallowable Costs

Costs were reimbursed for expenditures that did not occur. According to 2 CFR 200.309, a non-Federal entity may charge to the Federal award only allowable costs incurred during the period of performance. However, we identified that the State requested reimbursement for indirect charges that were not incurred. Specifically, the State's second reimbursement submission dated in February 2018 requested \$3,250.32 in indirect costs.

It appears the State self-identified the problem with the third reimbursement submission dated in May 2018, and reduced their requested reimbursement amount by \$1,961.58. However, that reduction was not enough. Specifically, the State received \$11,013.39 in indirect costs, but should have only received \$10,157.93, a difference of \$855.46 in unallowable indirect costs. According to the State, there was a lapse in experience due to an unexpected employee death which caused the unallowable costs to be recorded for reimbursement. Because oversight was not sufficient, the Forest Service needs to recover overpayment.

### Financial Reporting

We found that the State did not meet the Federal Financial Reporting requirement. According to the agreement, "A Federal Financial Report, form SF-425 (and Federal Financial Report Attachment, SF-425A, if required for

reporting multiple awards), must be submitted quarterly. These reports are due 30 days after the reporting period ending March 31, June 30, September 30, and December 31.”

Since the agreement was issued in May 2017, the State did not submit four of the five required quarterly financial reports. The State did not start meeting the requirement until August 2018, approximately one year since the first financial report was due. According to the State and similar to the prior section, there was a lapse in experience due to an unexpected employee’s death that caused the State to not submit their required financial reports. As a result, the Forest Service did not have the necessary financial information to appropriately oversee the agreement.

### **Labor Cost Matching**

We found that the State is exceeding their budgeted salaries/labor cost match category. According to 2 CFR 200.308, “Recipients are required to report deviations from budget or project scope or objective, and request prior approvals from Federal awarding agencies for budget and program plan revisions.”

According to the agreed upon financial plan, the State budgeted \$11,060.00 for salary/labor match for the life of the project. However, the State submitted \$13,952.76 in salary/labor costs towards the match resulting in costs of \$2,892.76 or 26% over budget.

As a result, the State is not in compliance with the federal regulation and the Forest Service needs to offer more effective oversight to assist the State in not exceeding their salary/labor cost match budget.

## **CONCLUSION**

The identified issues occurred because the timber sales program was not sufficiently managed, in part, due to the pressure to meet timber sales goals. Specifically, the average annual timber sales goal in the Region between Fiscal Years (FY) 2013 – 2017 was approximately 70 MMBF. Only in FY 2014 did the RO meet their timber sales goal due to the Big Thorne sale. Both sales just met their fiscal year deadline by entering into a contract by September 2014 and 2017 respectively, which is the last month of the fiscal year. According to SO and State officials, they felt the pressure to issue the sales within the FY’s to meet the performance goals. Overall, the issues we identified led to rushed advertised timber sales that included multiple errors. For example, the Big Thorne Stewardship Contract purchaser planned on taking the Forest Service to court due to the sale valuation issues.

This resulted in the Forest Service negotiating a settlement with the purchaser based on the results of the 2017 independent survey. The contract modification resulted in a decrease in overall sale value of approximately \$2 million, created a



surplus cash balance in the purchasers account and resulted in a \$700,000 refund to the purchaser of his surplus deposits.

## RECOMMENDATIONS

1. To ensure the Alaska Regional Office and the State of Alaska achieve better efficient and effective oversight of timber sales to help meet timber sale goals going forward, we recommend the Deputy Chief, National Forest System direct the following to the Alaska Region and Tongass National Forest:
  - A. Enhance Regional policy to address line officer responsibility for every section of the timber sales program, including but not limited to, the cruising, appraisal, sale preparation, and contracting program. This should include responsibility for Forest Service managed timber sales and good neighbor authority agreement timber sales.
  - B. Ensure the cruise plan is approved and complete before performing the cruise.
  - C. Ensure the Appraisal of Record review and approval is efficiently and effectively managed by the Regional Office.
  - D. Improve oversight and use of the Designation by Prescription cruising method for timber sales going forward.
2. We recommend the Regional Forester, Alaska Region, work with the State of Alaska, through the Good Neighbor Authority Agreement to:
  - A. Modify the Kosciusko Good Neighbor Authority agreement to include needed restoration projects to cover the anticipated funds receipts from the timber sales.
  - B. Recover the remaining \$855.46 in indirect costs.
  - C. Strengthen internal controls to address potential conflict of interests from occurring.
  - D. Use agreed upon, tested and reliable cruising software for future timber sale agreements with the Forest Service.
  - E. Revise the timber sale contract from 8" to 6" merchantable sawlogs to align with appraisal and request for proposals.
  - F. Ensure compliance with 2 CFR 200 federal requirements to include:
    1. Financial management standards are followed when requesting reimbursement.
    2. Financial Reports are submitted on a quarterly basis.
    3. Request cost match budget revision to financial plan.

## MANAGEMENT COMMENTS

Management provided the audit team initial comments and participated in an additional discussion to address areas that required additional clarification. Ultimately, management, the State, and the audit team agreed to the factual accuracy of the report and management agreed with the recommendations outlined in this report and will incorporate them into an Action Plan.

## OUR RESPONSE

We consider management's comments responsive to our recommendations. Management's comments included both the RO's and the State's remarks. Both offered additional documentation, clarifying comments, explanations and proposed more transparent wording to improve the understanding of some issues. We recognize that management will incorporate all the recommendations into an Action Plan.



## SCOPE

The Financial Compliance & Oversight Branch conducted an audit of the Alaska Region Timber Sales Program from July through May 2019. This audit includes the Big Thorne Stewardship Contract and the Kosciusko GNA Agreement. The Kosciusko GNA Supplemental Agreement is the first of its type within the RO and no timber has been harvested to date. Therefore, we did not review the Kosciusko GNA sale harvest post-sale operations. We performed a site visit of Southeast Alaska during August 20 - 31, 2018, including the RO (Juneau), State (Anchorage), and Forest Service offices (Ketchikan, Thorne Bay, Petersburg and Craig).

## METHODOLOGY

To accomplish the objective, we:

- Held discussions with key officials;
- Reviewed applicable laws, rules, and regulations;
- Reviewed Forest Service policy and procedures;
- Reviewed system generated financial accounting reports;
- Compared actual expenditures to budgeted amounts;
- Reviewed and analyzed pre and post-sale documentation; and
- Reviewed prior reports.

We conducted this performance audit using generally accepted Government auditing standards as a best practice. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Accordingly, we assessed internal controls and compliance with laws and regulations necessary to satisfy the audit objective.

Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. We did not rely on computer-processed data to satisfy our objective.

## REPORT RELEASE INSTRUCTIONS

The information contained in this report may be proprietary. It is not practical to identify all proprietary data elements during the review process. The USDA Forest Service will make a determination on proprietary information in the event of an external request to obtain this report. Consider the restrictions of 18 U.S.C. 1905 before releasing this information to the public.

Do not use the information contained in this report for purposes other than action on the subject of this report without first discussing its applicability with the auditor.