

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



**ANNUAL REPORT 2007**



# United States Department of the Interior

OFFICE OF INSPECTOR GENERAL  
Washington, DC 20240

NOV 09 2007

## Memorandum

To: Special Trustee for American Indians

From: Kimberly Elmore *Kimberly Elmore*  
Acting Assistant Inspector General for Audits

Subject: Independent Auditors' Report on the Tribal and Other Trust Funds and Individual Indian Monies Trust Funds Financial Statements for FY2007 and FY2006 (Report No. Q-IN-OST-0003-2007)

## ***INTRODUCTION***

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This memorandum transmits the KPMG LLP's (KPMG) auditors' report of the Office of the Special Trustee for American Indians (OST) financial statements for fiscal years (FYs) 2007 and 2006. The OST financial report contains separate financial statements and notes for Tribal and Other Trust Funds (Tribal) and Individual Indian Monies (IIM) trust funds.

The American Indian Trust Fund Management Reform Act of 1994 requires an audit of the Tribal and IIM financial statements. Under a contract issued by OST and monitored by the Office of the Inspector General (OIG), KPMG, an independent public accounting firm, performed an audit of the OST FY2007 and FY2006 financial statements. The contract required that the audit be performed in accordance with auditing standards generally accepted in the United States of America and the "Government Auditing Standards" issued by the Comptroller General of the United States.

## ***RESULTS OF INDEPENDENT AUDIT***

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In its audit report, dated November 9, 2007, KPMG issued qualified opinions on the Trust Funds financial statements because certain parties for whom OST holds assets in trust:

- have filed a class action lawsuit for an accounting of the individuals' trust funds, which may or may not lead to claims against the United States Government;
- do not agree with the balances recorded by OST and/or have requested an accounting of their trust funds; or
- have filed or are expected to file claims against the United States Government.

In addition, inadequacies in certain Department of the Interior trust-related systems and processes, which provide required trust financial information to OST, made it impractical to extend auditing procedures sufficiently to satisfy auditors as to the fairness of trust fund balances. KPMG identified two significant deficiencies in internal controls over financial reporting, one of which was

considered a material weakness: unresolved trust funds financial reporting matters from prior periods. KPMG found no instances where OST did not comply with laws and regulations.

## ***EVALUATION OF KPMG AUDIT PERFORMANCE***

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To fulfill our monitoring responsibilities, the OIG:

- reviewed KPMG's approach and planning of the audit;
- evaluated the qualifications and independence of the auditors;
- monitored the progress of the audit at key points;
- coordinated periodic meetings with OST management to discuss audit progress, findings, and recommendations;
- reviewed and accepted KPMG's audit report; and
- performed other procedures we deemed necessary.

KPMG is responsible for the attached auditors' report dated November 9, 2007, and the conclusions expressed. We do not express an opinion on OST financial statements, internal controls, or compliance with laws and regulations.

## ***REPORT DISTRIBUTION***

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The legislation, as amended, creating the OIG requires semiannual reporting to Congress on all audit reports issued, actions taken to implement audit recommendations, and recommendations that have not been implemented. Therefore, we will include the information in the attachment in our next semiannual report. The distribution of the report is not restricted, and copies are available for public inspection.

The OIG appreciates the courtesies and cooperation extended to KPMG and our staff during this audit. If you have any questions regarding the report, please contact me at 202-208-5512.

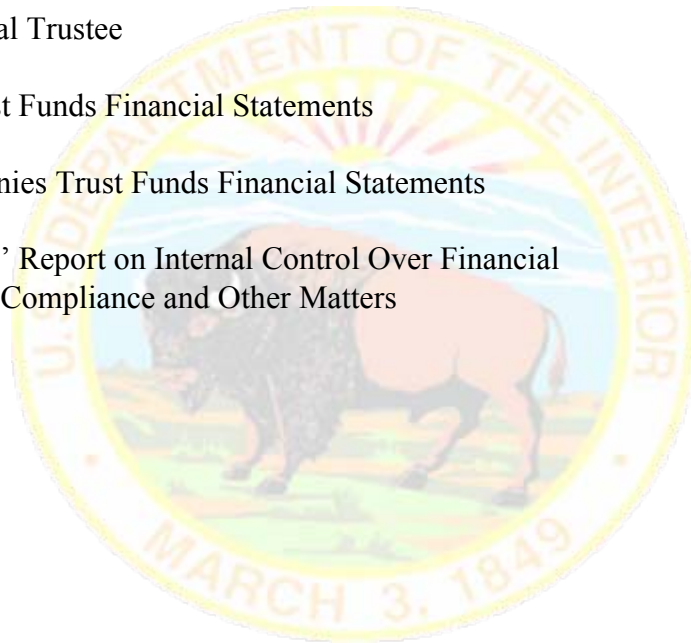
Attachment

cc: Principal Deputy Special Trustee  
Director, Office of Trust Review and Audit, Office of Special Trustee  
Program Analysis Officer, Office of Special Trustee  
Director, Office of Financial Management  
Associate Director, Office of Financial Management  
Audit Liaison Officer, Office of Financial Management  
Focus Group Leader, Internal Control and Audit Follow-up, Office of Financial  
Management

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# Letter from the Special Trustee

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I am pleased to present the FY 2007 Tribal and Other Trust Funds and Individual Indian Monies Trust Funds audited financial statements which are managed by the Office of the Special Trustee for American Indians. This letter provides information about what our office has accomplished in the fulfillment of the Department of the Interior's fiduciary responsibilities to American Indians, Alaska Natives, and tribes.

At OST, our day-to-day work has been guided by our Indian trust management mission statement – “to perform our fiduciary trust responsibilities to American Indian tribes, individual Indians, and Alaska Natives by incorporating a beneficiary focus and beneficiary participation while providing effective, competent, stewardship and management of trust assets.”

Interior's Comprehensive Trust Management Plan (CTM) has guided and described the vision, goals, and objectives of the fiduciary trust management and operations of the Indian trust for all bureaus and offices within Interior. Achieving the goals in the plan have resulted in enhanced beneficiary services, reliable ownership information, and quality administrative services; improved management of trust fund assets and increased support for Indian self-governance and self-determination.

OST continues to fulfill Indian fiduciary trust responsibilities by the continued implementation of the following strategies:

**Improve Indian Fiduciary Trust Beneficiary Services** by continuing our efforts to provide timely, accurate account performance statements and convenient access to trust account services; communicating with beneficiaries and facilitating beneficiary involvement in trust management.

**Support Indian Self-Governance and Self-Determination** by continuing to foster expansion of self-governance compacts and self-determination contracts.

**Improve Indian Trust Ownership and Other Information** through prompt distribution of financial trust assets to heirs after the Office of Hearing and Appeals (OHA) renders probate decisions; and ensuring accuracy of data maintained in offices and accounting systems.

**Manage Trust Fund Assets for Timely and Productive Use** through managing and investing funds held on behalf of individual Indians and tribes; and, receipting, disbursing, and accounting for funds timely and accurately.

**Improve Management of Land and Natural Resource Assets** by obtaining appraisal information as needed on trust and restricted lands for tribal and individual Indian owners; and supporting the Indian Land Consolidation program to reduce the number of fractionated ownership interests in land.

These are some of OST's accomplishments during FY 2007 which further improved services to trust beneficiaries:

- Completed the conversion of all remaining BIA regions to reformed accounting, title, and asset management systems, and business processes. The new systems enable employees to track leasing activity, ownership and income distribution electronically to ensure more efficiency and accountability.
- Provided information to beneficiaries on their accounts and services available by producing and distributing booklets, brochures and statement inserts.
- Delivered over 700,000 quarterly performance statements to beneficiaries who own assets, providing such information as source of funds, encumbrance information (who is leasing their trust property, duration of the lease and payment terms), and a listing of the trust property they own. This information is in compliance with the *American Indian Trust Fund Management Reform Act of 1994* (1994 Act).
- Distributed tribal account statements on CD-ROM to all requesting tribes.
- Received over \$286 million through a centralized commercial lockbox which allowed for timely deposit.
- Distributed over 90% of the funds received through the lockbox into beneficiaries' accounts within 10 business days.
- Established Self-Governance and Self-Determination agreements with 38 tribes for real estate appraisals and Individual Indian beneficiary trust functions.
- Processed more than 8 million trust transactions in beneficiaries' accounts.

- Extended the first TrustNet connectivity to a Self-Governance tribe.
- Awarded the Cannon Financial Institute *Certified Indian Fiduciary Trust Specialist* designation to 42 OST employees.
- Collected 21,182 cubic feet of records, and indexed 12,545 cubic feet of records. Records are indexed and then stored, maintained and preserved at the American Indian Records Repository.
- Provided records management training to more than 1,000 BIA, OST and tribal employees.
- Provided Vital Records training to more than 1,250 BIA, OST and tribal employees.
- Reviewed 23% of BIA and OST offices to identify improvements needed in their Records Management Program.
- Supported the National Indian Programs Training Center, (NITPC), located in Albuquerque, NM, through funding, collaboration and partnership.
- Submitted to Congress a comprehensive report, detailing the significant progress of trust reform since 1994, entitled; *Restoring Trust: The Reformation of Indian Trust Management (1994-2006)*.
- Deployed a major redesign of the OST public website ([www.doi.gov/ost](http://www.doi.gov/ost)).
- Received 185,116 beneficiary contacts in the Trust Beneficiary Call Center and field offices this fiscal year for a total of 283,576 contacts since the inception of the TBCC in 2004. As a whole, Field Operations responded to 172,273 of the 185,116 inquiries within two business days or less for a "within two business days" response rate of 93.1%.
- Conducted or participated in 2,676 outreach events. At these events OST staff discussed such things as AIPRA education, oil and gas statements, WAUs, Direct Deposit, Lockbox, benefit of TAAMS conversion changes, asset statements, and OST's role as the primary source for beneficiary's questions and assistance.
- Received a report by the Government Accountability Office (GAO), stating that

although independent auditor's had made approximately 60 recommendations to OST based upon their audits from 1996 to 2000, by the end of FY 2007 only one remained: a historic material weakness which has been outstanding since before 1996.

We continue to face the challenge of continued Court-ordered disconnection from the Internet. In FY 2008, we will submit a proposal to the Court to restore the Internet connection. In spite of this technological challenge, OST has improved its ability to serve its trust beneficiaries.

In keeping with the CTM, OST will pursue the following during FY 2008:

- Continue to address the backlog of probates, as well as an ongoing regulatory update initiative to improve and streamline probate processes.
- Continue to address the backlog of appraisal requests on trust land, and improve the tracking of appraisal status.
- Extend access to reformed Interior Indian fiduciary information systems, and training opportunities, to tribes to support their operation of trust programs under PL 98-638 agreements.
- Expand training opportunities for Indian Affairs employees and tribes to provide effective program management.
- Implement a new Debit Card program, which will allow beneficiaries to receive their trust funds electronically, even if they do not have a bank account.

I hope you find this year's Annual Report informative and useful. We welcome your help, comments or suggestions for continued improvement. Any comments may be directed to our Trust Beneficiary Call Center at 1.888.678.6836.



Ross O. Swimmer  
Special Trustee for American Indians



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

Financial Statements

September 30, 2007 and 2006

(With Independent Auditors' Report Thereon)



**KPMG LLP**  
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PO Box 3990  
Albuquerque, NM 87190

## **Independent Auditors' Report on Financial Statements**

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

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

We have audited the accompanying statements of assets and trust fund balances – cash basis of the Tribal and Other Trust Funds managed by the U.S. Department of the Interior Office of the Special Trustee for American Indians (OST) as of September 30, 2007 and 2006, and the related statements of changes in trust fund balances – cash basis for the years then ended. These financial statements are the responsibility of management of OST. Our responsibility is to express an opinion on these financial statements based on our audits.

Except as discussed in the fourth paragraph of this report, we conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control over financial reporting of the Tribal and Other Trust Funds managed by OST. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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

It was not practicable to extend our auditing procedures sufficiently to satisfy ourselves as to the fairness of trust fund balances in the accompanying financial statements as of September 30, 2007 and 2006 due to certain parties for whom OST holds assets in trust disagreeing with balances recorded by OST and/or having requested an accounting of their trust funds, and certain of these parties have filed, or are expected to file, claims against the United States Government and due to inadequacies in certain Department of the Interior trust-related systems and processes, which provide required trust financial information to OST. Trust fund balances enter into the determination of financial position and changes in trust fund balances.

In our opinion, except for the effects on the financial statements of such adjustments, if any, as might have been determined to be necessary had we been able to apply adequate procedures to determine the fairness of trust fund balances and related changes in trust fund balances, as discussed in the preceding paragraph, the financial statements referred to in the first paragraph above present fairly, in all material respects, the financial position of the Tribal and Other Trust Funds managed by OST as of September 30, 2007 and



2006, and the changes in trust fund balances for the years then ended in conformity with the basis of accounting described in note 2.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 9, 2007 on our consideration of internal control over financial reporting and on our tests of Tribal and Other Trust Funds' compliance with certain provisions of laws, regulations, contracts and other matters of the Tribal and Other Trust Funds managed by OST. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in assessing the results of our audits.

KPMG LLP

November 9, 2007

**TRIBAL AND OTHER TRUST FUNDS  
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OFFICE OF THE SPECIAL TRUSTEE FOR AMERICAN INDIANS**

Statements of Assets and Trust Fund Balances – Cash Basis

September 30, 2007 and 2006

(In thousands)

<b>Assets</b>	<b>2007</b>	<b>2006</b>
Cash and cash equivalents (note 3)	\$ 602,502	503,399
Investments (note 4)	<u>2,278,157</u>	<u>2,417,827</u>
Total assets	<u><u>\$ 2,880,659</u></u>	<u><u>2,921,226</u></u>
<b>Trust Fund Balances</b>		
Held for Indian tribes (notes 6 and 8)	\$ 2,590,799	2,637,066
Held by the Department of the Interior and considered to be U.S. Government funds (note 6)	<u>289,860</u>	<u>284,160</u>
Total trust fund balances	<u><u>\$ 2,880,659</u></u>	<u><u>2,921,226</u></u>

See accompanying notes to financial statements.

**TRIBAL AND OTHER TRUST FUNDS  
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Statements of Changes in Trust Fund Balances – Cash Basis

Years ended September 30, 2007 and 2006

(In thousands)

	<b>2007</b>	<b>2006</b>
Increases:		
Receipts	\$ 339,159	338,896
Interest received on invested funds	139,315	121,566
Gain on disposition of investments, net	604	24
	479,078	460,486
Decreases:		
Disbursements to and on behalf of Indian tribes and other trust funds and withdrawal of trust funds by Indian tribes (note 8)	(519,645)	(421,078)
(Decrease) increase in trust fund balances, net	(40,567)	39,408
Trust fund balances, beginning of year	2,921,226	2,881,818
Trust fund balances, end of year (notes 6 and 8)	\$ 2,880,659	2,921,226

See accompanying notes to financial statements.

**TRIBAL AND OTHER TRUST FUNDS  
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Notes to Financial Statements

September 30, 2007 and 2006

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

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

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

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

The accompanying financial statements include only the financial assets held in trust by the Office of the Special Trustee for American Indians (OST) for trust beneficiaries and do not include: (i) the operating account balances of OST (e.g., Fund Balance with Treasury; Property, Plant, and Equipment; etc.) or (ii) other Indian trust assets, including but not limited to, Indian lands, buildings, or other non-financial assets managed by the United States Department of the Interior (the Department).

**The Reform Act** – The American Indian Trust Fund Management Reform Act of 1994 (Public Law 103-412) (the Reform Act) authorized the establishment of OST, which is headed by the Special Trustee for American Indians (Special Trustee) who reports to the Secretary. Under this legislation, the Special Trustee is responsible for oversight, reform, and coordination of the policies, procedures, systems, and practices used by various bureaus and offices of the Department, including but not limited to OST, the Bureau of Indian Affairs (BIA) (a component of Indian Affairs (IA)), the Minerals Management Service (MMS), and the Bureau of Land Management (BLM), in managing Indian trust assets.

**Office of the Special Trustee for American Indians** – Indian trust assets, including the Tribal and Other Trust Funds, are primarily managed under the delegated authority of OST and BIA. Management of Indian trust assets on behalf of the trust beneficiaries is dependent upon the processing of trust-related transactions within certain information systems of the Department, including but not limited to OST, BIA, MMS, and other Departmental bureaus and offices. BIA and

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Notes to Financial Statements

September 30, 2007 and 2006

other Departmental bureaus and offices are responsible for managing the natural resources located within the boundaries of Indian reservations and trust lands, as well as the processing of data regarding the ownership and leasing of Indian lands. The allocation of receipts and disbursements by OST to trust beneficiaries are significantly dependent and reliant upon the receipt of timely and accurate information derived from records maintained by BIA, MMS, and other Departmental bureaus and offices (see note 7).

**Regional Offices** – OST and BIA maintain staff at regional offices located throughout the United States.

**Agency and Field Offices** – OST and BIA maintain staff at agency and field offices located throughout the United States, which are generally located near the tribes and individual Indians served. OST and BIA personnel located at most of the agency and field offices perform various functions related to trust fund activities.

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

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

- **Tribal Trust Funds** – As of September 30, 2007 and 2006, approximately 1,800 and 1,450 accounts, respectively, comprise the Tribal Trust Funds, which totaled approximately \$2,590,799,000 and \$2,637,066,000, respectively.

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

- **Other Trust Funds** – Other Trust Funds are comprised of those funds classified as *Held by the Department of the Interior and considered to be U.S. Government funds* (see note 6). Other Trust Funds totaled approximately \$289,860,000 and \$284,160,000 as of September 30, 2007 and 2006, respectively.

Other Trust Funds realize receipts from a variety of sources including leases, rights-of-way, settlement of Indian claims, donations and bequests, and investment income.

**(c) Investment of Trust Funds**

Authorizing legislation and a substantial body of case law specify how Indian trust funds should be managed and which financial instruments constitute appropriate investments for Indian trust funds. The Tribal and Other Trust Funds are invested in U.S. Government securities, including U.S. Department of the Treasury (U.S. Treasury) issues, U.S. Government agency issues, and U.S. Government-sponsored entity issues.

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

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

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

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

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

**(c) *Investments***

Investment securities at September 30, 2007 and 2006 consist of U.S. Treasury issues, U.S. Government agency issues, and U.S. Government-sponsored entity issues. Investment securities are recorded at historical cost. Interest income is recognized when received.

The Tribal and Other Trust Funds' investments have a concentration in U.S. Government securities, as mandated by 25 USC 162.

**(d) *Receipts***

Receipts from various leasing activities, mineral royalties and sales of extracted minerals, timber and other forest products, fees and fines, and the granting of easements are generated from a variety of non-financial assets that are held in trust by the U.S. Government and managed by BIA and other Departmental bureaus and offices on behalf of tribes. Receipts on hand at the regional and agency offices, and/or in-transit at September 30, 2007 and 2006, if any, awaiting deposit to the U.S. Treasury, are not included in the accompanying financial statements.

Receipts also include payments from the U.S. Government for judgment awards and the settlement of claims.

**(e) *Disbursements***

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

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Public Law 103-412 specifically allows for the voluntary withdrawal of judgment awards and settlement of claims funds from the Tribal and Other Trust Funds. Except where prohibited by statute, an Indian tribe may submit a plan to withdraw some or all funds held in trust for the tribe in accordance with 25 CFR 1200.

**(f) Use of Estimates**

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

**(3) Cash and Cash Equivalents**

Cash equivalents of approximately \$601 million and \$503 million at September 30, 2007 and 2006, respectively, consist of overnight investments with the U.S. Treasury.

**(4) Investments**

The historical cost, gross unrealized holding gains, gross unrealized holding losses, and fair value of investment securities by major class of security at September 30 were as follows (amounts exclude investments in U.S. Treasury overnight securities discussed in note 3):

	<u>Historical cost</u>	<u>Gross unrealized holding gains</u>	<u>Gross unrealized holding losses</u>	<u>Fair value</u>
	(in thousands)			
At September 30, 2007:				
U.S. Treasury and agency securities	\$ 1,988,966	16,395	(9,814)	1,995,547
Mortgage-backed securities	289,191	244	(3,871)	285,564
	<u>\$ 2,278,157</u>	<u>16,639</u>	<u>(13,685)</u>	<u>2,281,111</u>
At September 30, 2006:				
U.S. Treasury and agency securities	\$ 2,235,471	7,672	(30,287)	2,212,856
Mortgage-backed securities	182,356	127	(3,912)	178,571
	<u>\$ 2,417,827</u>	<u>7,799</u>	<u>(34,199)</u>	<u>2,391,427</u>

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Maturities of investment securities were as follows at September 30, 2007:

	<b>Historical cost</b>	<b>Fair value</b>
	(in thousands)	
Due in one year or less	\$ 141,693	141,552
Due after one year through five years	959,716	962,312
Due after five years through ten years	557,982	563,519
Due after ten years	618,766	613,728
	\$ 2,278,157	2,281,111

**(5) Contingencies**

Certain Indian tribes for whom OST holds assets in trust do not agree with balances recorded by OST and/or have requested an accounting of their trust funds, and certain of these Indian tribes have filed, or are expected to file, claims against the U.S. Government for failure to fulfill its fiduciary responsibilities and for other related charges. Seventy-seven tribal trust cases currently are pending in various federal district courts and the U.S. Court of Federal Claims. The cases, which were brought by seventy different tribes, involve claims for trust fund and asset mismanagement, accounting, and other declaratory relief. A substantial number of the cases are stayed pending settlement negotiations or discovery. In addition, in many of these cases, the court does not have jurisdiction to grant monetary relief. Neither OST nor the Office of the Solicitor for the Department can presently determine the outcome of these actions nor the total amount, responsibility, and funding source of the potential liability. Any settlement resulting from an adverse outcome of the claims described above is not expected to be satisfied with trust fund balances. No amounts have been recorded in the accompanying Tribal and Other Trust Funds' financial statements for potential claims from the U.S. Government.

**(6) Trust Fund Balances**

Trust fund balances are the aggregation of financial assets held in trust and represent the amounts owed to beneficiaries as of September 30, 2007 and 2006 for which OST has a fiduciary responsibility.

The Tribal and Other Trust Funds contain the following trust fund balance categories for U.S. Government budget purposes, which are reflected as separate components in the accompanying financial statements:

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



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A portion of trust fund balances represents estimated payments on production-type leases for which certain tribes and individual Indians hold an interest. When certain adjustments to production are identified, estimated payments in excess of production are returned to the depositor or adjusted for in future payments.

**(7) Related-Party Transactions with Other Government Organizations**

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

BIA is responsible for the collection of certain monies resulting from the management and use of Indian trust lands and other trust resources. Upon receipt, OST records the deposit of trust funds to trust accounts based on the information received from BIA.

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

For certain trust leases, MMS is responsible for the collection of royalty payments on behalf of Indian tribes and individual Indians holding mineral rights. MMS deposits the royalty payments with the U.S. Treasury and electronically transfers to OST the related accounting information, generally the next business day. The accounting information received from MMS provides OST an allocation of 100% tribally owned lease royalties, enabling OST to record trust deposits directly into tribal accounts. For tribally/individually co-owned leases and individually owned leases, allocation and accounting data is forwarded to OST via electronic interface through the Royalty Distribution Reporting System that is maintained by BIA. Pursuant to established procedure and appropriate authorization, the data is recorded by OST. MMS and BLM both perform verification and other monitoring procedures of mineral assets. Oil and gas companies sometimes forward payments to MMS based on estimated mineral production in order to comply with the Federal Oil and Gas Royalty Management Act of 1982 that requires timely distribution of royalties. These estimated payments may be disbursed by OST to the beneficiaries. Typically, the oil and gas companies adjust future payments for excess or shortfall amounts, if any, based on actual production.

**(c) *Other***

The U.S. Treasury holds cash and certain investments and in certain instances disburses for OST.

The Department's Office of the Solicitor serves as legal counsel for OST.

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September 30, 2007 and 2006

**(8) Transfers of Trust Funds**

OST, pursuant to information provided by BIA, utilizes special deposit accounts maintained within the Individual Indian Monies (IIM) Trust Funds for both tribal and IIM beneficiaries as suspense accounts, whereby funds are temporarily posted when allocation information is not provided when the funds are received. Following receipt of allocation information from BIA, the funds are transferred from the special deposit accounts to the designated tribal and/or IIM account(s). Special deposit accounts totaled approximately \$33 million and \$36 million as of September 30, 2007 and 2006, respectively. The majority of the special deposit account monies held in the IIM Trust Funds relates to historical balances and has not been distributed because the ultimate disposition of the funds has not been determined. Since the ultimate disposition is unknown at September 30, 2007, the portion attributable to the Tribal and Other Trust Funds is unknown. In addition, certain per capita disbursements authorized by tribes result in transfers from the Tribal and Other Trust Funds to the IIM Trust Funds while certain oil and gas distributions may result in transfers to/from the IIM Trust Funds from/to the Tribal and Other Trust Funds. Net transfers of trust funds from the Tribal and Other Trust Funds to the IIM Trust Funds totaled approximately \$60.0 million and \$43.3 million during the years ended September 30, 2007 and 2006, respectively. These transfers are reflected as disbursements in the accompanying statements of changes in trust fund balances.



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

Financial Statements

September 30, 2007 and 2006

(With Independent Auditors' Report Thereon)



**KPMG LLP**  
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Two Park Square  
6565 Americas Parkway NE  
PO Box 3990  
Albuquerque, NM 87190

## **Independent Auditors' Report on Financial Statements**

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

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

We have audited the accompanying statements of assets and trust fund balances – modified cash basis of the Individual Indian Monies Trust Funds managed by the U.S. Department of the Interior Office of the Special Trustee for American Indians (OST) as of September 30, 2007 and 2006, and the related statements of changes in trust fund balances – modified cash basis for the years then ended. These financial statements are the responsibility of management of OST. Our responsibility is to express an opinion on these financial statements based on our audits.

Except as discussed in the fourth paragraph of this report, we conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control over financial reporting of the Individual Indian Monies Trust Funds managed by OST. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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

It was not practicable to extend our auditing procedures sufficiently to satisfy ourselves as to the fairness of trust fund balances in the accompanying financial statements as of September 30, 2007 and 2006 due to certain parties for whom OST holds assets in trust having filed a class action lawsuit for an accounting of the individuals' trust funds which may or may not lead to claims against the United States Government and due to inadequacies in certain Department of the Interior trust-related systems and processes, which provide required trust financial information to OST. Trust fund balances enter into the determination of financial position and changes in trust fund balances.

In our opinion, except for the effects on the financial statements of such adjustments, if any, as might have been determined to be necessary had we been able to apply adequate procedures to determine the fairness of trust fund balances and related changes in trust fund balances, as discussed in the preceding paragraph, the financial statements referred to in the first paragraph above present fairly, in all material respects, the financial position of the Individual Indian Monies Trust Funds managed by OST as of September 30, 2007 and 2006, and the changes in trust fund balances for the years then ended in conformity with the basis of accounting described in note 2.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 9, 2007 on our consideration of internal control over financial reporting and on our tests of Individual Indian Monies Trust Funds' compliance with certain provisions of laws, regulations, contracts, and other matters of the Individual Indian Monies Trust Funds managed by OST. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in assessing the results of our audits.

KPMG LLP

November 9, 2007

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

Statements of Assets and Trust Fund Balances – Modified Cash Basis

September 30, 2007 and 2006

(In thousands)

<b>Assets</b>	<b>2007</b>	<b>2006</b>
Cash and cash equivalents (note 3)	\$ 48,325	61,938
Investments (note 4)	372,592	353,886
Accrued interest receivable	2,780	2,450
Total assets	\$ 423,697	418,274
<b>Trust Fund Balances</b>		
Held for individual Indians (notes 6 and 8)	\$ 423,697	418,274

See accompanying notes to financial statements.

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

Statements of Changes in Trust Fund Balances – Modified Cash Basis

Years ended September 30, 2007 and 2006

(In thousands)

	<b>2007</b>	<b>2006</b>
Increases:		
Receipts (note 8)	\$ 303,677	355,094
Interest earned on invested funds	20,806	20,582
Gain (loss) on disposition of investments, net	459	(2,729)
	324,942	372,947
Decreases:		
Disbursements to and on behalf of account holders	(319,519)	(374,542)
Increase (decrease) in trust fund balances, net	5,423	(1,595)
Trust fund balances, beginning of year	418,274	419,869
Trust fund balances, end of year (notes 6 and 8)	\$ 423,697	418,274

See accompanying notes to financial statements.

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

Notes to Financial Statements

September 30, 2007 and 2006

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

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

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

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

The accompanying financial statements include only the financial assets held in trust by the Office of the Special Trustee for American Indians (OST) for trust beneficiaries and do not include: (i) the operating account balances of OST (e.g., Fund Balance with Treasury; Property, Plant, and Equipment; etc.) or (ii) other Indian trust assets, including but not limited to, Indian lands, buildings, or other non-financial assets managed by the United States Department of the Interior (the Department).

**The Reform Act** – The American Indian Trust Fund Management Reform Act of 1994 (Public Law 103-412) (the Reform Act) authorized the establishment of OST, which is headed by the Special Trustee for American Indians (Special Trustee) who reports to the Secretary. Under this legislation, the Special Trustee is responsible for oversight, reform, and coordination of the policies, procedures, systems, and practices used by various bureaus and offices of the Department, including but not limited to OST, the Bureau of Indian Affairs (BIA) (a component of Indian Affairs (IA)), the Minerals Management Service (MMS), and the Bureau of Land Management (BLM), in managing Indian trust assets.

**Office of the Special Trustee for American Indians** – Indian trust assets, including the IIM Trust Funds, are primarily managed under the delegated authority of OST and BIA. Management of Indian trust assets on behalf of the trust beneficiaries is dependent upon the processing of trust-related



**INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE U.S. DEPARTMENT OF THE INTERIOR  
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Notes to Financial Statements

September 30, 2007 and 2006

transactions within certain information systems of the Department, including but not limited to OST, BIA, MMS, and other Departmental bureaus and offices. BIA and other Departmental bureaus and offices are responsible for managing the natural resources located within the boundaries of Indian reservations and trust lands as well as the processing of data regarding the ownership and leasing of Indian lands. The allocation and distribution of receipts and disbursements by OST to trust beneficiaries are significantly dependent and reliant upon the receipt of timely and accurate information derived from records maintained by BIA, MMS, and other Departmental bureaus and offices (see note 7).

**Regional Offices** – OST and BIA maintain staff at regional offices located throughout the United States.

**Agency and Field Offices** – OST and BIA maintain staff at agency and field offices located throughout the United States, which are generally located near the tribes and individual Indians served. OST and BIA personnel located at most of the agency and field offices perform various functions related to trust fund activities.

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

Certain of the IIM Trust Funds described below are subject to legal, regulatory, budgetary, court-ordered, or other restrictions. Approximately 371,000 and 323,000 open accounts, held primarily for the benefit of individual Indian account holder beneficiaries and tribal entities, comprise the IIM Trust Funds as of September 30, 2007 and 2006, respectively. The IIM Trust Funds contain certain special deposit accounts that will ultimately be distributed to tribal and other entities.

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

**(c) Investment of Trust Funds**

Authorizing legislation and a substantial body of case law specify how Indian trust funds should be managed and which financial instruments constitute appropriate investments for Indian trust funds. The IIM Trust Funds are pooled and invested in U.S. Government securities, including U.S. Department of the Treasury (U.S. Treasury) issues, U.S. Government agency issues, and U.S. Government-sponsored entity issues.

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

**(a) Basis of Accounting**

OST uses the cash basis of accounting with certain modifications for the IIM Trust Funds, which is a comprehensive basis of accounting other than generally accepted accounting principles. Receipts are recorded when received with the exception of interest earned on invested funds (including discount accretion and premium amortization), and disbursements are recorded when issued. Investments are

**INDIVIDUAL INDIAN MONIES TRUST FUNDS  
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Notes to Financial Statements

September 30, 2007 and 2006

stated at amortized cost. Accrual adjustments to reflect interest earned but not received, and to record any applicable accretion of discounts and amortization of premiums over the terms of the investments, have been recorded in the accompanying financial statements. Interest income reported in the statements of changes in trust fund balances reflects interest earned, net of any premium amortization or discount accretion recognized during the fiscal year.

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

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

**(c) *Investments***

Investment securities at September 30, 2007 and 2006 consist of U.S. Treasury issues, U.S. Government agency issues, and U.S. Government-sponsored entity issues. IIM Trust Funds are pooled and invested. Investment securities are recorded at amortized cost, adjusted for the amortization or accretion of premiums or discounts. Premiums and discounts are amortized or accreted over the expected life of the related investment security as an adjustment to yield using the effective-interest method. Interest income is recognized when earned.

The IIM Trust Funds' investments have a concentration in U.S. Government securities, as mandated by 25 USC 162.

**(d) *Receipts***

Receipts from various leasing activities, mineral royalties and sales of extracted minerals, timber and other forest products, fees and fines, and the granting of easements are generated from a variety of non-financial assets that are held in trust by the U.S. Government and managed by BIA and other Departmental bureaus and offices on behalf of individual Indians. Receipts on hand at the regional and agency offices, and/or in-transit at September 30, 2007 and 2006, if any, awaiting deposit to the U.S. Treasury, are not included in the accompanying financial statements.

Receipts also include payments from the U.S. Government for judgment awards and the settlement of claims.

**(e) *Disbursements***

Payments disbursed from the IIM Trust Funds consist of accumulations of funds from various income-producing activities such as leasing, royalty receipts, mineral extraction, timber and other forest product sales, judgment awards, tribal per capita distributions, and investment income.

**(f) *Use of Estimates***

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

**INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE U.S. DEPARTMENT OF THE INTERIOR  
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Notes to Financial Statements

September 30, 2007 and 2006

**(3) Cash and Cash Equivalents**

Cash equivalents of approximately \$46 million and \$57 million at September 30, 2007 and 2006, respectively, consist of overnight investments with the U.S. Treasury.

**(4) Investments**

The amortized cost, gross unrealized holding gains, gross unrealized holding losses, and fair value of investment securities by major class of security at September 30 were as follows (amounts exclude investments in U.S. Treasury overnight securities discussed in note 3):

	<b>Amortized cost</b>	<b>Gross unrealized holding gains</b>	<b>Gross unrealized holding losses</b>	<b>Fair value</b>
		(in thousands)		
At September 30, 2007:				
U.S. Treasury and agency securities	\$ 163,444	1,145	(555)	164,034
Mortgage-backed securities	209,148	328	(2,983)	206,493
	\$ 372,592	1,473	(3,538)	370,527
At September 30, 2006:				
U.S. Treasury and agency securities	\$ 184,227	647	(2,686)	182,188
Mortgage-backed securities	169,659	189	(2,474)	167,374
	\$ 353,886	836	(5,160)	349,562

Maturities of investment securities were as follows at September 30, 2007:

	<b>Amortized cost</b>	<b>Fair value</b>
	(in thousands)	
Due in one year or less	\$ 10,000	9,939
Due after one year through five years	43,754	43,243
Due after five years through ten years	48,839	48,675
Due after ten years	269,999	268,670
	\$ 372,592	370,527

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

Notes to Financial Statements

September 30, 2007 and 2006

**(5) Contingencies**

Certain parties for whom OST holds assets in trust have filed a class action lawsuit for an accounting of the individuals' trust funds, which may or may not lead to claims against the U.S. Government. The lawsuit alleges that the Department and U.S. Treasury have breached their trust obligations with respect to management of funds in the IIM accounts. Neither OST nor the Office of the Solicitor for the Department can presently determine the outcome of these actions nor the total amount, responsibility, and funding source of the potential liability. Any settlement resulting from an adverse outcome of the claims described above is not expected to be satisfied with trust fund balances. No amounts have been recorded in the accompanying IIM Trust Funds' financial statements for potential claims from the U.S. Government.

**(6) Trust Fund Balances**

Trust fund balances are the aggregation of financial assets held in trust and primarily represent the amounts owed to beneficiaries as of September 30, 2007 and 2006 for which OST has a fiduciary responsibility.

The net total of the balances reflected in the IIM account holders' subsidiary detail of accounts as of September 30, 2006 was less than the trust fund balances reported in the accompanying financial statements due to certain accounts with negative balances aggregating approximately \$44 million (of which approximately \$164,000 is attributed to individual Indian accounts and the rest to historical house/suspense accounts). As of September 30, 2006, the aggregate sum of positive account balances in the IIM subsidiary detail of account holders' balances exceeded the trust fund balances reported in the accompanying financial statements by approximately \$6 million.

During the year ended September 30, 2007, adjusting entries were posted to the subsidiary ledger eliminating the approximate \$44 million in negative account balances (of which approximately \$113,000 was attributable to individual Indian accounts). As of September 30, 2007, the net total of the balances reflected in the IIM account holders subsidiary detail of account holders' balances exceeded the trust fund balances reported in the accompanying financial statements by approximately \$6 million.

The subsidiary detail of IIM account balances contains approximately 13,000 and 22,000 special deposit accounts with balances totaling approximately \$33 million and \$36 million as of September 30, 2007 and 2006, respectively. The majority of the special deposit account monies held in the IIM Trust Funds relates to historical balances and has not been allocated because the allocation information for the funds has not been provided by BIA. Since the ultimate allocation is unknown at September 30, 2007, the portion attributable to the IIM Trust Funds is unknown.

The subsidiary detail of IIM account balances contains certain oil and gas holding accounts with balances totaling approximately \$5.3 million and \$7.4 million as of September 30, 2007 and 2006, respectively, which have not been distributed to beneficiaries. Upon receipt of the allocation and accounting data, provided by MMS and BIA, the monies will be distributed to IIM account holders' accounts (see note 7).

A portion of trust fund balances represents estimated payments on production-type leases for which certain individual Indians and tribes hold an interest. When certain adjustments to production are identified, estimated payments in excess of production are returned to the depositor or adjusted for in future payments.

**INDIVIDUAL INDIAN MONIES TRUST FUNDS  
MANAGED BY THE U.S. DEPARTMENT OF THE INTERIOR  
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Notes to Financial Statements

September 30, 2007 and 2006

**(7) Related-Party Transactions with Other Government Organizations**

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

BIA is responsible for the collection of certain monies resulting from the management and use of Indian trust lands and other trust resources. Upon receipt, OST records the deposit of trust funds to trust accounts based on the information received from BIA.

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

For certain trust leases, MMS is responsible for the collection of royalty payments on behalf of Indian tribes and individual Indians holding mineral rights. MMS deposits the royalty payments with the U.S. Treasury and electronically transfers to OST the related accounting information, generally the next business day. For tribally/individually co-owned leases and individually owned leases, the allocation and accounting data to distribute the monies to the proper IIM account is forwarded to OST via electronic interface through the Royalty Distribution Reporting System that is maintained by BIA. Pursuant to established procedure and appropriate authorization, the data is recorded by OST. MMS and BLM both perform verification and other monitoring procedures of mineral assets. Oil and gas companies sometimes forward payments to MMS based on estimated mineral production in order to comply with the Federal Oil and Gas Royalty Management Act of 1982 that requires timely distribution of royalties. These estimated payments may be disbursed by OST to the beneficiaries. Typically, the oil and gas companies adjust future payments for excess or shortfall amounts, if any, based on actual production.

**(c) *Other***

The U.S. Treasury holds cash and certain investments and in certain instances disburses for OST.

The Department's Office of the Solicitor serves as legal counsel for OST.

**(8) Transfers of Trust Funds**

OST, pursuant to information provided by BIA, utilizes special deposit accounts (see note 6) maintained within the IIM Trust Funds for both tribal and IIM beneficiaries as suspense accounts, whereby funds are temporarily posted when allocation information is not provided when the funds are received. Following receipt of allocation information from BIA, the funds are transferred from the special deposit accounts to the designated tribal and/or IIM account(s). In addition, certain per capita disbursements authorized by tribes result in transfers from the Tribal and Other Trust Funds to the IIM Trust Funds while certain oil and gas distributions may result in transfers to/from the IIM Trust Funds from/to the Tribal and Other Trust Funds. Net transfers of trust funds to the IIM Trust Funds from the Tribal and Other Trust Funds totaled approximately \$60.0 million and \$43.3 million during the years ended September 30, 2007 and 2006, respectively. These transfers are reflected as receipts in the accompanying statements of changes in trust fund balances.



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

Independent Auditors' Report on Internal Control Over  
Financial Reporting and on Compliance and Other Matters

September 30, 2007



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## **Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters**

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

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

We have audited the statements of assets and trust fund balances – cash basis of the Tribal and Other Trust Funds as of September 30, 2007 and 2006, and the related statements of changes in trust fund balances – cash basis for the years then ended, and the statements of assets and trust fund balances – modified cash basis of the Individual Indian Monies Trust Funds (IIM) as of September 30, 2007 and 2006, and the related statements of changes in trust fund balances – modified cash basis for the years then ended (collectively referred to as the Trust Funds Financial Statements) managed by the U.S. Department of the Interior Office of the Special Trustee for American Indians (OST) and have issued our reports thereon dated November 9, 2007. The objective of our audits was to express opinions on the fair presentation of the Trust Funds Financial Statements. In connection with our fiscal year 2007 audits, we also considered internal control over financial reporting for the Tribal and Other Trust Funds and IIM Trust Funds managed by OST and tested compliance with certain provisions of applicable laws, regulations, and contracts that could have a direct and material effect on the Trust Funds Financial Statements.

### **Summary**

Our audit reports on the Trust Funds Financial Statements were qualified because it was not practicable to extend our auditing procedures sufficiently to satisfy ourselves as to the fairness of trust fund balances in the Trust Funds Financial Statements as of September 30, 2007 and 2006 due to: (i) certain parties for whom OST holds assets in trust having filed a class action lawsuit for an accounting of the individuals' IIM trust funds which may or may not lead to claims against the United States Government, (ii) tribal parties for whom OST holds assets in trust disagreeing with the balances recorded by OST, and/or having requested an accounting of their trust funds, and certain of these parties have filed, or are expected to file, claims against the United States Government, and (iii) inadequacies in certain Department of the Interior (the Department) trust-related systems and processes, which provide required trust financial information to OST (see *B. Reliance on Processing of Trust Transactions at the Bureau of Indian Affairs* below). Trust fund balances enter into the determination of financial position and changes in trust fund balances.

Our reports also state that the Trust Funds Financial Statements are prepared in accordance with a basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles as described in note 2 to the Trust Funds Financial Statements.

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

Significant Deficiency Considered to be a Material Weakness

A. Unresolved trust funds financial reporting matters from prior periods

Other Significant Deficiency

B. Reliance on processing of trust transactions at the Bureau of Indian Affairs

The results of our tests of compliance with certain provisions of laws, regulations, and contracts disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards*, issued by the Comptroller General of the United States.

The following sections present an overview of the Trust Funds Financial Statements, and discuss our consideration of internal control over financial reporting for the Tribal and Other Trust Funds and IIM Trust Funds managed by OST, our tests of compliance with certain provisions of applicable laws, regulations, and contracts for the Tribal and Other Trust Funds and IIM Trust Funds managed by OST, and management's and our responsibilities.

**Overview – Trust Funds Financial Statements**

The United States Congress has designated the Secretary of the United States Department of the Interior (the Secretary) as the trustee delegate with responsibility for the financial and non-financial resources held in trust on behalf of American Indian tribes, individual Indians, and other trust funds. In carrying out the management and oversight of the Indian trust assets, the Secretary has a fiduciary responsibility to ensure monies are received for the use of Indian lands and the extraction of natural resources from Indian lands, distribute such monies collected to the appropriate beneficiaries, ensure that trust accounts are properly maintained and invested, and ensure that accurate and complete reports are provided to the trust beneficiaries in accordance with applicable law.

The American Indian Trust Fund Management Reform Act of 1994 (Public Law 103-412) (the Reform Act) authorized the establishment of OST, which is headed by the Special Trustee for American Indians (Special Trustee) who reports to the Secretary. Under this legislation, the Special Trustee is responsible for oversight, reform, and coordination of the policies, procedures, systems, and practices used by various bureaus and offices of the Department of the Interior (the Department), including but not limited to OST, the Bureau of Indian Affairs (BIA) (a component of Indian Affairs (IA)), the Minerals Management Service (MMS), and the Bureau of Land Management (BLM), in managing Indian trust assets.

**Internal Control Over Financial Reporting**

Our consideration of the internal control over financial reporting was for the limited purpose described in the Responsibilities section of this report and would not necessarily identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects management's ability to initiate, authorize, record, process, or report financial data reliably such that there is more than a remote likelihood that a misstatement of the Trust Funds Financial Statements that is more than inconsequential will not be prevented or detected by management's internal control over financial reporting. A material weakness is a significant deficiency, or combination of



significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by management's internal control.

In our fiscal year 2007 audits, we considered the deficiency described below to be a material weakness as a result of historical internal control matters over financial reporting:

***A. Unresolved Trust Funds Financial Reporting Matters from Prior Periods***

*Condition*

Indian trust assets, including the trust funds, are primarily managed under the delegated authority of OST and BIA. Management of Indian trust assets on behalf of the trust beneficiaries is dependent upon the processing of trust-related transactions within certain information systems of the Department, including but not limited to OST, BIA, MMS, and other Departmental bureaus and offices. BIA and other Departmental bureaus and offices are responsible for managing the natural resources located within the boundaries of Indian reservations and trust lands, as well as the processing of data regarding the ownership and leasing of Indian lands. The allocation of receipts and disbursements by OST to trust beneficiaries are significantly dependent and reliant upon the receipt of timely and accurate information derived from records maintained by BIA, MMS, and other Departmental bureaus and offices.

The financial information systems and internal control procedures used in the processing of Indian trust transactions have suffered historically from a variety of system and procedural internal control weaknesses. In addition, current management is burdened with the ongoing impact of decades of accumulated discrepancies in the accounting records. Furthermore, certain Indian trust beneficiaries do not agree with the Indian trust balances and/or have requested an accounting of the Indian trust funds. The Department has invested a significant amount of resources identifying historical records, isolating and working to resolve historical differences, and preparing an accounting of the Indian trust fund balances and will continue with this historical accounting effort.

As of September 30, 2007, several significant financial reporting differences from prior periods have not been resolved. These items have a material effect on the Trust Funds Financial Statements as of September 30, 2007 and 2006, and for the years then ended. These differences from prior periods, which have not been resolved, include the following:

*Lack of Reliable IIM Balance – IIM*

The Trust Funds Accounting System (TFAS) control account for IIM represents the aggregate net balance of trust funds held on behalf of IIM account holders, as well as house/suspense accounts, as reflected in the detailed subsidiary ledger of IIM accounts (subsidiary ledger) also in TFAS. The control account balance has historically not agreed to the sum of the balances from the subsidiary ledger and it cannot be determined which balance, if either, is correct. As of September 30, 2006, the aggregate sum of all positive balances included in the subsidiary ledger exceeded the control account by approximately \$6,000,000. The amount invested for IIM is based on the IIM control account balance in TFAS. Consequently, the balance of funds invested for IIM may not be correct, which in turn would affect interest earnings. In addition, as of September 30, 2006, the subsidiary ledger contained negative account balances totaling approximately \$43,800,000 (of which approximately \$164,000 was attributed to individual Indian accounts and the rest to historical house/suspense accounts).

During the year ended September 30, 2007, management posted adjusting entries to the subsidiary ledger eliminating the approximate \$43,800,000 in negative account balances (of which approximately \$113,000 was attributable to individual Indian accounts). KPMG was unable to perform procedures over management's adjusting entries, and is therefore unable to conclude on the propriety of these

entries. As of September 30, 2007 the balance of all subsidiary ledger account balances exceeds the IIM control account balance in TFAS by approximately \$6,000,000, and it cannot be determined which balance, if either, is correct.

#### *Trust Fund Balances – Tribal*

An historical “undistributed interest” house account of approximately \$1,800,000 existed at September 30, 1995. The balance as of September 30, 2006 was approximately \$2,009,000. Interest earned on these funds was allocated to the house account. In prior years OST commissioned a report to assist in determining the recipients of these funds, and based on that report distributed the balance of this account in October 2006.

#### *Cash – Tribal*

As of September 30, 2007 and 2006, there were eleven accounts in TFAS with negative balances totaling approximately \$721,000, carried forward from the previous trust funds accounting system prior to the conversion to TFAS.

#### *Special Deposit Accounts – Tribal and IIM*

As of September 30, 2007 and 2006, there were approximately 13,000 and 22,000 special deposit accounts reflected in the subsidiary ledger in TFAS with balances totaling approximately \$33 million and \$36 million, respectively. In accordance with Title 25 of the Code of Federal Regulations and as directed by BIA, historically OST recorded receipts into special deposit accounts within the subsidiary ledger when the recipient trust fund account was unknown at the time of receipt. When BIA identifies the trust fund account(s), OST transfers the amount from the special deposit account(s) to the designated trust fund account(s) in accordance with BIA instructions. A significant number of special deposit accounts have remained inactive for the past several years and new accounts continued to be established during the years ended September 30, 2007 and 2006. During fiscal years 2002 and 2001, management of OST, together with BIA and a contractor, developed and put in place a formal plan to address special deposit accounts. Beginning in fiscal year 2003, the Office of Historical Trust Accounting began working with OST and BIA to distribute funds in special deposit accounts that were opened on or before December 31, 2002. Special deposit account activity after that date will be addressed by BIA, with instructions for distributions being provided to OST. At September 30, 2007, a significant number of special deposit accounts represent historical balances and continue to require resolution and management is actively pursuing the resolution of these accounts.

#### *Trust Fund Balances – IIM*

An historical “undistributed interest” house account of approximately \$1,205,000 existed at September 30, 1990. The balances as of September 30, 2007 and 2006 were approximately \$2,300,000 and 2,200,000, respectively. Interest earned on these funds is recorded in the house account. The allocation of these funds has not been determined.

During fiscal years 2002 and 2004, approximately \$922,000 and \$375,000, respectively, was transferred from certain special deposit accounts to “undistributed interest” house accounts in connection with the review of certain special deposit accounts performed by OST, together with BIA and a contractor. Interest earned on these funds was allocated to current IIM accounts through September 30, 2005. Beginning October 1, 2005, interest earned on these funds was allocated to the respective undistributed interest accounts. The balances as of September 30, 2007 were approximately \$1,010,000 and \$447,000, respectively, and as of September 30, 2006 were approximately \$962,000 and \$390,000, respectively. The allocation of these funds has not been determined.

We also considered the deficiency described below, as identified in the Departmental Offices (DO) report on internal control over financial reporting, to be a significant deficiency in internal control over financial reporting for the Trust Funds Financial Statements:

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

The regional and agency offices of BIA perform a critical role in the initial input and subsequent changes to Indian trust information. The independent auditors' report on internal control over financial reporting and compliance and other matters for the year ended September 30, 2007 at DO noted significant deficiencies at BIA, identified as part of the fiscal year 2007 IA audit, in the following areas:

- a. Trust Fund Records - IA did not consistently maintain ownership records for rights of way lease agreements on lands held in trust for the Indian Trust Funds because IA was unable to provide evidence of ownership for 38 of the 45 lease agreements tested. Additionally, IA did not consistently obtain appraisals from the Bureau of Land Management prior to entering into the lease agreements related to lands held in trust for the Indian Trust Funds. Furthermore, IA did not consistently follow its policies contained in Part 53 of the Indian Affairs Manual because IA did not obtain and approve Forest Management Plans for 2 of 30 locations tested.
- b. Distribution of Funds to OST - IA did not consistently sign the Trust Funds Receivable Worksheet (TFR) prior to submitting funds to OST for 9 of the 115 items tested. IA did not consistently transfer funds to OST within 24 hours of the lease agreement approval for 15 of 115 items tested and within 24 hours of receipt for 3 of the 115 items tested in accordance with its policies. In addition, IA did not use the fastest means possible in forwarding funds to the lockbox in accordance with its policies for 5 of 115 items tested.
- c. Accounts Receivable – IA had not fully developed and communicated standardized policies and procedures for establishing, tracking, and pursuing historical accounts receivable for the Indian Trust Funds. This resulted in inconsistent processes and increases the risk that amounts due to Indian Trust Funds are not identified and ultimately collected.
- d. Probate Backlog – IA did not consistently enter probate orders for land title into the trust management systems timely. Although IA made progress in reducing the backlog, IA indicated that it had probate orders that had not been prepared, adjudicated, recorded, and/or encoded. IA expects to have the backlog resolved in September 2009. This increases the potential for untimely distributions of income to the account holders of the Indian Trust Funds.
- e. Supervised and Restricted Accounts – IA did not consistently perform reviews over active supervised accounts. Finally, although each of the regions that we visited had compiled a listing of active supervised accounts, the regions expended significant efforts generating the listing. IA has identified reports from TFAS and Strata Vision, which list all active supervised accounts and needs to work with OST to ensure its timely distribution to the appropriate agency offices.

The presence of these significant deficiencies directly impacts OST's ability to process trust transactions on behalf of trust beneficiaries and to provide accurate information to account holders due to the interrelationship between BIA and OST.

### ***Recommendation***

We recommend that management of OST:

- 1 Continue to work to resolve the unresolved trust funds financial reporting differences as soon as practicable. In situations where actions or inputs from Department officials are needed to resolve a matter, we recommend management of OST continue to work with appropriate Department officials such that all matters are resolved as soon as practical; and
- 2 Continue to work collaboratively with BIA to correct the significant deficiencies identified above such that OST may fulfill its fiduciary responsibility to the trust fund beneficiaries.

### ***OST Management's Response to Unresolved Trust Funds Financial Reporting Matters from Prior Periods***

Management does not concur that the findings above are a material weakness individually or collectively. Based on Office of Management and Budget Bulletin 07-04, Material Weakness is a significant deficiency, or combination of significant deficiencies, that result in a more than remote<sup>1</sup> likelihood that a material misstatement of the financial statements will not be prevented or detected. This material weakness definition aligns with the same material weakness definition used by management to prepare an agency's FMFIA assurance statement. The historical conditions that resulted in the findings have been corrected through internal controls that mitigate the risk of recurrence. These controls are in place and operating effectively, therefore, there is no impact or no material impact on the current financial internal control environment (e.g. \$6 million in differences in IIM and \$721,000 of over-drafts in Tribal). In addition, as of the end of FY 2007, there are only three allowable instances when it is acceptable to post trust funds to a SDA: 1) funds collected are under litigation/appeal; 2) a solicitor's opinion or policy change is needed; or 3) the trust land which generated the funds requires a survey. Support documentation is required at the time a SDA is established. Implementation of TAAMS-Leasing along with the TAAMS-TFAS interface allows trust funds to be posted directly to the beneficiary account.

<sup>1</sup> The term "remote" is defined in SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, as the chance of the future event, or events, occurring is slight. Therefore, the likelihood of an event is "more than remote" when it is at least reasonably possible.

### ***Auditors' Response to Management's Response to Unresolved Trust Funds Financial Reporting Matters from Prior Periods***

As summarized in the condition section above, management had not resolved significant financial reporting differences from prior periods as of September 30, 2007. Therefore, we continue to believe that the weaknesses identified constitute a material weakness.

### ***Departmental Offices Management's Response to Processing of Trust Transactions at IA***

**Management does not concur.** Upon careful consideration of the significant corrective action progress, procedures and internal controls that have been implemented and we continue to believe that our efforts to address the deficiencies in controls related to Indian Trust Funds are substantially complete and provide for reliable information. This position is based on the results of our extensive internal controls testing. Controls are in place and are operating effectively; therefore, there is no adverse material impact on the current financial internal control environment. We believe that there is a high degree of accuracy in the Trust Fund account balances, the accounting and asset management resource systems are reliable, and monies are being properly and timely accounted for.

***Auditors' Response to Management's Response to Processing of Trust Transactions at IA***

As summarized above, we identified control deficiencies in the current year that adversely affect Departmental Offices' ability to initiate, authorize, record, process, and report Indian Trust Fund data reliably. Therefore, we continue to believe that the control deficiencies identified constitute a significant deficiency.

**Compliance and Other Matters**

The results of our tests of compliance described in the Responsibilities section of this report disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards*.

We noted other matters involving compliance with laws, regulations, and contracts that, under *Government Auditing Standards*, were not required to be included in this report, which we have reported to OST management in a separate letter dated November 9, 2007.

**Responsibilities**

***Management's Responsibilities***

The American Indian Trust Fund Management Reform Act of 1994 requires that the Secretary shall cause to be conducted an annual audit on a fiscal year basis of all funds held in trust by the U.S. Government for the benefit of an Indian tribe or an individual Indian, which are deposited or invested pursuant to the Act of June 24, 1938 (25 U.S.C. 162a).

Management is responsible for the financial statements, including:

- Preparing the financial statements in conformity with the basis of accounting described in note 2 of the Trust Funds Financial Statements;
- Establishing and maintaining internal control; and
- Complying with laws, regulations, and contracts applicable to the Tribal and Other Trust Funds and IIM Trust Funds managed by OST.

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

***Auditors' Responsibilities***

Our responsibility is to express opinions on the fiscal year 2007 and 2006 Trust Funds Financial Statements based on our audits. Except as discussed in the fourth paragraph of our auditors' reports, we conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing opinions on the effectiveness of internal control over financial reporting of the Tribal and Other Trust Funds and IIM Trust Funds managed by OST. Accordingly, we express no such opinions.

An audit also includes:

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

We believe that our audits provide a reasonable basis for our opinions.

In planning and performing our fiscal year 2007 audits, we considered internal controls over financial reporting for the Tribal and Other Trust Funds and IIM Trust Funds managed by OST by obtaining an understanding of the internal controls, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in *Government Auditing Standards*. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*. The objective of our audits was not to provide opinions on internal control over financial reporting for the Tribal and Other Trust Funds and IIM Trust Funds managed by OST. Accordingly, we do not express an opinion on the effectiveness of the Trust Funds' internal control over financial reporting.

As part of obtaining reasonable assurance about whether the fiscal year 2007 Trust Funds Financial Statements are free of material misstatement, we tested compliance with certain provisions of laws, regulations, and contracts for the Tribal and Other Trust Funds and IIM Trust Funds managed by OST, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, and contracts applicable to the Tribal and Other Trust Funds and IIM Trust Funds managed by OST. However, providing an opinion on compliance with laws, regulations, and contracts was not an objective of our audits, and accordingly, we do not express such an opinion.

**Restricted Use**

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

**KPMG LLP**

November 9, 2007

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

**Status of Prior Year Findings, Reported as of September 30, 2006**

**September 30, 2007**

<u>Reference</u>	<u>Condition</u>	<u>Current-Year Status</u>
OST-2006	Unresolved Financial Reporting Matters from Prior Periods	Repeated, with certain modifications in current-year report – see current-year significant deficiency A, considered a material weakness.
	Reliance on Processing of Trust Transactions at the Bureau of Indian Affairs	Repeated, with certain modifications in current-year report – see current-year significant deficiency B.