

**TESTIMONY
OF
SANDRA K. JOHNIGAN, CPA, CFE
BEFORE THE
UNITED STATES SENATE COMMITTEE ON INDIAN
AFFAIRS AND THE
UNITED STATES HOUSE COMMITTEE ON RESOURCES
REGARDING
SETTLEMENT OF COBELL V. NORTON**

MARCH 1, 2006

I am pleased to appear today, at the request of the Chairmen of these distinguished Committees, to present testimony on the settlement of Cobell v. Norton. This testimony is based on my experience as a forensic accounting specialist. Relevant experience includes private sector trust accounting disputes and, recently, Tribal trust fund disputes. During the last year and a half I have had the opportunity to participate as the lead accounting consultant for the Confederated Tribes of the Warm Springs Reservation in a trust funds dispute with the United States Government. As described in a February 21, 2006 filing in the Court of Federal Claims, the parties have reached a settlement in principle on the Phase I issues in the matter. Since February of 2005 I have also been engaged by the InterTribal Monitoring Association (ITMA) as the lead accounting consultant for a cooperative effort to develop a methodology to use in the settlement of Tribal trust fund accounts for the 1972 to 1992 time period. The participating Tribes are involved in a negotiation with the United States Government to use the methodology mutually developed. My resume is included at Attachment A.

Introduction

My testimony is intended to address forensic accounting issues and approaches that may be of use in the settlement of **Cobell v Norton**. I am not an attorney and want to emphasize that my testimony is not meant to cover any legal issues. As I mentioned, I have been engaged as a consultant for certain Tribes, on Tribal trust issues. I have not been engaged by either side to assist in the **Cobell v Norton** case.

In my experience, the first key to a successful resolution of a dispute is asking the right questions. Asking questions does not change the underlying facts in a matter, but it can help to identify which facts are relevant to the resolution. Every matter comes equipped with facts, generally far too many of them. There are some facts that both sides agree upon, and others that are called “facts” by one side and “unproved allegations” by the other side. Framing the right questions, and answering them, can strip away the “static” and uncover the facts that can actually be used to reach a resolution.

The second key to a successful resolution of a dispute is getting the parties to mutually develop a process to answer those questions. Unless both parties have reason to believe the process is unbiased, the resulting “answers” will not be acceptable as a basis for resolution.

I have seen that process work in the Tribal cases in which I am currently engaged as well as private sector trust disputes. That experience is the reason for my testimony here today. I do not presume to have answers for the Cobell dispute. What I do hope to do is assist in the development of questions, and a process for answering them, that may help to resolve the dispute.

Background

It is my understanding that Title I of S. 1439 and H. R. 4322 are intended to

“provide benefits that are reasonably calculated to be fair and appropriate in lieu of performing an accounting of an IIM [Individual Indian Monies] account, or assuming liability for errors in such an accounting, mismanagement of IIM account funds (including undetermined amounts of interest in IIM accounts, losses in which may never be discovered or quantified if a complete historical accounting cannot be performed), or breach of fiduciary duties with respect to the administration of IIM accounts, in order to transmute claims by the beneficiaries of IIM accounts for undetermined or unquantified accounting losses and interest to a fixed amount to be distributed to the beneficiaries of IIM accounts”,

The amounts determined in the above effort are to be distributed taking into consideration:

“the risks and costs to IIM account beneficiaries, as well as any delay, associated with the litigation of claims that will be resolved by this title; and ...the benefits to IIM account beneficiaries available under this title”

To accomplish the above goal an amount of money is proposed as an Initial Deposit into the Settlement Fund. This amount is currently listed as \$[___],000,000,000 It is my understanding that the Plaintiffs have proposed an amount of \$27.5 billion. It is also my understanding that the Defendants have rejected this amount as materially differing from their belief as to an appropriate amount.

To analyze the positions of the parties, a fair question is what the bases are for amounts that the parties propose. Knowing the bases with some level of specificity will provide the needed data to determine how the bases can be verified or adjusted to provide individual Indians, the United States Government Department of Interior and Congress with an understanding of the relevance and reliability of an agreed upon or proposed amount. Testimony to the United States Committee on House Resources provided by Eloise Cobell and Associate Deputy Secretary James Cason provided some information about how the Plaintiffs developed the \$27.5 billion number and the United States' view of the amount. It provides some insight into the above numbers. Where applicable I have included information from their testimony in the following discussion.

What Are the Parties Attempting to Resolve and Therefore What is the Legislation Attempting to Resolve?

A critical first question is “what are the parties attempting to resolve”? Without a clear understanding of the issues being addressed in the litigation, legislation could provide settlement for only a portion of what is at the heart of the dispute.

The Plaintiffs initially asked the Department of Interior to provide an “accounting”. The nature of what is required for such an accounting is in dispute, but the general concept provides a useful framework for discussion. Generally an accounting calls for:

1. Determining all receipts,
2. Determining all disbursements
3. Computing the difference between all receipts and disbursements; for each required reporting period to determine the outstanding balance based on the accounting and
4. Comparing the computed accounting balance to the historical balance that exists in the account

5. Resolving any difference between the balance determined from the accounting and the recorded balance as it exists in the account.

The Plaintiffs' expectation appears to be that there will be an amount computed that is owed to the individual Indian account holders and that the resolution will be payment to those account holders. The Department of Interior's position appears to be that work to date does not support a significant amount of funds due to individual Indian monies (IIM) account holders. In order to break this impasse, it may help to focus on the individual elements of the "accounting", and what the appropriate questions might be, related to each element.

Receipts

It is not clear from the testimony in December whether the parties have even agreed on the total receipts involved. Eloise Cobell stated in her December 8, 2005 testimony: "Since both sides agree that the government should have paid roughly \$13 billion into the individual Indian Trust accounts since 1887..."

However, Assistant Secretary James Cason did not specifically discuss the \$13 billion of receipts. He did discuss the statistical approach they are applying and suggested that results to date support exempting Judgment and Per Capita funds from any proposed legislation. He then discussed the remaining "land based accounts" and described a 99% completion rate for the sampled and high dollar (over \$100,000) items selected for testing. His discussion indicated that there are relatively small "difference rates" for the sample period. It should be noted that the sample period he refers to appears to have started no earlier than 1985. He does not describe the effect of those rates on the more than 100 year accounting period, nor the need for adjustment of the rates, if applicable, due to differences in systems and management during earlier periods.

Therefore, questions to address for receipts include:

- Do the parties generally agree with the \$13 billion of total receipts? If so, do they agree on the timing of the receipts? If there are differences, what are the bases for the differing amounts?
- Does the \$13 billion (or some other agreed upon amount) represent only what is known to be recorded?
- Are there claims for additional amounts that should have been received but were not (such as non collection of surface leases that were contractual obligations.)?

There is another type of receipt that could produce claims, i.e. amounts that would have been received absent alleged mismanagement of assets, such as leases entered into at less than fair market value. According to Assistant Secretary James Cason's December 2005 testimony the Plaintiffs' proposed settlement amount does not include resolution of such claims.

In other words, even an apparently simple term such as "total receipts" involves at least three subsets, each with its own questions: 1) amounts shown as being recorded, 2) amounts that should have been received but were not, and 3) amounts that were recorded but which should have been for greater amounts. Each subset will in turn have its own questions, depending upon what is driving the estimates and what documentation is available to answer the questions. If the parties can agree upon the questions in sufficient detail, they will be a long way toward working out a "mutually agreed upon" system for answering the questions.

Claims for what "should have been received" will need to be explicitly addressed in any settlement. The following is a further consideration of these claims.

Amounts That Should Have Been Received But Were Not

If there is an expectation that the receipts should also include what “should have been received but were not” for existing transactions and contracts, then the work performed requires more than an analysis of already recorded receipts. For Tribal trust accounts during the 1972 to 1992 time frame Arthur Andersen performed a certain agreed upon procedures (AA Project) to test this concern for a limited number of contracts and Tribes. This specific work in the AA Project was called “Fill the Gap”. Work in this area:

- Requires an understanding of the resources managed in Trust for the account holder;
- Development of the universe of transactions that result in receipts to the account holder for the managed resources
- Development of a method to account for the receipts that should have been received from that universe.

Resources managed in Trust for the individual Indians will generally mirror the type of resources that are described in the AA Project for the Tribal accounts. During the AA Project these resource transactions were identified as:

- Surface Leases – e.g. allotments for grazing and agricultural [the growing of crops] purposes
- Oil and Gas Royalties
- Coal Royalties – the same approach would be considered for other extractive minerals such as sand & gravel.
- Timber Sales – e.g. sale of standing, dead or down timber [stumpage revenues]
- Other Surface Leases – e.g. hunting, fishing and right-of-way permits.

In developing approaches in the current ITMA project as well as for any large forensic investigation, an analysis of each of the revenue systems combined with some kind of sampling to determine error rates is a logical approach. Any sampling in this area will likely provide more confidence to those concerned with errors if it is stratified for selected attributes during selected time periods expected to result in error.

The parties would be well served to agree on a mutual approach to determining the attributes that could result in error, especially in the years when the document retention is expected to be low and the efforts to provide an accounting too prohibitive. If this has not already been done in the current sampling, then the selected attributes could be derived from several sources including perceived defects in each revenue collection system as well as anomalies in data entry.

If the parties could agree on what constitutes the proper periods, accounting system changes, particular area offices requiring closer scrutiny and other issues that they may determine, the work could be performed based on mutual agreement to resolve a significant question in the application of any current statistical work performed. That question is simply, why would the work on the electronic record period (starting in 1985) provide a reliable and relevant factor to apply to prior years that were manual and operated with different approaches and personnel?

Any error rates developed both for the current periods and the prior periods could be applied to groups of individual claimants. This would allow for the fact that not all individuals had identical sources of revenues. In addition to assisting in the development of an amount for the settlement process, such information could also be considered for use in determining the distribution process.

Receipts Recorded But Which Should Have Been for Greater Amounts

The concept of claims for what “should have been received” as related to alleged asset mismanagement will need to be explicitly addressed in any settlement.

This type of claim is as previously discussed focused on trust management not obtaining fair value for resources and other non cash or contractual issues. As discussed previously, it does not appear to be included in the settlement amounts discussed by the Plaintiffs.

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Disbursements

Eloise Cobell stated, “The proposed settlement makes a generous assumption on behalf of the government. It assumes for purposes of calculation that the government has enough records to prove that it accurately made 80 percent of the payments it was supposed to have made to trust beneficiaries and that it made them on time.” In contrast, Assistant Secretary James Cason in his testimony refers to samples in which supporting documents could be found for 99% of the tested transactions, with relatively small difference rates. However, as noted previously, the sample appears to be based on a period going back to at most 1985.

Therefore, questions to address for disbursements include:

- Do the Plaintiffs agree that the results of the study referred to by Assistant Secretary James Cason can be used to evaluate disbursements for the period tested?
- If not, can the parties mutually agree upon an approach to test the disbursements for the period in question? (If possible, this might involve a modified use of data already assembled as opposed to a totally new test.)

- Does the U.S. Government agree that the results of the study can not necessarily be extrapolated to earlier periods that involved different government systems?
- If so, can the parties agree on an approach to sample prior periods and extrapolate from the results?

Any forensic search for information over long periods of time, whether in a private sector trust arrangement or the trust arrangement established for Indian funds, is unlikely to provide complete information. The quantity and quality of such record retention will be highly dependent on the systems and processes that were in place over time, size and complexity of the systems and processes and the number of years under review when data was collected and recorded manually.

The cases I have worked on have helped to educate me with regard to some of the issues about the quality of records for Trust Funds held for Tribes as opposed to private sector Trust accounts. The following is a brief summary¹ of some of the process background that may be important in considering alternative solutions to determining an amount to settle ***Cobell v Norton***.

Before 1950 the responsibility for the maintenance of both Tribal and Individual Indian accounting records took place at the Agency level. Besides sending one copy of its monthly records to the BIA Central Office, each agency was responsible for the forwarding of its monthly reports to the Indian Claims Division of the General Accounting Office for an administrative audit. This practice ended in 1950-51.

¹Provided by Paul J. Gillis, based on his over 40 years of providing forensic accounting support related to Indian Tribal Claims.

In 1950 the Congress of the United States enacted legislation that revised the accounting system of the Government. Pursuant to that revision the primary responsibility for maintenance of the accounting records for both Tribal and Individual financial transactions was moved to the Area Office level.

In 1964-5 the BIA began to keep financial records by computer. It was at this point the BIA Central Finance Office West in Albuquerque, New Mexico began keeping records for the Tribes and Individuals. By 1971 the computer operations were such that the BIA Central Finance Office could assume the primary responsibility for maintenance of the financial records.

However, both the Agency and Area Office levels continued to maintain some duplicate or supporting records. With records being maintained at three different levels, Agency, Area Office and Central Office, discrepancies arose between the three sets of records as to transactions and as to balances of accounts. It may be worth noting that discrepancies in the financial records were noted as early as 1929 by the Comptroller General of the United States in an audit report submitted to the U.S. Senate.

The BIA employed agency-wide accounting systems to capture financial transactions. That is to say, each Agency or Area Office did not employ its own practices. They all followed a uniform system that was standard throughout the BIA. The practices and procedures employed within each system were adapted to meet the particular circumstances regarding the collection of revenues from different sources.

The above system description is to provide some understanding of the changes over time that might affect the accuracy of the record keeping. As more controls were put in place over time this would understandably improve the operations. The issue for disbursements in this matter is the possibility that payments were not properly recorded, or otherwise were paid for the benefit of others than the IIM account holder. The existence of a document supporting the disbursement is of course evidence, depending on the quality of the document. However, the absence of a specific document does not necessarily demonstrate that the payment was inappropriate. In a private trust dispute in which I participated as the lead accounting consultant (State of California and all Political Subdivisions vs Bank of America et al), the court found in a preliminary finding that gaps in records could be filled with other sources or records and that an accounting could be determined through statistical sampling or reconstruction, pending the presentation of the results. We learned in that forensic investigation that covered over 40 years that the reasons for non payment were more important than finding the source documents.

To rely on other sources and to use statistical results from periods with more complete document retention is probably not a completely satisfying answer to those who believe they are due funds. Consequently, some other approaches to show whether over time certain errors were or were not made in the accounts that would be unrelated to true disbursements should be reviewed. These could include:

- Test to determine whether transactions [entries] on the Control Accounts are supported by the aggregate dollar value of entries made to the IIM accounts of the individual Indians within an Agency or an Area Office.
- Test to determine whether large dollar and/or year-end transactions to the Control Accounts are for payments and not

entries to control accounts to get the account balances into agreement at all three levels: the Central Office, the Area Offices, and the Agencies. Such entries would not reflect actual financial transactions, but would merely be adjusting for unlocated errors and omissions.

In this matter one of the most difficult issues is accounting for periods where complete records are not available or the attempt to obtain the records would require unreasonable effort. Consequently, sampling that has already been performed is an important source of information to help develop attributes that suggest a higher susceptibility to error. The determination of the cause of errors should then be considered for any proposed extrapolation to other periods. It will help to develop the criteria and investigation procedures to determine or test the likely change in such errors in prior, untested periods.

A source of already available information that might assist the parties in analyzing earlier periods are audits that the GAO performed. The GAO began field and operational audits by 1951 or earlier. Thus, there exists a fifty year record of objective analysis of the BIA's operations.

- The audits were carried out contemporaneously with the financial operations that were being audited rather than many years later when records could have been lost and personnel familiar with the systems were no longer available for questioning.
- The audits included both the audits of operations at specific sites [Agencies, Area Offices, etc.] as well as the audit of bureau wide operations [the harvesting of timber, investment practices, mineral extraction, the leasing of lands, etc.].

- The GAO audits also included reviews of the financial systems utilized by the BIA, including the adequacy of their design, their suitability to their intended purposes, and the problems encountered in the actual application and operations of the systems.

Accordingly, it may be worth while for the parties to review the audit findings set out in the GAO audit reports. These findings may enable the parties to arrive at agreed methodologies.

What does that mean to the settlement of **Cobell v Norton**? I believe the statistical sampled work that has been completed for the IIM accounts should be reviewed by both parties to determine the usefulness for the periods tested and the extent it can be used for extrapolation to prior periods.

The issues are the same as they were for receipts. The parties need to mutually agree to an approach to use the available data or else agree upon methods for developing new data relevant to the current periods. They also need to agree on methods for testing older periods and/or applying extrapolation to them.

Other

I have not discussed the review of interest earned and received on the IIM accounts. Interest is a receipt and as such is subject to the same questions of whether it was recorded at all and, if so, for the appropriate amount. In some ways this aspect is easier to test. The rate paid is known from the Bureau of Indian Affairs records, the balances that should have been outstanding as computed in the accounting (whether through a full accounting or a sampling method) would be analyzed to see if the interest rate applied to those amounts would in fact result in the amount received. If not, an adjustment would need to be made for that amount. This is a more mechanical exercise once there is

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agreement on the amount that should be in the accounts. There could, however, be a separate question as to whether the rate paid was appropriate.

A handwritten signature in cursive script that reads "Sandra Johnigan". The ink is dark and the signature is fluid, with a large initial 'S' and a long, sweeping underline.

Date: February 27, 2006

Attachment A

SANDRA K. JOHNIKAN, CPA, CFE

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Ms. Johnigan has over 36 years of experience, of which 19 were with Arthur Young & Company (now Ernst & Young, LLP) where she was an audit partner, the National Office Chair of the Thrift Industry Group and the Real Estate Industry Group and Co-Chair of the Financial Services Group. Since 1990 she has provided litigation consulting and forensic investigation services through Johnigan, P.C. Engagements during this period have ranged from providing expert testimony to providing case management for law firms, such as coordinating the work of accounting and consulting professionals in preparation for trial and mediation.

Engagements have included such matters as the duties of officers and directors of publicly held companies, investigation of fraud, and the application of generally accepted auditing standards and generally accepted accounting principles to a wide variety of issues including internal controls, financial instruments, sub prime lending and revenue recognition for high tech companies. Forensic accounting matters have also included the reconstruction of municipal bond trust accounting records.

She is a member of the American Institute of CPAs (AICPA) Council. In addition she is a member of the AICPA Business Valuation and Forensic and Litigation Services Executive Committee. She participates in the AICPA's antifraud initiatives and in 2004 completed a three year term as chair of the AICPA Forensic & Litigation Services Committee which has oversight for a number of task forces including fraud. She has also participated in American Arbitration Association panels, as member and chair. See below for additional detail.

² Johnigan, P.C. has met the criteria for certification as a Women's Business Enterprise (WBE) and is certified as a WBE by the Women's Business Council – Southwest.

PROFESSIONAL AND SERVICE AFFILIATIONS

- Certified Public Accountant: Oklahoma 1970; Texas 1972; New York 1981
- Association of Certified Fraud Examiners
Member and certified 1993 to present
- American Institute of Certified Public Accountants
AICPA Council – elected 2004 for a three year term
AICPA Forensic and Litigation Services Volunteer of the Year - 2004
AICPA Business Valuation and Forensic and Litigation Services
Executive Committee – appointed 2004 for a one year term
AICPA Forensic & Litigation Services Committee:
Chair - 2001 to 2004; Member - 1998 to 2001
Editorial Adviser, “The Journal of Accountancy” – 2004 to present
Editorial Adviser, “The CPA Expert” – 2001 to present
Chair, 2001 AICPA National Conference on Advanced Litigation
Services
AICPA Savings and Loan Committee
Chair - 1983 to 1986; Member – 1982
- Texas Society of Certified Public Accountants
Member, Professional Standards Committee appointed 2004
Chair, Professional Standards Subcommittee on Accounting
Standards, 2004 to present
Member, TSCPA Litigation Services Member Section Committee 1999
to 2002
- American Arbitration Association (AAA)
Approved panel member 1993 to present
Participated in panels as both member and chair
- Federal Savings and Loan Advisory Committee
Member - 1986 to 1987
- Friends of the Dallas Public Library
Currently member of Board of Directors, Executive Committee,
Financial Oversight Committee and Treasurer

EXPERIENCE AND EDUCATION

- JOHNIGAN, P.C., owner 1990 to present
See opening description
- COAST-TO-COAST FINANCIAL CORPORATION
President and Director 1988 to 1990
- ARTHUR YOUNG & COMPANY (now Ernst & Young LLP) 1969 to 1988
Partner in National Office, New York, 1981 to 1988.
Co-Chair, Financial Services Group 1983 to 1988
Chair, Thrift Industry Group, 1983 to 1988.
Chair, Real Estate Industry Group, 1986 to 1988.
In addition, responsibilities included assisting clients in evaluating potential acquisitions, negotiating acquisitions, and coordinating post acquisition activities, as well as consulting on accounting and regulatory issues including meetings with SEC and other regulators.
Staff accountant, Manager, Principal in audit practice, primarily in Dallas, 1969 to 1981.
- UNIVERSITY OF TULSA, Graduated BSBA 1969, Major: Accounting