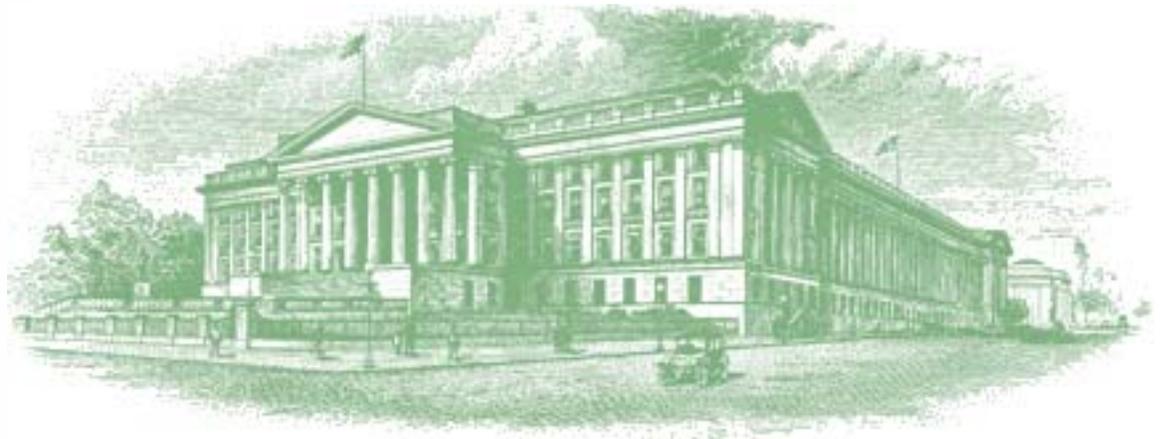




Audit Report



OIG-06-002

Management Letter for Fiscal Year 2004 Audit of the
Federal Financing Bank's Financial Statements

October 4, 2005

Office of
Inspector General

Department of the Treasury



OFFICE OF
INSPECTOR GENERAL

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

October 4, 2005

**MEMORANDUM FOR BRIAN D. JACKSON, CHIEF FINANCIAL OFFICER
FEDERAL FINANCING BANK**

FROM:

William H. Pugh *William H. Pugh*
Deputy Assistant Inspector General
for Financial Management and Information
Technology Audits

SUBJECT:

Management Letter for Fiscal Year 2004 Audit of
the Federal Financing Bank's Financial Statements

I am pleased to transmit the attached management letter in connection with the audit of the Federal Financing Bank's (FFB) Fiscal Year (FY) 2004 financial statements. We contracted with the independent certified public accounting firm of KPMG LLP to audit FFB's financial statements for FY 2004. The contract required that the audit be performed in accordance with generally accepted government auditing standards; applicable provisions of Office of Management and Budget Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*; and the *GAO/PCIE Financial Audit Manual*.

As part of its audit, KPMG LLP issued and is responsible for the accompanying management letter that discusses certain matters that were identified during the audit, which were not required to be included in the audit reports.

In connection with the contract, we reviewed KPMG LLP's letter and related documentation and inquired of its representatives. Our review disclosed no instances where KPMG LLP did not comply, in all material respects, with generally accepted government auditing standards.

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Should you have any questions, please contact me at (202) 927-5400, or a member of your staff may contact Mike Fitzgerald, Director, Financial Audits at (202) 927-5789.

Attachment

cc: Donald V. Hammond
Vice President, FFB

Roger Kodat
Vice President and Treasurer, FFB



KPMG LLP
2001 M Street, NW
Washington, DC 20036

June 10, 2005

Inspector General, U.S. Department of the Treasury, and the
Fiscal Assistant Secretary of the U.S. Department of the Treasury:

We have audited the financial statements of the Federal Financing Bank (the Bank), for the year ended September 30, 2004, and have issued our report thereon dated June 10, 2005. In planning and performing our audit of the financial statements of the Bank, we considered internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control. We have not considered internal control since the date of our report.

During our audit, we noted certain matters involving internal control and other operational matters that we present for your consideration. These comments and recommendations are summarized in Exhibit I and have been discussed with the appropriate members of management and are intended to improve internal control or result in other operating efficiencies. We also provide in Exhibit II the status of the comments and recommendations included in our letter arising from the fiscal year 2003 audit.

Our audit procedures are designed primarily to enable us to form an opinion on the financial statements, and therefore, may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of the Bank gained during our work to make comments and suggestions that we hope will be useful to you.

This report is intended solely for the information and use of the Bank's management, the U.S. Department of the Treasury's Office of Inspector General, the U.S. Government Accountability Office, OMB, 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

FEDERAL FINANCING BANK

Comments and Recommendations

September 30, 2004

1. Financial Reporting Standards

The Federal Accounting Standards Advisory Board (FASAB), the accounting standards-setting body for the Federal Government, has allowed the Bank and other Federal entities that issued financial statements prior to October 1999 using Financial Accounting Standards Board (FASB) accounting principles, to either continue doing so or to issue financial statements using FASAB accounting principles. The Bank elected to continue issuing financial statements using FASB accounting principles. The Bank also prepares financial statements and related disclosures using the FASAB accounting principles; however, the Bank only provides this information to the U.S. Department of the Treasury for consolidation into the Treasury Department-wide financial report. As a result, users of the Bank's financial statements do not receive key information that is required to be disclosed under FASAB accounting principles, such as:

- Mission, programs, and related organizational structure;
- Most important challenges;
- Assessment of the reliability and completeness of the performance and financial data in the financial report and management's plan to address any deficiencies;
- Statement of assurance indicating whether (a) management controls are in place and (b) financial systems conform with government-wide standards;
- Systems, controls, and compliance with applicable laws and regulations;
- Forward-looking information regarding significant demands, risks, uncertainties, events, conditions, and trends;
- Performance goals and results;
- Financial statement highlights;
- Statement of budgetary resources; and
- Statement of financing.

Recommendation

We recommend that the Bank consider issuing a single set of financial statements using the FASAB accounting principles. This will eliminate the additional effort required to prepare two sets of financial statements, eliminate financial statement differences that result from applying different accounting principles, and provide additional financial information to users of the Bank's financial statements.

Management Response

Management does not concur with the finding and recommendation. Since the Bank was established as a "Wholly Owned Government Corporation", 31 U.S.C. Chapter 91, Section 9106 under Management reports, states that the management report to congress shall include: "a statement of financial position, a statement of operations, and a statement of cash flows". FASAB standards do not make reference to these schedules.

Along with the management report to congress, the Bank's user community includes a mailing list of influential channels for the media and financial community that are typically accustomed to reviewing the public statements

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Comments and Recommendations

September 30, 2004

of financial institutions. The analysis of a financial institution is fairly unique requiring a narrowly defined level of knowledge and experience not generally possessed by evaluators of financial statements for other industries. This community is not and would not be familiar with FASAB statements in general and more specifically the FASAB format of financial presentation clearly does not capture the key financial measurements of a financial institution. In conclusion, the Bank's financial user community would find it problematic to translate FASAB statements into key statistics historically based upon FASB generated data. Most importantly should the Bank successfully execute its long range strategic goal to expand the depth and complexity of its operations, that user community would become even broader and become more demanding with regard to the financial detail provided by the Bank.

Though the financial schedules for FASAB are incompatible with the operations of a bank, such details as "mission, programs, organizational structure, forward-looking information regarding significant demands, risks, uncertainties, events, conditions, and trends, etc." are typically found in an MD&A. While an MD&A is not a requirement for FASB statements it is often provided by companies either due to regulation or for the benefit of private investors. Therefore, as an alternative to a change to FASAB presentation, we would propose that the FFB include an MD&A with its annual statements in the future.

Auditors' Response to Management's Response

We understand that 31 U.S.C. Chapter 91, Section 9106 under Management reports, states that the Bank's report to congress shall include: "a statement of financial position, a statement of operations, and a statement of cash flows; however, the legislation does not indicate the accounting standards that the Bank should follow and the financial statements for a federal entity provide the financial information included in statement of financial position, a statement of operations, and a statement of cash flows. We also understand the Bank's need to report the appropriate financial information to meet user needs.

2. Memorandum of Agreement

The Bank does not have a signed Memorandum of Agreement between the Bank and the Network Administration personnel responsible for the Departmental LAN and the Operations Management responsible for the system platform. The Bank indicated that the agreement is not signed because U.S. Department of the Treasury's Legal Counsel needs to review the agreement before it is approved by the Bank and other parties.

Recommendation

We recommend that the U.S. Department of the Treasury's Legal Counsel complete their review of the MOA and that Bank management and the other parties sign the MOA.

Management's Response

Management concurs with the finding and recommendation. The MOA was reviewed by counsel, signed by FFB management and delivered to the Chief Information Officer for Treasury.

3. System Development Methodology and Configuration Management Plan

The Bank has implemented certain programming changes without a formally documented system development methodology plan or configuration management plan. National Institute of Standards and Technology Special

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Publication (NIST SP) 800-18, *Guide for Developing Information Technology Security Plans*, includes requirements and guidance on planning for security applicable to systems development life cycle stages.

Recommendation

We recommend that the Bank formally document its system development methodology and configuration management plans. The system development methodology plan should include programming naming conventions, a description of the system development phases, procedures to be performed in each phase, emergency program change procedures, application test procedures, as well as a development, test and production access control lists. The configuration management plan should discuss the process for migrating LMCS source code changes into the production environment and the DEC Code Management System as well as the dual password authentication process.

Management's Response

Management concurs with the finding and recommendation. Over the past year Bank management has completed a review of the capabilities of the LMCS system in relation to the forward strategic plan for the Bank. As a result of this review management has concluded that a broader reconfiguration of the LMCS system is required in order to more effectively support future operations. The scope of this reconfiguration is such that it will be necessary to engage third party expertise to assist in project planning and execution. One of the key deliverables of this assistance will be the design and documentation of a system development methodology and configuration management plan.

4. Policies

The U.S. Department of the Treasury Information Systems group responsible for the creation of applicable policies and procedures for all of Treasury's information systems does not have policies related to segregation of duties. The *Information Systems Audit and Control Foundation's Governance, Control and Audit for Information and Related Technology*, states that management should implement a division of roles and responsibilities and establish policies to ensure that personnel are performing only those duties stipulated for their position.

Recommendation

We recommend that the Bank work with the Information Systems group to develop and distribute a policies addressing segregation of duties. The policy should emphasize that it is the responsibility of management to ensure that incompatible duties are not assigned to any one individual. This will help ensure that responsibilities are properly segregated.

Management's Response

Management concurs with the finding and recommendation; however, management cannot require the Information Systems group to implement the recommendation.

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Status of Prior Year Management Letter Comments

Prior Year Recommendations	Current Year Status
1. Accounting Policy and Procedures Manual	This comment has been corrected.
2. VAX/Alpha Platform Certification and Accreditation	This comment has been corrected.
3. Memorandum of Agreement	This comment has not been corrected and is repeated as comment 2.
4. Designated Approving Authority	This comment has been corrected.
5. System Development Methodology and Configuration Management Plan	This comment has not been corrected and is repeated as comment 3.
6. Software Program Changes	This comment has been corrected.
7. Passwords	This comment has been corrected.
8. Policies	This comment has not been corrected and is repeated as comment 4.
9. Storage of Back Up Tapes at Off-site Facility	This comment has been corrected.