Audit Report

OIG-12-020

Management Letter for the Audit of the United States Mint's Fiscal Years 2011 and 2010 Financial Statements

December 5, 2011

Office of Inspector General

Department of the Treasury

OFFICE OF
INSPECTOR GENERAL

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

December 5, 2011

MEMORANDUM FOR RICHARD A. PETERSON, DEPUTY DIRECTOR
UNITED STATES MINT

FROM: Michael Fitzgerald
Director, Financial Audits

SUBJECT: Management Letter for the Audit of the United States Mint's Fiscal Years 2011 and 2010 Financial Statements

I am pleased to transmit the attached management letter in connection with the audit of the United States Mint's (Mint) Fiscal Years 2011 and 2010 financial statements. Under a contract monitored by the Office of Inspector General, KPMG LLP, an independent certified public accounting firm, performed an audit of the financial statements of the Mint as of September 30, 2011 and 2010, and for the years then ended. 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. 07-04, *Audit Requirements for Federal Financial Statements,* as amended; 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 other matters involving internal control over financial reporting and its operation that were identified during the audit but were not required to be included in the auditors' 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.

Should you have any questions, please contact me at (202) 927-5789 or a member of your staff may contact Shiela Michel, Manager, Financial Audits, at (202) 927-5407.

Attachment

THE UNITED STATES MINT

Management Letter

Fiscal Year 2011

Transmittal Letter 3

Appendix A – Fiscal Year 2011 Management Letter Comments 4

Asset Management

A-1 Controls over Retirements Should be Strengthened 4

A-2 Controls over Assets Should be Strengthened 6

Inventory Management

B-1 Controls over Annual Physical Inventory Procedures should be Strengthened 9

Budgetary Resources

C-1 Controls over Review of Open Obligations Should be Strengthened 10

Appendix B – United States Mint's Response to Management Letter Comments FY 2011 12

Appendix C – Status of Prior Year Management Letter Comments 13

KPMG LLP
2001 M Street, NW
Washington, DC 20036-3389

December 2, 2011

Inspector General
United States Department of the Treasury
740 15th Street, NW, Suite 600
Washington, DC 20220

Deputy Director
The United States Mint
801 9th Street, NW
Washington, DC 20001

Gentlemen:

In planning and performing our audit of the financial statements of the United States Mint (Mint), as of and for the years ended September 30, 2011 and 2010, in accordance with auditing standards generally accepted in the United States of America, we considered the Mint's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements but not for the purpose of expressing an opinion on the effectiveness of the Mint's internal control. Accordingly, we do not express an opinion on the effectiveness of the Mint's internal control.

During our audit we noted certain matters involving internal control and other operational matters that are presented for your consideration. These comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve internal control or result in other operating efficiencies and are summarized in Appendix A.

In addition, we identified a deficiency in internal control that we consider to be a significant deficiency, and communicated it in writing to management and those charged with governance on December 2, 2011.

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 Mint's organization gained during our work to make comments and suggestions that we hope will be useful to you.

We would be pleased to discuss these comments and recommendations with you at any time.

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

Very truly yours,

KPMG LLP

KPMG LLP is a Delaware limited liability partnership, the U.S. member firm of KPMG International Cooperative ("KPMG International"), a Swiss entity.

Asset Management

A-1 Controls over Retirements Should be Strengthened

We noted the following during our interim testwork over property, plant and equipment:

- For two out of 57 samples tested, the retirement form (USM-207 or SF-120) was not provided.
- For three out of 57 samples tested, the assets were not removed from the Enterprise Resource Planning (ERP) system within 30 days of the date of disposal.
- For one out of 57 samples tested, the asset was sold for $4,534 and the gain was recorded in the Other revenue account instead of on Gains on Disposition of Assets - Other account.

Per The United State Mint's Standard Operating Procedures (SOP), titled Recording Fixed Asset and Property Retirements:

> A USM-207 form and an SF-120 form (id the property is excess to GSA) is prepared listing the equipment with identifying information (i.e., barcode number, type of property, location of property, reason for action, book value, and the Plant, if in the field) and sent to the Property Management Office and Financial Manager (FM).
>
> The Fixed Assets Accountant will remove the asset from the ERP System within 30 days of the asset being physically removed from the premises, and ensure that the proper files (i.e., copy of USM-207 form, appropriately signed by the Plant Manager, Officer-In-Charge, CIO, CFO, or their designees; an SF-120 form, if applicable, with appropriate authorizing signature by the Property Manager; and any emails or other documents related to the disposal of the asset) are maintained.

Per the Statement of Federal Financial Accounting Standards 6, *Accounting for Property, Plant and Equipment*, paragraphs 38-39:

> In the period of disposal, retirement, or removal from service, general PP&E shall be removed from the asset accounts along with associated accumulated depreciation/amortization. Any difference between the book value of the PP&E and amounts realized shall be recognized as a gain or a loss in the period that the general PP&E is disposed of, retired, or removed from service.
>
> General PP&E shall be removed from general PP&E accounts along with associated accumulated depreciation/amortization, if prior to disposal, retirement or removal from service, it no longer provides service in the operations of the entity. This could be either because it has suffered damage, becomes obsolete in advance of expectations, or is identified as excess.

Per OMB Circular No. A-123, *Management's Responsibility for Internal Control*, (revised December 31, 2004), Section II, Subsection C, Paragraph 1:

> Control activities include policies, procedures and mechanisms in place to help ensure that agency objectives are met. Several examples include: proper segregation of duties (separate personnel with authority to authorize a transaction, process the transaction, and review the transaction); physical controls over assets (limited access to inventories or equipment); proper authorization; and appropriate documentation and access to documentation.

The causes are as follows:

- Policies and procedures were not followed to ensure that the disposals of assets were properly documented.
- Policies and procedures were not followed to ensure that the retirement form was submitted in a timely manner in order for assets to be removed from the ERP system within 30 days.
- Policies and procedures did not specify the proper accounting policies for recording the gain from the sale of assets.

The effects are as follows:

- Inadequate internal controls do not allow the timely detection and correction of errors or irregularities related to the timeliness of asset disposals.
- Assets may be not removed from the Mint's records on a timely basis which could result in inaccurate gain/loss calculations and/or an overstatement of depreciation expense.
- Gain on Disposition of Assets - Other (account 711001) is understated by $4,534 and Other revenue (account 590001) is overstated by $4,534.

We recommend that Mint management:

1. Follow the SOP to ensure that retirement forms are properly completed, filed and ensure that the forms are available for examination for a reasonable time period after the retirement transaction.
2. Follow the SOP to ensure that assets are removed from the ERP system within 30 days of the date of disposal.
3. Record a journal entry to properly account for the gain on disposition of asset.
4. Update the SOP to ensure it includes procedures on how to properly account for gains/losses from the disposition of asstes.

A-2 Controls over Assets Should be Strengthened

We noted the following during our interim testwork over Property, Plant and Equipment (PP&E) additions, capitalizations and adjustments:

Timeliness of placing assets into a PP&E depreciable account:

- For one out of 30 addition samples tested, with a cost of $32,637, the asset should have been placed into service in the prior fiscal year (FY), but was not moved from Construction in Progress (CIP) into a depreciable account until the current FY.
- For two out of 30 addition samples tested and four out of 15 capitalized samples tested, the assets were not moved to a PP&E depreciable account in a timely manner within the current FY. This condition does not have a monetary effect.
- For six out of 14 capitalized samples tested and 14 out of 27 adjustment samples tested, adjustments were made to the assets after they were in service. This condition does not have a monetary effect.
- For one out of 27 adjustment samples tested, with a cost of $24,806, an adjustment was made to the asset after it was in service. The asset was placed in service in the prior FY. This also resulted in the understatement of the FY 2010 Depreciation, Amortization and Depletion and Accumulated Depreciation on Equipment's beginning balance of $689 and FY 2011 depreciation expense overstatement of $689.

Capitalizing Costs:

- For one out of 14 capitalized samples tested, freight and software costs of $5,187 were incorrectly expensed instead of capitalized. In addition, depreciation expense is understated by $172.
- For one out of 27 adjustments samples tested, cost of $93,342 was capitalized instead of being expensed. In addition, depreciation expense is overstated by $69,617.

Per The United State Mint's Standard Operating Procedures, titled Determining when Construction in Process Assets become Capital Assets:

> Each month, the Fixed Assets (FA) Accountant meets with the U.S. Mint Engineers to get status of each CIP asset.
>
> The FA Accountant uses the information given by the Engineers to update the status of each CIP asset and tracks the information in an Excel spreadsheet.
>
> If it is determined that a CIP asset is completed and ready to be placed into production, the Engineers/Contracting Officer Technical Representative (COTR)s will issue a Project Closeout Form or an e-mail that details the relevant project closeout information in it to the Fixed Assets Accountants alerting them that the equipment has been approved for production. The memorandum or e-mail will include information about the asset and will identify the date placed into service, a description of the asset, the cost of it, along with any other relevant information.

In the event that the U.S. Mint field offices do not receive a copy of the Project Closeout Form or e-mail from the Engineers, the Accounting Office will then, communicate to the U.S. Mint field office(s) that this equipment should begin to be capitalized from the date that the asset was placed into service.

Per the Statement of Federal Financial Accounting Standards No 6, *Accounting for Property, Plant and Equipment*:

Paragraph 26

All general PP&E shall be recorded at cost. Cost shall include all costs incurred to bring the PP&E to a form and location suitable for its intended use. For example, the cost of acquiring property, plant, and equipment may include:

- transportation charges to the point of initial use.
- fixed equipment and related installation costs required for activities in a building or facility.

Paragraph 35

Depreciation expense is calculated through the systematic and rational allocation of the cost of general PP&E, less its estimated salvage/residual value, over the estimated useful life of the general PP&E.

Paragraph 37

Costs which either extend the useful life of existing general PP&E, or enlarge or improve its capacity shall be capitalized and depreciated/amortized over the remaining useful life of the associated general PP&E.

Per the Statement of Federal Financial Accounting Standards No. 10, *Accounting for Internal Use Software*:

Paragraph 22

Computer software that is integrated into and necessary to operate general PP&E, rather than perform an application, should be considered part of the PP&E of which it is an integral part and capitalized and depreciated accordingly.

Per OMB Circular No. A-123, *Management's Responsibility for Internal Control*, (revised December 31, 2004):

Section II, Subsection C, Paragraph 1

Control activities include policies, procedures and mechanisms in place to help ensure that agency objectives are met. Several examples include: proper segregation of duties (separate personnel with authority to authorize a transaction, process the transaction, and review the transaction); physical controls over assets (limited access to inventories or equipment); proper authorization; and appropriate documentation and access to documentation.

The causes are as follows:

- The COTRs have a different interpretation of determining when a CIP asset is complete and ready to be placed into production compared to the FA Accountants. Additionally, the COTR's are not communicating to the FA Accountant in a timely manner when the CIP assets should be placed into service in the system.
- The Mint is not capitalizing the entire cost of the asset when the asset is placed into production, but is adjusting the asset cost as invoices are received.
- The Mint is not following accounting standards when determining the treatment of costs related to PP&E.
- A cost which neither extends the useful life of the asset nor enlarged or improved its capacity was capitalized as part of the asset.

The effects are as follows:

- CIP's beginning balance was overstated by $32,637.
- Asset Clearing Account's beginning balance was overstated by $24,806.
- Equipment's beginning balance was understated by $57,443.
- FY 2010 Depreciation, Amortization and Depletion expense was understated by $689.
- Accumulated Depreciation on Equipment's beginning balance was understated by $689.
- Equipment is overstated by $88,154.
- Operating expense is understated by $88,154.
- Depreciation expense is overstated by $70,134.

We recommend that Mint management:

1. Enforce compliance with the SOP for determining when CIP assets become capital assets to ensure PP&E are timely and accurately moved to a depreciable account and begin depreciation in the correct period.
2. Ensure that all costs related to an asset, including the costs of acquiring the asset, are capitalized.
3. Ensure that costs that do not extend the useful life of an existing PP&E, or enlarge or improve its capacity are not capitalized.
4. Adjust the appropriate property related accounts to correct for the effects of this finding.

Inventory Management

B-1 Controls over Annual Physical Inventory Procedures should be Strengthened

We noted the following during the fourth quarter physical inventory at the Mint contractor-operated distribution facility, Pitney Bowes:

- 23 tanks of scrap metal, with an approximate cost of $460,000, were not included in the annual physical inventory (API).
- Tornado damaged goods (PBT) received from the PFS Web facility (the Mint's previous contractor-operated distribution facility), with an approximate cost of $300,000, were not included in the API.

Per OMB Circular No. A-123, *Management's Responsibility for Internal Control*, (revised December 31, 2004), Section II, Subsection C, Paragraph 1

> Control activities include policies, procedures and mechanisms in place to help ensure that agency objectives are met. Several examples include: proper segregation of duties (separate personnel with authority to authorize a transaction, process the transaction, and review the transaction); physical controls over assets (limited access to inventories or equipment); proper authorization; and appropriate documentation and access to documentation.

Per Statement of Federal Financial Accounting Standards Number 3, *Accounting for Inventory and Related Property*, Paragraphs 29 and 30.

> EXCESS, OBSOLETE, AND UNSERVICEABLE INVENTORY.
>
> "Unserviceable inventory" is damaged inventory that is more economical to dispose of than to repair. The category "excess, obsolete and unserviceable inventory" shall be either (1) included in the inventory line item on the face of the financial statements with separate disclosure in footnotes or (2) shown as a separate line item on the face of the financial statements.
>
> Such inventory shall be valued at its expected net realizable value. The difference between the carrying amount of the inventory before identification as excess, obsolete or unserviceable and its expected net realizable value shall be recognized as a loss (or gain) and either separately reported or disclosed. Any subsequent adjustments to its net realizable value or any loss (or gain) upon disposal shall also be recognized as a loss (or gain).

Per United States Mint's Standard Operating Procedures (SOP), titled Numismatic Warehouse Physical Inventory:

> 1.3 Definitions: Non-Inventory Items: material not required to be included in the wall-to-wall count, including envelopes, sleeves, certificates of authenticity (COAs), capsules, boxes and other replacement-type material with no metal content.

The cause is as follows:

- The SOP over the numismatic warehouse physical inventory was not followed. Scrap metal and tornado-damaged inventory was recorded as "non-inventory items" and was not included in the wall-to-wall count.

The effects are as follows:

- Raw Material (Account 152501) was understated by $460,000.
- Finished Goods (Account 152701) was understated by $300,000.

We recommend that Mint management:

1. Follow the Numismatic Warehouse Physical Inventory SOP, and require that all inventory be counted during the physical inventory.
2. Adjust the appropriate inventory related accounts to correct for the effects of this finding.

Budgetary Resources

C-1 Controls over Review of Open Obligations Should be Strengthened

We noted the following during our interim test work over open obligations:

- For one out of 73 samples tested, the obligation was not valid as of June 30, 2011 and should have been de-obligated. We also noted that this obligation was not de-obligated as of September 30, 2011.

We noted the following during our final test work over open obligations:

- For five out of 67 samples tested, the obligations were not valid as of September 30, 2011 and should have been de-obligated.

Per OMB Circular No. A-123, *Management's Responsibility for Internal Control*, (revised December 31, 2004), Section II, Subsection C, Paragraph 1

> Control activities include policies, procedures and mechanisms in place to help ensure that agency objectives are met. Several examples include: proper segregation of duties (separate personnel with authority to authorize a transaction, process the transaction, and review the transaction); physical controls over assets (limited access to inventories or equipment); proper authorization; and appropriate documentation and access to documentation.

Federal Managers Financial Integrity Act of 1982 (FMFIA)

> (d) (1) (A) To ensure compliance with the requirements of subsection (a)(3) of this section, internal accounting and administrative controls of each executive agency shall be established in accordance with standards prescribed by the Comptroller General, and shall provide reasonable assurances that –
>
> (i) obligations and costs are in compliance with applicable law

(ii) funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and

(iii) revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the assets.

Per United States Mint's Standard Operating Procedures, titled Open Obligations Review

Procurement Research and Review:

1. (Contract Specialist) Review all items in the file and determine appropriate action, including contacting the COTRs for assistance with the review, if needed. Note dispensation of every of item within two weeks from receipt of file. Dispensation notation should explain the status, for example "open-still a valid contract" or "de-obligated, contract modified on 3/15/09" or "error-contacted ARC to resolve on 3/15/09."

3. (Contract Specialist) De-obligate items determined to be paid and closed. This shall be done by taking appropriate action in PRISM to modify the contract to reflect the final status of the contract. De-obligations should be completed by the 5th business day from the quarter end.

The causes are as follows:

- The quarterly open obligations review was performed; however, not all obligations that were invalid were identified as needing to be closed.
- Obligations that were identified as needing to be researched and closed were not de-obligated in a timely manner.

The effect is as follows:

- The Undelivered Orders (UDO) balance is overstated by $9,486,481.54 as of 9/30/2011. The most likely error in the UDO population is $18,700,549.44.

We recommend that Mint management:

1. Strengthen controls over the quarterly review and de-obligation of open obligations at year end.
2. Perform a reconciliation of obligations in PRISM to open obligations in Oracle.
3. Adjust the UDO balance to correct for the effect of this finding.

DEPARTMENT OF THE TREASURY
UNITED STATES MINT
WASHINGTON, D.C. 20220

December 2, 2011

KPMG LLP
2001 M Street N.W.
Washington, DC 20036

Ladies and Gentlemen:

We have reviewed the fiscal year 2011 auditors' report and are in substantial agreement with the reported observations. The United States Mint recognizes the need for strong internal controls and is taking corrective actions to address the noted deficiencies. We have made significant progress toward resolving the reported issues and will continue to work with KPMG and the Office of Inspector General in identifying the specific actions that will ensure we have taken appropriate corrective action.

Sincerely,

David Motl
Acting Associate Director/Chief Financial Officer
United States Mint

THE UNITED STATES MINT

Status of Prior Year Management Letter Comments

Fiscal Year 2011 Management Letter

Fiscal Year 2010 Management Letter Comment	Fiscal Year 2011 Status
Human Resources	
A-1 Controls over the Segregation of Duties within WebTA should be strengthened	Closed.
Asset Management	
B-1 Controls over Assets Should be Strengthened	Repeated: See fiscal year 2011 revised comment at A-2.
B-2 Controls over Retirements Should be Strengthened	Repeated: See fiscal year 2011 revised comment at A-1.
Revenue and Accounts Receivables	
C-1 Controls over Numismatic Accounts Receivables should be strengthened	Closed.
Inventory Management	
D-1 Controls over Quarterly Physical Inventory Procedures should be Strengthened	Closed.
D-2 Controls over the Calculation of the Weighted Average Adjustment should be Strengthened	Closed.