



# Audit Report



OIG-12-030

Audit of the Bureau of Engraving and Printing's Fiscal Years  
2011 and 2010 Financial Statements

December 16, 2011

Office of  
Inspector General

Department of the Treasury



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

OFFICE OF  
INSPECTOR GENERAL

December 16, 2011

**MEMORANDUM FOR LARRY R. FELIX, DIRECTOR  
BUREAU OF ENGRAVING AND PRINTING**

**FROM:** Michael Fitzgerald  
Director, Financial Audits

**SUBJECT:** Audit of the Bureau of Engraving and Printing's  
Fiscal Years 2011 and 2010 Financial Statements

I am pleased to transmit the attached audited Bureau of Engraving and Printing (BEP) financial statements for fiscal years 2011 and 2010. 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 BEP 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*.

The following reports, prepared by KPMG LLP, are incorporated in the attachment:

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

In its audit, KPMG LLP found that the financial statements were fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. KPMG LLP also found that management's assertion that BEP maintained effective internal control over financial reporting as of September 30, 2011 was fairly stated in all material respects. However, KPMG LLP identified an internal control deficiency related to year end liability accruals that was considered a significant deficiency. Further, KPMG LLP found no instances of reportable noncompliance with laws and regulations tested.

KPMG LLP also issued a management letter dated December 14, 2011 discussing certain 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. This letter will be transmitted separately.

In connection with the contract, we reviewed KPMG LLP's reports and related documentation and inquired of its representatives. Our review, as differentiated from an audit in accordance with generally accepted government auditing standards, was not intended to enable us to express, and we do not express, opinions on BEP's financial statements or BEP management's assertion on the effectiveness of internal control over financial reporting, or a conclusion on compliance with laws and regulations. KPMG LLP is responsible for the attached auditors' reports dated December 14, 2011 and the conclusions expressed in the reports. However, 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 DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING**

**Financial Statements**

**Years ended September 30, 2011 and 2010**

(With Independent Auditors' Reports Thereon)

**THE DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING  
FINANCIAL STATEMENTS  
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010**

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

## Independent Auditors' Report

The Inspector General, Department of the Treasury and  
The Director of the Bureau of Engraving and Printing, Department of the Treasury:

We have audited the accompanying balance sheets of the Bureau of Engraving and Printing (the Bureau) as of September 30, 2011 and 2010, and the related statements of operations and cumulative results of operations, and cash flows (hereinafter referred to as "financial statements") for the years then ended. These financial statements are the responsibility of the Bureau's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended. Those standards and OMB Bulletin No. 07-04 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Bureau of Engraving and Printing as of September 30, 2011 and 2010, and the results of its operations, and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

We have also examined in accordance with attestation standards established by the American Institute of Certified Public Accountants, and the standards applicable to attestation engagements contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, management's assertion, included in the accompanying Management's Report on Internal Controls Over Financial Reporting, that the Bureau maintained effective internal control over financial reporting as of September 30, 2011, and have issued our report thereon dated December 14, 2011. 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 fiscal year 2011 audit.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 14, 2011, on our tests of the Bureau's compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion 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 fiscal year 2011 audit.

**KPMG LLP**

December 14, 2011

**THE DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING**

Balance Sheets

As of September 30, 2011 and 2010

	(In Thousands)	
	2011	2010
<b>ASSETS</b>		
Current assets		
Cash (Note 3)	\$ 130,178	\$ 153,662
Accounts receivable (Note 10)	38,436	28,622
Inventories, net (Note 4)	148,826	140,229
Prepaid expenses	3,698	3,908
Total current assets	321,138	326,421
Property and equipment, net (Note 5)	381,507	346,358
Other assets, net (Note 6)	20,220	16,706
Total assets	\$ 722,865	\$ 689,485
<b>LIABILITIES AND EQUITY</b>		
Liabilities		
Current liabilities (Notes 7 and 8)		
Accounts payable	\$ 33,683	\$ 20,044
Accrued liabilities	35,949	33,513
Advances	8,460	11,321
Total current liabilities	78,092	64,878
Workers' compensation liability (Note 8)	62,423	58,835
Total liabilities	140,515	123,713
Contingencies and commitments (Notes 12 and 13)		
Equity		
Invested capital	32,435	32,435
Cumulative results of operations	549,915	533,337
Total equity	582,350	565,772
Total liabilities and equity	\$ 722,865	\$ 689,485

See accompanying notes to the financial statements.

**THE DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING**

Statements of Operations and  
Cumulative Results of Operations

For the Years Ended September 30, 2011 and 2010

		(In Thousands)	
		<u>2011</u>	<u>2010</u>
Revenue from sales (Note 10)	\$	548,094	\$ 631,422
Cost of goods sold		<u>442,769</u>	<u>508,832</u>
Gross margin		<u>105,325</u>	<u>122,590</u>
Operating costs:			
General and administrative expenses		80,433	67,448
Research and development		<u>8,314</u>	<u>11,714</u>
		<u>88,747</u>	<u>79,162</u>
Excess of revenues over expenses		16,578	43,428
Cumulative results of operations at beginning of year		<u>533,337</u>	<u>489,909</u>
Cumulative results of operations at end of year	\$	<u><u>549,915</u></u>	\$ <u><u>533,337</u></u>

See accompanying notes to the financial statements.



**THE DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING**

Statements of Cash Flows

For the Years Ended September 30, 2011 and 2010

	(In Thousands)	
	<b>2011</b>	<b>2010</b>
<b>Cash flows from operating activities</b>		
Excess of revenues over expenses	\$ 16,578	\$ 43,428
Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities:		
Depreciation	32,566	27,759
Loss from inventory obsolescence	720	917
Loss from disposal of property and equipment	53	—
Changes in assets and liabilities		
(Increase) decrease in accounts receivable	(9,814)	367
(Increase) decrease in inventories	(8,729)	8,954
Decrease in prepaid expenses	210	1,351
Increase in other assets	(4,102)	(1,176)
Increase in accounts payable	13,639	3,106
Increase (decrease) in accrued liabilities	2,436	(4,500)
Decrease in advances	(2,861)	(2,744)
Increase in workers' compensation liability	3,588	2,868
Net cash provided by operating activities	44,284	80,330
<b>Cash flows from investing activities</b>		
Purchases of property and equipment	(67,768)	(66,188)
Net cash used in investing activities	(67,768)	(66,188)
Net increase (decrease) in cash	(23,484)	14,142
Cash at beginning of year	153,662	139,520
Cash at end of year	\$ 130,178	\$ 153,662

See accompanying notes to the financial statements.

**THE DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING**

Notes to the Financial Statements

September 30, 2011 and 2010

**1. Reporting Entity**

The Bureau of Engraving and Printing (Bureau), a component of the United States (U.S.) Department of the Treasury, is the U.S. Government's security printer. The Bureau designs and produces U.S. currency. The Bureau also advises and assists federal agencies in the design and production of other U.S. Government documents requiring counterfeit deterrence or secure production.

The Bureau operates under basic authorities conferred by the Act of July 11, 1862, (12 Stat. 532; also, 31 U.S.C. 5114) and other laws and regulations. In accordance with the provisions of Public Law 81-656, effective August 4, 1950, the operations of the Bureau are financed by means of a revolving fund. This fund is reimbursed through billings to the Bureau's customers for products delivered. Public Law 95-81 authorized the Bureau to include in its product prices an amount to provide funding for the acquisition of capital equipment and future working capital. Invested capital represents the historical value of the initial contribution made by the Federal Government.

The financial statements represent the consolidation of two federal revolving funds. The majority of all financial transactions are contained in the Bureau of Engraving and Printing Revolving Fund, which finances Bureau operations. The other revolving fund, the Mutilated Currency Revolving Fund, is used to redeem damaged paper currency received from the public. All significant balances and transactions between the funds have been eliminated in consolidation.

**2. Summary of Significant Accounting Policies**

*Basis of Accounting*

The Bureau has historically prepared its financial statements in conformity with U.S. generally accepted accounting principles (GAAP), based on accounting standards issued by the Financial Accounting Standards Board (FASB), the private-sector standards-setting body. Under such standards, the Bureau prepares its financial statements using the full accrual basis of accounting under which revenues are recognized when earned and expenses are recognized as incurred, regardless of when cash is exchanged.

The Federal Accounting Standards Advisory Board (FASAB) has been designated by the American Institute of Certified Public Accountants as the standards-setting body for financial statements of Federal Government entities, with respect to the establishment of GAAP. FASAB has indicated, however, that financial statements prepared based upon accounting standards published by the FASB may also be regarded as in conformity with GAAP for those federal agencies, such as the Bureau, that have issued financial statements based upon FASB accounting standards in the past. Accordingly, consistent with historical reporting, the Bureau's financial statements are presented in accordance with accounting standards published by the FASB.

**THE DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING**

Notes to the Financial Statements

September 30, 2011 and 2010

*Estimates*

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related revenues and expenses. Those estimates most significant to the Bureau's financial statements are the actuarial estimates made by the Department of Labor (DOL) in arriving at the liabilities for workers' compensation, allowances for obsolescence, the useful lives of property and equipment, the likelihood of losses associated with contingent liabilities, and certain accrued expenses at the date of the financial statements. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed herein.

*Cash*

Cash represents the aggregate amount of the Bureau's funds held on deposit with the U.S. Treasury and are available to pay liabilities.

*Inventories*

Raw material and supply inventories are stated at standard cost, except for one advanced counterfeit deterrent material, which is valued using the first-in-first-out (FIFO) method. Finished goods inventories are stated at weighted average unit cost. All methods approximate actual cost. Cost elements included in work-in-process and finished goods inventories are direct materials, direct labor, manufacturing overhead and manufacturing support.

*Property and Equipment*

Property and equipment are recorded at cost. Major alterations and renovations are capitalized, while maintenance and repair costs are charged to expense as incurred. The capitalization threshold is \$50,000. The Bureau capitalizes all cost associated with new construction and building improvements.

The Bureau occupies and uses buildings and land owned by the Department of the Treasury. The Bureau is not charged for the use of the buildings or land, but is responsible for maintenance and repair of all buildings and land improvements. The land and building shell for the Bureau's Western Currency Facility were donated by the City of Fort Worth, Texas to the Department of the Treasury (See Note 5).

Depreciation of property and equipment is calculated using the straight-line method over the following estimated useful lives:

Machinery and equipment	3 - 15 years
Building improvements	3 - 40 years
Information technology (IT) equipment and software	3 - 5 years
Office machines	5 - 10 years
Furniture and fixtures	5 - 10 years
Motor vehicles	3 - 9 years

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Notes to the Financial Statements

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*Other Assets*

Other assets consist principally of machine repair parts and tools, which are used in the production of the Bureau's products. Other assets are stated at standard cost, which approximates actual cost, net of a reserve for obsolescence.

*Employee Retirement Plans*

Bureau employees participate in the contributory Civil Service Retirement System (CSRS) or Federal Employees' Retirement System (FERS), to which the Bureau and employees make contributions according to plan requirements. Consistent with reporting under multi-employer pension plans, the Bureau does not report CSRS and FERS assets, accumulated plan benefits or future liabilities, if any, applicable to its employees. This data is reported for plan participants by the Office of Personnel Management (OPM).

*Postretirement Benefits Other than Pensions*

Postretirement benefits for former Bureau employees, specifically health care costs and life insurance, are administered and paid by OPM through appropriations received from the U.S. Government. The Bureau does not reimburse OPM for these payments. The Bureau's financial statements do not include the cost of employee postretirement benefits paid by OPM, or the actuarial liability for such benefits.

*Workers' Compensation Costs*

The Federal Employee Compensation Act (FECA) provides income and medical cost protection to covered federal civilian employees injured on the job, employees who have incurred a work-related occupational disease and beneficiaries of employees whose death is attributable to a job-related injury or occupational disease. Claims incurred for benefits for the Bureau's employees under FECA are administered by DOL and are ultimately paid by the Bureau.

The FECA liability consists of two components. The first component, the accrued FECA liability, is based on actual claims paid by DOL but not reimbursed by the Bureau. The Bureau reimburses DOL for the amount of actual claims normally within one to two years after payment is made by DOL. As a result, the Bureau recognizes a current and non-current liability for actual claims paid by DOL, to be reimbursed by the Bureau.

The second component, the actuarial FECA liability, is the estimated liability for future benefit payments. These future workers' compensation estimates were generated from an application of actuarial procedures developed to estimate the liability for future FECA benefits. The actuarial liability for future worker's compensation benefits includes the expected liability for death, disability, medical and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. These annual benefit payments have been discounted to present value using the Office of Management and Budget's (OMB) economic assumptions for 10-year Treasury notes and bonds, which resulted in discount rates as of September 30, 2011 and 2010,

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Notes to the Financial Statements

September 30, 2011 and 2010

of 3.54% and 3.65% in year one and 4.03% and 4.30% thereafter. The Department of the Treasury allocated the overall liability to Treasury components based on past claims paid information provided by DOL. The use of these rates approximates the use of average historical rates on marketable Treasury securities with maturities consistent with the projected benefit payments.

*Annual, Sick, and Other Leave*

Annual leave is accrued as a liability when earned and the accrual is reduced as leave is taken. The balance in this accrued liability account reflects current pay rates.

Sick leave and other types of non-vested leave are expensed as the leave is taken.

*Revenue Recognition*

Revenue from sales to the Federal Reserve Board is recognized when finished goods satisfactorily pass all Bureau quality control standards and are delivered to the on-site Federal Reserve Depository vaults. Finished goods are released for shipment in accordance with customer requirements. Revenue from the sale of uncut currency to the public is recognized at the time the product is shipped. The Bureau does not record an allowance for returns because of a historically negligible return rate.

*Research and Development Costs and Public Education (Advertising) Costs*

Research and development costs and public education costs are expensed as incurred. Public education costs, which are reported in cost of goods sold, amounted to \$3.1 million and \$15.9 million in the years ended September 30, 2011 and 2010, respectively.

*Tax Status*

The Bureau is a federal entity, and therefore is not subject to federal, state, or local income taxes. Accordingly, no provision for income taxes is made in the accompanying financial statements.

*Contingencies*

Liabilities from loss contingencies arising from claims, assessments, litigation, fines and penalties, and other sources, are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation cost can be reasonably estimated. Loss contingencies that do not meet these criteria, but are reasonably possible and estimable are not accrued, but are disclosed in Note 12.

*Fair Value Measurements*

ASC 820-10, *Fair Value Measurements and Disclosures*, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The Bureau's financial instruments are comprised of cash, accounts receivable, accounts payable, accrued liabilities, and advances as of September 30, 2011 and 2010, respectively. The carrying amounts of these

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Notes to the Financial Statements

September 30, 2011 and 2010

financial instruments approximate fair value because of the short-term nature of these instruments. The Bureau holds no financial instruments that are required by ASC 825-10 to be valued at, reported, or disclosed at fair value as of September 30, 2011 or 2010.

**3. Cash**

The year-end cash balances by fund are as follows as of September 30, 2011 and 2010:

	(In Thousands)	
	<u>2011</u>	<u>2010</u>
Bureau of Engraving and Printing		
Revolving Fund	\$ 126,264	\$ 146,885
Mutilated Currency Revolving Fund	<u>3,914</u>	<u>6,777</u>
Total	<u>\$ 130,178</u>	<u>\$ 153,662</u>

The balance in the mutilated currency revolving fund, consisting of processed claims for mutilated currency submitted by the public for redemption, is offset by a liability to the public which is included in advances on the balance sheets as of September 30, 2011 and 2010, respectively (See Note 7).

**4. Inventories, net**

Inventories consist of the following as of September 30, 2011 and 2010:

	(In Thousands)	
	<u>2011</u>	<u>2010</u>
Raw material and supplies	\$ 46,429	\$ 54,344
Work-in-process	40,203	45,489
Finished goods - currency	48,270	26,154
Finished goods - uncut currency	<u>13,924</u>	<u>14,242</u>
Total	<u>\$ 148,826</u>	<u>\$ 140,229</u>

The allowance for inventory obsolescence was \$952 thousand and \$820 thousand, at September 30, 2011 and 2010, respectively.

In 2010, the Bureau adjusted (wrote down) the value of its currency paper and work-in-process inventories relating to the redesigned \$100 notes due to a problem with intermittent creasing that is occurring during intaglio printing that is resulting in abnormally high spoilage. The services of an appraiser were not used. This adjustment resulted in the recognition of a loss of \$840 thousand in 2010. This adjustment is included in the cost of goods sold on the Statement of Operations.

**THE DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING**

Notes to the Financial Statements

September 30, 2011 and 2010

**5. Property and Equipment, net**

Property and equipment consist of the following as of September 30, 2011 and 2010:

	(In Thousands)	
	<u>2011</u>	<u>2010</u>
Machinery and equipment	\$ 477,455	\$ 471,129
Building and land improvements	234,314	234,284
IT equipment and software	56,821	46,456
Office machines	2,791	2,752
Furniture and fixtures	1,272	1,222
Donated assets - art work	125	125
Motor vehicles	212	212
	<u>772,990</u>	<u>756,180</u>
Less accumulated depreciation	<u>512,831</u>	<u>481,858</u>
	260,159	274,322
Construction-in-progress	121,348	72,036
Net property and equipment	<u>\$ 381,507</u>	<u>\$ 346,358</u>

Depreciation expense for the years ended September 30, 2011 and 2010 was \$32.6 million and \$27.8 million, respectively.

The Bureau occupies and uses buildings and land owned by the Department of the Treasury. The land and building shell for the Fort Worth, Texas facility were donated by the City of Fort Worth to the Department of the Treasury in 1987, which holds the title thereto. At the time of donation, the land had an appraised value of \$1.5 million and the building shell cost was \$5.6 million. In accordance with the provisions of Public Law 81-656, Bureau financial statements include only the costs to build out the facility.

**6. Other Assets, net**

Other assets consist principally of machine repair parts and tools. The allowance for obsolescence for these parts and tools for the years ended September 30, 2011 and 2010 was \$5.9 million and \$5.4 million, respectively.

**THE DEPARTMENT OF THE TREASURY  
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Notes to the Financial Statements

September 30, 2011 and 2010

**7. Current Liabilities**

All current liabilities are funded and consist of the following as of September 30, 2011 and 2010:

	(In Thousands)	
	<u>2011</u>	<u>2010</u>
Intragovernmental	\$ 10,084	\$ 9,731
With the public	68,008	55,147
Total	<u>\$ 78,092</u>	<u>\$ 64,878</u>

Accrued current liabilities consist of the following as of September 30, 2011 and 2010:

	(In Thousands)	
	<u>2011</u>	<u>2010</u>
Payroll	\$ 17,591	\$ 15,619
Annual leave	11,591	11,676
Workers' compensation	5,270	5,146
Other	1,497	1,072
Total	<u>\$ 35,949</u>	<u>\$ 33,513</u>

Advances consist of the following as of September 30, 2011 and 2010:

	(In Thousands)	
	<u>2011</u>	<u>2010</u>
Other Federal Agencies	\$ 4,513	\$ 4,537
Mutilated Currency	3,914	6,777
Public sales	33	6
Total	<u>\$ 8,460</u>	<u>\$ 11,321</u>

**8. Workers' Compensation Liability**

Claims incurred and paid by DOL as of September 30, 2011 and 2010, but not yet reimbursed to DOL by the Bureau, are approximately \$12.3 million and \$12.1 million, of which approximately \$5.3 million and \$5.1 million represent a current liability, as of September 30, 2011 and 2010, respectively. The Bureau will reimburse DOL for these claims in the next two years. The Bureau's estimated non-current, actuarially derived future workers' compensation liability was approximately \$55.4 million and \$51.8 million as of September 30, 2011 and 2010, respectively. The Bureau's estimated, undiscounted, non-current, actuarially derived future workers' compensation liability was approximately \$87.5 million and \$84.1 million as of September 30, 2011 and 2010, respectively.



**THE DEPARTMENT OF THE TREASURY  
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Notes to the Financial Statements

September 30, 2011 and 2010

**9. Employee Retirement Plans and Postretirement Benefits Other than Pensions**

Employer contributions to the retirement plans were \$17.9 million and \$17.0 million for 2011 and 2010, respectively. The CSRS employer contribution rate for fiscal years 2011 and 2010 was 7.0%. The FERS agency contribution rate was 11.7% and 11.2% for fiscal years 2011 and 2010, respectively. The cost of providing the CSRS and FERS benefits is more than the amounts contributed by the Bureau and the employees to OPM. The additional cost of providing benefits, including the cost financed by OPM, which is not included in the Bureau's Statements of Operations, totaled \$26.5 million and \$26.7 million in 2011 and 2010, respectively.

OPM paid costs totaling \$11.2 million and \$11.1 million for the Federal Employees Health Benefits Program (FEHBP) and Federal Employees Group Life Insurance (FEGLI) programs in 2011 and 2010, respectively. These costs are not included in the Bureau's Statements of Operations. The Bureau paid costs totaling \$14.1 million and \$13.0 million for the FEHBP and FEGLI programs in 2011 and 2010, respectively.

**10. Related Party Transactions and Concentration of Revenue**

The Bureau's principal customers are other federal and quasi-federal governmental organizations. During 2011 and 2010, the Bureau's sales revenue from these organizations as well as the outstanding amounts due from them as of September 30, 2011 and 2010, are reflected in the following table:

	<b>Revenue</b>		<b>Accounts Receivable</b>	
	(In Thousands)		(In Thousands)	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
Federal Reserve Board:				
Currency Production	\$ 523,009	\$ 614,860	\$ 36,993	\$ 27,220
Mutilated Currency	3,472	3,547	873	869
Other Federal Agencies	<u>3,291</u>	<u>3,752</u>	<u>126</u>	<u>106</u>
	<u>529,772</u>	<u>622,159</u>	<u>37,992</u>	<u>28,195</u>
Public sales	18,320	8,555	56	6
Other	<u>2</u>	<u>708</u>	<u>388</u>	<u>421</u>
	<u>18,322</u>	<u>9,263</u>	<u>444</u>	<u>427</u>
Total	<u>\$ 548,094</u>	<u>\$ 631,422</u>	<u>\$ 38,436</u>	<u>\$ 28,622</u>

Revenues from other federal agencies are derived principally from the sale of security printing products to U.S. Government agencies and related fees charged.

Substantially all products are sold on a fixed price basis. When the revenue from such pricing is not sufficient to cover all costs and provide for necessary working capital the Bureau will negotiate with the Federal Reserve Board for an additional surcharge. The required surcharge

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Notes to the Financial Statements

September 30, 2011 and 2010

totaled approximately \$97.8 million and \$211.9 million in 2011 and 2010, respectively. This amount is included in Revenue on the Statement of Operations.

**11. Principal Suppliers**

The Bureau is dependent upon sole suppliers for distinctive currency paper and several advanced counterfeit deterrent materials.

**12. Commitments and Contingencies**

The Bureau is a party in various administrative proceedings, legal actions, and claims brought against the Federal Government by employees, contractors, and other parties. As of September 30, 2011 and 2010, there are no contingencies for litigation involving the Bureau, where the risk of loss is probable. Contingencies, where the risk of loss is reasonably possible, are approximately \$4.0 million and \$2.9 million as of September 30, 2011 and 2010, respectively. Since the risk of loss for these litigations is not probable, the Bureau did not record any liability. Management believes that the ultimate resolution of these litigations will not have a material impact on the reported financial position, results of operations, and cash flows.

In 2007, a judge ruled that the current U.S. currency design violates Section 504 of the Rehabilitation Act. The Court awarded no monetary damages. However, the Bureau is required to provide meaningful access to United States currency for blind and other visually impaired persons as part of the next currency redesign. The cost of currency changes necessary to provide meaningful access will be incorporated into future currency redesign costs. No costs have been accrued in the accompanying financial statements as of September 30, 2011 and 2010.

The Bureau has contracted to purchase three large finishing presses, incorporating automated inspection and packaging capability, costing approximately \$53.0 million. As of September 30, 2011, the Bureau has made cumulative payments of \$30.8 million and the remaining commitment outstanding is \$22.2 million. Delivery of the presses will be determined upon successful completion of final factory inspection tests. Progress payments related to the above contract is included in construction-in-progress within Property and Equipment on the balance sheets as of September 30, 2011 and 2010, respectively.

The Bureau does not carry commercial insurance on its physical assets because by law the Federal Government is self-insured.

**13. Operating Lease**

In 2002, the Bureau entered into a cancelable operating lease for warehouse space that expires in 2012. The operating lease for warehouse space was renewed in 2011 for an additional 10 years and will expire in 2022.

Rental expense for the years ended September 30, 2011 and 2010 was \$1.9 million and \$1.8 million, respectively.

**THE DEPARTMENT OF THE TREASURY  
BUREAU OF ENGRAVING AND PRINTING**

Notes to the Financial Statements

September 30, 2011 and 2010

Future minimum payments under the lease as of September 30, 2011, are (in thousands):

For the years ending September 30:	
2012	\$ 2,451
2013	3,039
2014	3,051
2015	3,064
2016	3,077
Thereafter	<u>17,157</u>
Total	<u><u>\$ 31,839</u></u>

**14. Subsequent Events**

The Bureau has evaluated subsequent events through December 14, 2011, the date which the financial statements were available to be issued. There were no material events that required additional accruals or disclosures.



**DEPARTMENT OF THE TREASURY**  
**BUREAU OF ENGRAVING AND PRINTING**  
**WASHINGTON, D.C. 20228**

Management's Report on Internal Control Over Financial Reporting

We as management of the Bureau of Engraving and Printing (Bureau) are responsible for establishing and maintaining adequate internal control over financial reporting and for our assertion on the effectiveness of internal control over financial reporting. The Bureau's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

The Bureau's internal control over financial reporting includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect our transactions and dispositions of the assets of the Bureau;
- provide reasonable assurance that our transactions are recorded as necessary to permit preparation of our financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures of the Bureau are being made in accordance with authorizations of management of the Bureau and those charged with governance; and
- provide reasonable assurance regarding prevention, or timely detection and correction of unauthorized acquisition, use, or disposition of the Bureau's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that internal controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

We assessed the effectiveness of the Bureau's internal control over financial reporting as of September 30, 2011. In making this assessment, the Bureau used the criteria established in the *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Based on our assessment and those criteria, we conclude that the Bureau maintained effective internal control over financial reporting as of September 30, 2011.

KPMG LLP, an independent public accounting firm, has issued their reports, included herein, on (1) our financial statements; (2) our compliance with certain provisions of laws, regulations, and contracts and other matters; and (3) our assertion on the effectiveness of internal control over financial reporting.

Larry R. Felix  
Director

Leonard R. Olijar  
Chief Financial Officer

December 14, 2011



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

## **Independent Auditors' Report on Internal Control Over Financial Reporting**

To the Inspector General, Department of the Treasury, and  
The Director of the Bureau of Engraving and Printing, Department of the Treasury:

We have examined management's assertion, included in the accompanying "Management's Report on Internal Control Over Financial Reporting," that the Bureau of Engraving and Printing (Bureau) maintained effective internal control over financial reporting as of September 30, 2011, based on the criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Bureau's management is responsible for maintaining effective internal control over financial reporting, and for its assertion on the effectiveness of internal control over financial reporting, included in the accompanying "Management's Report on Internal Control Over Financial Reporting." Our responsibility is to express an opinion on management's assertion based on our examination.

We conducted our examination in accordance with attestation standards established by the American Institute of Certified Public Accountants, and the standards applicable to attestation engagements contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the examination to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our examination included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our examination also included performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, designed to provide reasonable assurance regarding the preparation of reliable financial statements in accordance with U.S. generally accepted accounting principles. An entity's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the entity; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures of the entity are being made only in accordance with authorizations of management and those charged with governance; and (3) provide reasonable assurance regarding prevention, or timely detection and correction of unauthorized acquisition, use, or disposition of the entity's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.



In our opinion, management's assertion that the Bureau of Engraving and Printing maintained effective internal control over financial reporting as of September 30, 2011 is fairly stated, in all material respects, based on the criteria established in *Internal Control – Integrated Framework* issued by COSO.

In accordance with *Government Auditing Standards*, we are required to report findings of significant deficiencies. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness in internal control over financial reporting, yet important enough to merit attention by those charged with governance. We consider the deficiency in the Bureau's internal control described in Exhibit I of this report to be a significant deficiency. The Bureau's response to the finding identified in our examination is included in Exhibit I. We did not examine the Bureau's response and, accordingly, we express no opinion on the response.

We also have audited, in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended, the balance sheets of the Bureau as of September 30, 2011 and 2010, and the related statements of operations and cumulative results of operations, and cash flows, of the Bureau and our report dated December 14, 2011 expressed an unqualified opinion.

We noted certain additional matters that we have reported to management of the Bureau in a separate letter dated December 14, 2011.

KPMG LLP

December 14, 2011

**Fiscal Year 2011 Significant Deficiency**

***Internal Control Over Year End Liability Accruals Needs Improvement***

During our test work over the Bureau of Engraving and Printing's (the Bureau) year end liability accruals, we noted the following two instances where the Bureau's supervisory review controls did not detect overstatements in its liability accruals.

During fiscal year 2011, the Federal Reserve Bank (Federal Reserve) discontinued having the Bureau provide public education services on its behalf. Pursuant to this agreement, the Bureau was to provide the Federal Reserve with a final accounting associated with providing such services as of the fiscal year end. The Bureau completed its internal analysis which resulted in its recording an amount due to the Federal Reserve of approximately \$10.7 million as of September 30, 2011. During our audit, we noted that the Bureau inadvertently excluded approximately \$5.5 million in program expenses from its analysis, resulting in an overstatement of accounts payable and an understatement of revenues of approximately \$5.5 million in its draft financial statements as of and for the year ended September 30, 2011.

At the end of each fiscal year the Bureau's Office of Financial Management inquires of other Bureau divisions regarding un-invoiced goods or services received for which the Bureau should accrue a liability. The Bureau incurs a liability once the terms of the contract between the Bureau and its supplier have been met. During our audit, we noted that the specific terms of two contracts had not been met as of September 30, 2011, resulting in an overstatement of accounts payable and property, plant and equipment by \$1.4 million as of September 30, 2011.

OMB Circular A-123 states, "Management is responsible for developing and maintaining effective internal control. Effective internal control provides assurance that significant weaknesses in the design or operation of internal control, that could adversely affect the agency's ability to meet its objectives, would be prevented or detected in a timely manner."

In both conditions noted, the initial analysis to determine the payable amount was incorrectly performed, and the review of the analysis was not sufficient to identify the error. The total error was subsequently corrected by the Bureau.

We recommend the Bureau (1) develop and implement policies and procedures to improve the reliability of reviews over significant and unusual accounting transactions and reconciliations by individuals most knowledgeable of the subject matter, (2) ensure policies and procedures are followed to verify all significant and unusual accounting transactions and reconciliations were performed properly, (3) require supporting documentation be provided with, and be examined as part of, the Bureau's review of year end specific item accounts payable estimates, and (4) ensure all year end specific item accounts payable estimates are adequately supported and properly accrued.

**Management Response:**

Management concurs with the recommendation; and will take the necessary steps to implement policies and procedures requiring additional reviews of significant and unusual accounting transactions and reconciliations by individuals most knowledgeable of the subject matter.

Additionally, management's current process for obtaining and documenting support for year-end accounts payable estimates will be evaluated and appropriate steps will be taken to ensure the reasonableness of management estimates and assumptions.



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## Independent Auditors' Report on Compliance and Other Matters

The Inspector General, Department of the Treasury and  
The Director of the Bureau of Engraving and Printing, Department of the Treasury:

We have audited the balance sheets of the Bureau of Engraving and Printing (Bureau) as of September 30, 2011 and 2010, and the related statements of operations and cumulative results of operations and cash flows (hereinafter referred to as "financial statements") for the years then ended, and have issued our report thereon dated December 14, 2011.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended. Those standards and OMB Bulletin No. 07-04 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of the Bureau is responsible for complying with laws, regulations, and contracts applicable to the Bureau. As part of obtaining reasonable assurance about whether the Bureau's financial statements are free of material misstatement, we performed tests of the Bureau's compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of the financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 07-04. 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 Bureau. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests of compliance described in the preceding paragraph, disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 07-04.

This report is intended solely for the information and use of the Bureau's management, the Department of the Treasury's Office of Inspector General, OMB, 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**

December 14, 2011