



Audit Report



OIG-14-038

Management Letter for the Audit of the Office of D.C. Pensions' Fiscal Years 2013 and 2012 Financial Statements

June 2, 2014

Office of
Inspector General

Department of the Treasury



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

June 2, 2014

**MEMORANDUM FOR NANCY OSTROWSKI, DIRECTOR
OFFICE OF D.C. PENSIONS**

FROM: Michael Fitzgerald
Director, Financial Audit

SUBJECT: Management Letter for the Audit of the
Office of D.C. Pensions' Fiscal Years 2013 and 2012
Financial Statements

I am pleased to transmit the attached management letter in connection with the audit of the Office of D.C. Pensions' (ODCP) Fiscal Years 2013 and 2012 financial statements. Under a contract monitored by the Office of Inspector General, KPMG LLP (KPMG), an independent certified public accounting firm, performed an audit of ODOP's financial statements as of September 30, 2013 and 2012, and for the years then ended. The contract required that the audit be performed in accordance with generally accepted government auditing standards and applicable provisions of Office of Management and Budget Bulletin No.14-02, *Audit Requirements for Federal Financial Statements*.

As part of its audit, KPMG issued and is responsible for the accompanying management letter that discusses matters involving internal control over financial reporting 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's letter and related documentation and inquired of its representatives. Our review disclosed no instances where KPMG 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 Audit, at (202) 927-5407.

Attachment



KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

May 28, 2014

Inspector General, U.S. Department of the Treasury, and
Director, Office of D.C. Pensions:

In planning and performing our audit of the consolidated financial statements of the U.S. Department of the Treasury's Office of D.C. Pensions (the ODCP), as of and for the year ended September 30, 2013, 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. 14-02, *Audit Requirements for Federal Financial Statements*, we considered the ODCP'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 consolidated financial statements but not for the purpose of expressing an opinion on the effectiveness of the ODCP's internal control. Accordingly, we do not express an opinion on the effectiveness of the ODCP's internal control.

During our audit, we noted certain matters involving internal control and other operational matters that are presented for your consideration. These findings 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 to this report.

In addition, we identified certain deficiencies in internal control over financial reporting that we consider to be a material weakness and a significant deficiency, and communicated them in writing as Exhibits I and II, respectively, to the Independent Auditors' Report on Internal Control Over Financial Reporting to management and those charged with governance on May 28, 2014.

Our audit procedures are designed primarily to enable us to form an opinion on the consolidated 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 ODCP's organization gained during our work to make comments and suggestions that we hope will be useful to you. The ODCP's responses to our findings and recommendations are included in Appendix A. We did not audit the ODCP's responses and, accordingly, we express no opinion on them.

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 ODCP's management, the U.S. 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.

Very truly yours,

KPMG LLP

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Review of Interim Financial Statements

During our audit, we reviewed the ODCP March 31, 2013 financial statements, and noted that Fund Balance with Treasury, Recoveries of Prior Year Unpaid Obligations, and Obligations Incurred reflected an unusually high increase over March 31, 2012 as follows:

Financial Statement	3/31/2013	3/31/2012	Change
<u>Balance Sheet</u>			
Fund Balance with Treasury	\$ 8,563,000	\$ 503,000	\$ 8,063,000
<u>Statement of Budgetary Resources (SBR)</u>			
Recoveries of Prior Year Unpaid Obligations	\$ 65,278,000	\$ 3,481,000	\$ 61,797,000
Obligations Incurred	\$ 347,631,000	\$ 291,864,000	\$ 55,676,000

Based on discussions with ODCP and the Administrative Resource Center (ARC) accounting personnel, as well as our review of related supporting documentation, we noted that:

- \$8 million was collected from the District of Columbia Retirement Board on December 31, 2012, and was not invested until after our inquiry in May 2013. Hence, this amount remained in Fund Balance with Treasury for over 4 months.
- When the September 30, 2012 benefits payable accrual for \$53.5 million was reversed in October 2012, two lines on the Statement of Budgetary Resources (*Recovery of Prior Year Unpaid Obligations* and *Obligations Incurred*) were overstated. This error was not corrected until our inquiry in May 2013.

The cash receipt occurred on December 31, 2012, after the process to reconcile daily cash receipts to daily amount invested had been completed at ARC.

ODCP's and ARC's review of the interim financial statements was not performed at a sufficient level of detail to determine whether the balances reported in the monthly financial statements were reasonable. Further, ODCP does not review journal entries with posting logic which automatically generates reversing entries to ensure they are recorded appropriately, or if necessary, reversed timely in the general ledger.

The U.S. Government Accountability Office's (GAO) *standards for internal controls in the Federal Government* state the following: "Transactions should be promptly recorded to maintain their relevance and value to management in controlling operations and making decisions. This applies to the entire process or life cycle of a transaction or event from the initiation and authorization through its final classification in summary records. In addition, control activities help to ensure that all transactions are completely and accurately recorded. Control activities occur at all levels and functions of the entity. They include a wide range of diverse activities

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such as approvals, authorizations, verifications, reconciliations, performance reviews, maintenance of security, and the creation and maintenance of related records.”

Office of Management and Budget’s Circular A-123, *Management’s Responsibility for Internal Control*, prescribes the expectation of management and the responsibility of managers for the quality and timeliness of program performance. Management controls are the organization, policies, and procedures used to reasonably ensure that....(v) reliable and timely information is obtained, maintained, reported and used for decision making.

In addition, OMB Circular A-123 states that “transactions should be promptly recorded, properly classified and accounted for, in order to prepare timely accounts and reliable financial and other reports.”

Also, ODCP Fiscal Year 2013 Investment Guidance Memorandum dated September 13, 2012 states “We invest cash balances in one-day certificates, except for a small balance on the last day of each month to cover unanticipated late in the day withdrawals” and “invest the remaining receipts in one-day certificates, except for amounts necessary to pay disbursements”.

Recommendations

We recommend that ODCP Management:

1. Establish and implement a process for reviewing the quarterly financial statements in more detail. The review should include comparison to previous period financial statements, and obtaining explanations and support for any unusual variances while taking into consideration current period activity; and
2. Work closely with ARC to:
 - Review ODCP-specific transactions and journal entries with posting logic which automatically generates reversing entries. Specifically, the system-generated reversing entries involved with the Prior Year Activity (PYA) transactions should be thoroughly reviewed.
 - Reconcile all cash receipts to the investment records monthly.

Management’s Response

ODCP will:

- 1) Establish and implement a process to review quarterly financial statements.
- 2) Review ODCP-specific transactions and journal entries with posting logic automatically generating reversing entries.
- 3) Establish and implement a monthly process to review investment records.

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Office of Management and Budget (OMB) Circular No. A-123, *Management's Responsibility for Internal Control Implementation*

During our review of ODCP's internal control review that was performed in compliance with Office of Management and Budget (OMB) Circular No. A-123, *Management's Responsibility for Internal Control* (A-123), we noted the following:

- Internal control testing relating to the review of the Actuarial Pension Liability journal entry was conducted by an ODCP employee who is also responsible for executing the control; and
- For the reconciliation control related to recording maturities of investment transactions, the ODCP testing binder did not include the reconciliation or documentation evidencing testing was performed for the month that was selected.

ODCP did not perform testing in accordance with the Guidance and Implementation Plan received from Treasury. Specifically, ODCP did not assign an alternate individual to complete the testing over the Actuarial Valuation journal entry.

Internal Control Evaluation Checklist GAO Internal Control Management and Evaluation Tool guidelines requires citation of the appropriate manuals, memos, other guidance or reviews that support the written responses. Source documentation does not need to be submitted to Treasury with the final A-123 report. However, documentation must be readily available in the event of an onsite audit by either external or internal auditors.

Per the Department of Treasury *Fiscal Year 2013 Guidance and Implementation Plan OMB Circular A-123, Management's Responsibility for Internal Control, Appendix A, Internal Control over Financial Reporting*:

Section 2 "The methodology supporting the assessment of internal controls over financial reporting is centered upon the documentation, testing, and assessment of internal controls at the transaction level that are applied on a day-to-day basis. The methodology further includes factors surrounding the operational environment of internal controls including the financial reporting compilation and preparation process, an assessment of the control environment, compliance with governing laws and regulations, and information and actions derived from audit report findings and recommendations.

Each bureau or office is responsible for maintaining documentation of their OMB Circular A-123 tested transactions. Bureaus and offices must maintain their documentation at a level that is able to withstand management and auditor scrutiny.

Section 3H "Bureaus and offices should ensure that controls are tested by individuals other than those routinely executing them."

If ODCP's testing is not performed in accordance with the requirements received from Treasury and in accordance with OMB A-123, ODCP may not be able to identify material weaknesses that should be reported in its annual Statement of Assurance. Further, failure to meet FMFIA requirements may result in ODCP not having effective internal controls in place to ensure that:

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(1) obligations and costs comply with applicable law; (2) assets are safeguarded against waste, loss, unauthorized use or misappropriation; and (3) revenues and expenditures are properly recorded and accounted for.

Recommendations

We recommend that:

- 1 ODCP comply with Treasury's Implementation Guidance for executing OMB A-123 Appendix A.
- 2 The Senior Assessment Team should dedicate appropriate resources to the FMFIA process and assign alternative individuals to perform testing, to ensure that controls are tested by individuals other than those routinely executing them.

Management's Response

ODCP will ensure the individuals testing controls are not also routinely executing those controls to comply with Treasury's Implementation Guidance for OMB A-123 Appendix A.

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Status of Fund Balance with Treasury Disclosure

During our review of the ODCP September 30, 2013 financial statements and related notes, we noted that in the “Status of Fund Balance with Treasury” section of note 2, Fund Balance with Treasury, ODCP erroneously reflected the entire Fund Balance with Treasury financial statement line item as Unobligated Balance – Available, when it should have been reflected as Obligated Balance Not Yet Disbursed (as reported in the Statement of Budgetary Resources) offset by an adjustment for non-budgetary items.

Office of Management and Budget’s Circular A-123, *Management’s Responsibility for Internal Controls*, states that “transactions should be properly classified and accounted for, in order to prepare timely accounts and reliable financial and other reports.”

Statement of Federal Financial Accounting Standards (SFFAS) 1, *Accounting for Selected Assets and Liabilities* – paragraph 1.37, “Disclosure should be made to distinguish two categories of funds within the entity’s fund balance with Treasury: the obligated balance not yet disbursed and the unobligated balance. The obligated balance not yet disbursed is the amount of funds against which budgetary obligations have been incurred, but disbursements have not been made.”

Office of Management and Budget Circular A-136 (OMB Circular A-136), *Financial Reporting Requirements* provides further guidance as to the form and content of this note:

“Segregate the status of fund balance with Treasury as follows: (OC II.4.9.3)

- (1) Unobligated balance.
 - (a) Available
 - (b) Unavailable
- (2) Obligated balance not yet disbursed
- (3) Non-budgetary fund balance with Treasury (e.g. balances in unavailable receipt accounts, clearing accounts, and so forth that do not have budget authority and non-entity fund balance with Treasury recognized on the balance sheet).”

ODCP’s and ARCs review of the financial statements was not performed at a sufficient level of detail to determine whether the balances reported in the FBWT note was presented in accordance with SFFAS 1 and OMB Circular A-136.

Recommendation:

We recommend that the ODCP management reassess the current process for ensuring the completeness and accuracy of note disclosures and implement changes to strengthen the internal controls.

Management’s Response

ODCP will reassess the current process for ensuring the completeness and accuracy of note disclosures.