OFFICE OF INSPECTOR GENERAL

Audit Report

Fiscal Year 2008 Financial Statement Audit Letter to Management

Report No. 09-02
March 24, 2009

RAILROAD RETIREMENT BOARD

UNITED STATES RAILROAD RETIREMENT BOARD

OFFICE OF INSPECTOR GENERAL

March 24, 2009

Michael S. Schwartz
Chairman
U.S. Railroad Retirement Board

The purpose of this letter is to transmit a memorandum on internal control communicating certain matters concerning internal control that came to our attention during our recent audit of the Railroad Retirement Board's (RRB) financial statements.

We have audited the RRB's general purpose financial statements and issued our report thereon dated November 6, 2008, except for matters relating to the fair market value of the net assets of the National Railroad Retirement Investment Trust as of September 30, 2008, as to which the date was November 17, 2008. We performed our audit in accordance with U.S. generally accepted government auditing standards and OMB audit guidance as applicable to the scope of our audit.[1] We have not considered internal control since we obtained sufficient appropriate audit evidence to support the audit opinion on November 6, 2008; internal control was not among those matters to which we gave consideration between November 6th and November 17th.

During our audit, we noted certain matters involving the RRB's internal control structure and its operation that, individually, did not rise to the level of a significant deficiency, the details of which are presented in the attached memorandum. That memorandum also presents the full text of those matters previously reported as material weaknesses and significant deficiency in conjunction with our opinion on the financial statements. However, neither this letter, nor the attached memorandum, modifies our report dual dated as of November 6, 2008 and November 17, 2008, referred to above.

Our observations concerning internal control were presented to responsible agency management who were offered the opportunity to review and comment on the draft memorandum. Their responses are also attached.

[1] See our report on the RRB's financial statements for a full description of the scope and methodology.

844 N RUSH STREET CHICAGO IL 60611-2092

In planning and performing this audit, we considered internal control in order to determine our auditing procedures for the purpose of issuing our report on the RRB's principal financial statements and not to provide assurance on internal control. The maintenance of adequate internal control designed to fulfill the RRB's control objectives is the responsibility of management. Because of inherent limitations in any system of internal control, errors or irregularities may nevertheless occur and not be detected. Also, controls found to be functioning at a point in time may later be found deficient because of the performance of those responsible for applying them. There can be no assurance that controls currently in existence will prove to be adequate in the future as changes take place in the organization.

Our work was not conducted for the primary purpose of making detailed recommendations about the RRB's system of internal control. Had we done so, other matters might have come to our attention that we would have reported to you.

We wish to express our appreciation for the many courtesies and cooperation extended to us during the audit.

Very truly yours,

Original Signed by …

Martin J. Dickman
Inspector General

Attachments

cc: V.M. Speakman, Jr., Labor Member
Jerome F. Kever, Management Member
Kenneth P. Boehne, Chief Financial Officer
Dorothy Isherwood, Director of Programs
Steven A. Bartholow, General Counsel
Frank J. Buzzi, Chief Actuary
Beatrice E. Ezerski, Secretary to the Board

Memorandum on Internal Control
Table of Contents

Memorandum on Internal Control
Table of Contents

Memorandum on Internal Control

MATERIAL WEAKNESSES AND SIGNIFICANT DEFICIENCY

In conjunction with our opinion on the RRB's financial statements for the fiscal years ended September 30, 2008 and 2007, we reported the following material weaknesses and significant deficiency.

Material Weaknesses

Information Security

During fiscal year (FY) 2008, the Office of Inspector General (OIG) evaluated information security pursuant to the provisions of the Federal Information Security Management Act.[2] Our review disclosed continued weaknesses in many areas of the RRB's information security program. Significant deficiencies in program management and access controls make the agency's information security program a source of material weakness in internal control.

RRB efforts to strengthen information security continue and progress is being made; however, previously identified significant deficiencies in access controls, risk assessments, and periodic testing and evaluation continue to exist. In addition, the agency's information security program is not yet fully compliant with current requirements for risk based policies and procedures, a certification and accreditation program, or a comprehensive remedial action process.

Agency management is working to address the weaknesses in its information security program. Although some progress has been made, much work remains to be completed.

Financial Reporting

We first reported this control deficiency in the report on internal control issued with our opinion on the RRB's FY 2006 audit of the RRB's financial statements. Management action has not fully addressed the underlying cause and the condition has deteriorated. Although we observed notable efforts to strengthen internal control over financial accounting during FY 2007, we find that the RRB has been unable to sustain that improvement during FY 2008. In addition, a quality assurance process implemented during FY 2007 has not proven to be fully effective.

An effective control structure allows management and/or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis.

---

[2] "Fiscal Year 2008 Evaluation of Information Security at the Railroad Retirement Board," OIG Report #08-05, September 30, 2008

Memorandum on Internal Control

The Bureau of Fiscal Operations (BFO) is responsible for preparing agency financial statements and publishing the RRB's annual performance and accountability report. During our FY 2006 audit, we observed that existing procedures and controls over the financial reporting process needed to be updated to fully ensure the quality of the RRB's response to the expanding responsibilities and short timeframes inherent to the Federal financial reporting process. We also observed that the existing control framework was overly reliant on the OIG's annual audit of the financial statements to ensure the completeness and accuracy of the performance and accountability report.

During FY 2007, we found the agency reporting process much improved by the efforts of BFO management and staff. BFO responded to the OIG's prior year finding by implementing OIG-recommended corrective actions and by implementing an enhanced year-end financial statement review process of their own design.

During our FY 2008 audit, we identified material transactions that were recorded incorrectly which were not detected and corrected timely because the primary control, supervisory review and approval of transactions, is not operating as designed. As a result, financial accounting controls cannot be relied upon to ensure that material errors will be detected to prevent misstatements in financial reporting. In addition, controls over financial statement preparation are not fully effective.

Significant Deficiency

Reconciliation of Benefit Payment Subsystems with the General Ledger

Current accounting procedures do not provide for periodic reconciliation of the general ledger with the benefit payment systems in which those transactions originate. There is no compensating control that would provide similar assurance concerning the completeness of recording and reporting for benefit payment expense which exceeded $10 billion during FY 2008.

Significant accounts should be reconciled to the general ledger timely; the lack of such reconciliations represents a control deficiency. The detailed records concerning payments adjudicated and issued is stored in various automated systems that support the benefit payment process. Benefit payment activity is manually recorded in the general ledger from summary data originating in other systems.

This weakness was brought to management's attention in connection with earlier audits.[3] Upon detailed review, management did not implement the recommended

---

[3] "Review of Internal Control Over Financial Accounting for Debt Recoveries," OIG Audit Report #00-16, September 29, 2000, page 10.

"Letter to Management," OIG Audit Report #02-07, February 8, 2002, page 5.

reconciliation process citing the inability of existing benefit payment subsystems to support a cost-effective control and reconciliation process. Since that time, the OIG has identified a more cost-effective reconciliation process. RRB financial managers have been receptive to reconsidering the issue and have agreed to study the OIG's suggestion.

Recommendation

We recommend that BFO:

1. reconcile benefit payments as recorded in the general ledger to the benefit payment subsystem.

Management's Response

BFO has agreed to implement a reconciliation process. The full text of management's response is presented as Attachment 1 to this memorandum.

Memorandum on Internal Control

The individual matters that contributed to our overall finding of a material weakness in internal control over financial reporting are described in detail in the following section of this memorandum.

MATTERS INVOLVING INTERNAL CONTROL THAT, IN THE AGGREGATE, REPRESENT A MATERIAL WEAKNESS

During our FY 2008 audit, we identified material transactions that were recorded incorrectly. These errors were not detected and corrected timely because the primary control, supervisory review and approval of transactions, is not operating as designed. We also observed that many of the issues that created the significant deficiency in financial reporting cited in our FY 2006 and FY 2007 Letters to Management had not been corrected. As a result, financial accounting controls cannot be fully relied upon to ensure that material errors will be detected to prevent misstatement in financial reporting.

BFO advised us that during FY 2008, they had taken action to implement OIG recommendations to correct control deficiencies previously reported in the FY 2006 and FY 2007 Letters to Management. BFO provided training on voucher preparation, updated their accounting procedures guide to include detailed instructions and examples of accounting transactions, developed a checklist and review process to ensure the accuracy of financial statement preparation and developed a line of responsibility to ensure separation of duties. In addition, BFO refined their quality assurance process for vouchers.

Although BFO has worked to correct the control deficiencies in financial reporting we find that their actions have not fully addressed the underlying cause and the condition persists in the following areas:

- transaction documentation needs improvement,
- controls over report preparation are not fully effective, and
- additional controls are needed to ensure compliance with requirements.

During the current-year audit we identified the following additional control weaknesses that indicate the persistence of a material weakness in internal control over financial reporting:

- review and approval of vouchers needs improvement, and
- the quality assurance process for voucher preparation is not yet fully effective.

Previously Reported Weaknesses Persist

During the audit, we also observed that key control weaknesses previously reported had not been corrected. In general, the inability to correct, or sustain correction of a previously reported significant deficiency is an indicator of material weakness. In addition, our audit disclosed weaknesses in controls over compliance with applicable requirements for the form and content of financial statements that resulted in revisions to the statement of budgetary resources. The details of our findings follow.

Transaction Documentation Needs Improvement

We previously recommended that BFO:

> instruct staff on the proper documentation needed to support transactions prior to the preparation of a voucher, the need to evidence proper voucher preparation even when automated signatures are used, and the need for accurate and consistent documentation to support journal vouchers.[4]

In response to our recommendation, BFO conducted training for accounting staff and documented guidance for voucher preparation.

During the audit, we observed that the previously identified control deficiency in voucher documentation persists. We identified vouchers with insufficient documentation to support transactions recorded in the general ledger. Some of the exceptions include:

- nine vouchers supporting a total of $2.5 billion in cash advances from the U.S. Treasury did not include documentation confirming receipt prior to recording;
- two vouchers supporting investment of $538 million cash in U.S. Treasury securities did not include confirmation of the investment;
- two vouchers supporting investment of $570 million cash in U.S. Treasury securities did not include a copy of the memorandum authorizing the transaction;
- one voucher supporting a $4 million inter-fund transfer was not supported by a memorandum authorizing the transaction;
- an authorizing memorandum supporting recording of $136 million transferred-in from the National Railroad Retirement Investment Trust was undated;

[4] "Fiscal Year 2007 Financial Statement Audit Letter to Management," OIG Audit Report #08-01, March 6, 2008, Recommendation 11.

- two authorizing memoranda supporting redemption of $68 million in investments were dated after the date of redemption;
- four vouchers that support recording for over $956 million in transactions show a supervisory approval dated prior to the date that the voucher was signed by the preparing accountant;
- nine vouchers that support recording for $1.9 billion in transactions were entered into the general ledger based on document approvals applied by lower graded staff than required by applicable procedure;
- documentation supporting the need to transfer funds was missing evidence of the third approval for $20.7 million recorded on 11 vouchers, and three other vouchers totaling $11.4 million omitted that documentation entirely; and
- documentation for one voucher was incomplete with respect to $1.4 million because BFO did not return an incomplete funds breakdown form to the originating bureau.

In addition, we questioned charges of $15.3 million posted to the general ledger before BFO had verified that these costs had been properly charged to the RRB. We also questioned the reversal of an $843,000 accrual that was not adequately supported by the documentation attached to the voucher.

Because our prior recommendation for corrective action is pending; the OIG has no additional recommendations to offer at this time.

Controls Over Report Preparation Are Not Fully Effective

We previously recommended that BFO:

> determine the cause of the errors identified during our audit, whether existing controls were in operation [throughout the year], and whether additional controls may be required to ensure that the financial statements, notes, and supporting schedules are properly [prepared].[5]

In response to our recommendation, BFO created a checklist addressing financial statement preparation and selected notes. We evaluated the effectiveness of its implementation and found that the previously identified conditions persist.
During the audit, we identified errors in the financial statements that were not disclosed by BFO's checklist because the checklist does not prompt for agreement between the financial statements and the supporting documentation, or between the financial statements and related note disclosures.

[5] "Fiscal Year 2007 Financial Statement Audit Letter to Management," OIG Report #08-01, March 6, 2008, Recommendation 9. The text presented above has been corrected. Corrected text is presented in square brackets.

Memorandum on Internal Control

During our audit we identified differences between the financial statement presentation and BFO's supporting documentation which required additional audit procedures to reconcile the differences and confirm the accuracy of the statements. We identified a discrepancy of $3.2 billion between BFO's supporting workpapers and the audited Statement of Budgetary Resources. We also identified a $3.4 million discrepancy between the support and the required supplementary information disaggregating budgetary resources.

The BFO working papers are submitted as evidence for the sources of data and how they have been assembled into the final financial statement presentation as delivered for audit. Discrepancies between the two indicate (1) the lack of an effective review process and (2) the existence of some other undocumented process that may have been operating when the statements were prepared.

With respect to the accuracy of the financial presentation, our audit identified several notes to the financial statements that did not agree with the amounts recorded in the general ledger or reported in the financial statements. These errors required correction prior to publication.

We identified discrepancies between the audited balance sheet and the related note disclosures of intra-governmental transactions with the Social Security Administration and the Centers for Medicare and Medicaid Services. These discrepancies amounted to $200 million and $400,000 respectively. In addition the details of RRB's fund balance with Treasury disagreed with the audited statement of budgetary resources, under-reporting the "available" and "unavailable" components of that balance by $100,000 and $900,000 respectively, thus over-reporting the "obligated balance" not yet disbursed by approximately $1 million.

We also observed that certain controls over the financial statement preparation process had not been operating as designed during interim reporting periods. For example, BFO did not maintain evidence of the formal review and approval of the Balance Sheet and Statement of Net Cost for interim financial statements and that all adjusting entries were not subject to the same type of approval process.

In addition, during our audit, we identified differences between amounts recorded in the spreadsheets created to establish certain beginning balances for financial reporting and the balances as reported in the general ledger. There is also an inadequate audit trail for some prior-year balances. Although the discrepancies and lack of audit trail did not result in errors in the current-year financial statements, they do indicate a weak control environment and increased risk of undetected errors.

The OIG's prior recommendation for corrective action is pending for additional corrective action by management; no additional recommendations will be offered at this time.

Memorandum on Internal Control

Additional Controls Are Needed To Ensure Compliance with Requirements

We previously recommended that BFO:

> develop more detailed procedures for the change identification process used to update the form and content of the RRB's performance and accountability report, or replace it with a more comprehensive identification of requirements. Whichever method BFO uses should be supported by controls that include at least one level of supervisory approval and retention of supporting documentation. [6]

In response to our recommendation, BFO documented its procedures for the review of authoritative guidance for the purpose of identifying changes.

During the audit, we determined that the previously identified control deficiencies with form and content requirements persist. We identified instances of non-compliance or inadequate controls, which include the following issues:

- BFO does not have a formal review process of the crosswalks used in the preparation of agency financial statements;
- the note disclosure for "other liabilities" did not include all the details required by Office of Management and Budget (OMB) Circular A-136;
- the legal representation schedule did not include contact information as required by OMB Circular A-136; and
- BFO's procedure to identify and document changes in authoritative guidance does not always provide evidence that the changes have been implemented.

In addition, the fiscal year-end Statement of Budgetary Resources (SBR) submitted for audit was not compliant with U. S. Generally Accepted Accounting Principles (GAAP) and required extensive revision to obtain an unqualified auditor's opinion.

Early in FY 2008 OMB requested that the RRB change the budgetary accounting treatment for certain material transactions exceeding $3 billion. As a result, the FY 2007 SBR needed to be restated to provide comparability with the FY 2008 presentation. When BFO restated the FY 2007 SBR, they did not fully evaluate the impact of the change in accounting treatment which resulted in an SBR that did not properly reflect all transactions and was not compliant with the Treasury crosswalk. Responsible management advised the OIG that they had determined that a partial restatement would be sufficient. However, the OIG was not advised of this determination until after questioning the manner in which the restated SBR had been prepared. Ultimately, BFO needed to revise the SBR to obtain an unqualified opinion because the statement as originally drafted was not compliant with GAAP.

---

[6] "Fiscal Year 2006 Financial Statement Audit Letter to Management," OIG Report #07-01, February 9, 2007, Recommendation 11.

We believe the underlying cause of the non-compliant statements was weak controls and a lack of understanding of the potential impact of agency decisions on the audit process and the auditor's opinion.

A prior recommendation for corrective action is pending; the OIG has no additional recommendations to offer at this time.

ADDITIONAL WEAKNESSES IDENTIFIED DURING FY 2008

Earlier in this memorandum (see page 7), we discuss the need for improvement in the documentation that supports transactions recorded in the general ledger. This weakness in control was initially identified during FY 2006 and again reported in connection with our audit of the FY 2007 financial statements. Although the prior finding was based only on our observation of the operation of internal control; during FY 2008, we identified transactions that were not correctly recorded.

The following sections of this memorandum describe the errors identified during FY 2008 and our evaluation of agency efforts to implement a quality assurance process for the documentation that should support transaction recording. We believe that the weaknesses in documentation, the errors in general ledger recording and the need for a strengthened quality assurance process are closely related.

Review and Approval of Vouchers Needs Improvement

During our audit, we identified the following errors in benefit payment recording which we attribute to a weak review and approval process. On page 7 we reported that the documentation supporting general ledger recording of transactions continues to need improvement. Review and approval is a key part of controlling transactions recorded in the general ledger.

Benefit Payment Recording

As part of the summarization process, BFO enters various amounts into electronic spreadsheets to facilitate computations needed for general ledger recording. Input errors and formula errors resulted in the following general ledger recording errors:

- $9.9 million overstatement in the Railroad Retirement Supplemental Account and an understatement of $31.3 million in the Railroad Retirement Account; and
- $703,648 overstatement in the unemployment benefit expense account and an understatement of the same amount in the sickness benefit expense account as a result of errors made on nine vouchers.

Memorandum on Internal Control

Benefit Payment Reimbursement

We also identified an error which resulted in an under-reimbursement of $3,000 from the Social Security Administration. The RRB disburses Social Security benefits to those annuitants who are also entitled to a Social Security benefit at the same time it pays Railroad Retirement benefits. BFO requests reimbursement from the Social Security Administration for the amounts disbursed. During FY 2008, calculation errors made by BFO staff resulted in the under reimbursement of funds and a related understatement of the general ledger account balance.

Recommendation

We recommend that BFO:

2. ensure that the procedure for voucher approval includes tests of voucher accuracy.

Management's Response

BFO has agreed to ensure that the procedure for voucher approval includes tests of voucher accuracy. The full text of management's response is presented as Attachment 1 to this memorandum.

Quality Assurance Process for Voucher Preparation Not Yet Fully Effective

In FY 2007, BFO responded to an OIG recommendation by implementing a quality assurance process for voucher preparation. During FY 2008, BFO took action to further strengthen the process by reducing the number of acceptable errors, increasing the number of vouchers subject to review and randomly sampling from among all vouchers that support general ledger recording. BFO also conducted training in voucher preparation and provided a listing of required voucher documentation.

Although BFO has strengthened its quality assurance process for voucher preparation, our current-year assessment of the adequacy of voucher documentation (see page 7) has led us to conclude that the process is not fully effective. The current quality assurance process is not fully effective because it does not establish a desirable threshold for correct transactions and does not employ an accepted statistical methodology for assessing error rates.

During our review we also observed that the listing of required voucher documentation was incomplete and does not provide for retention of sufficient documentation in all cases.

Recommendations

We recommend that BFO:

3. implement a statistical methodology to measure the quality of voucher preparation; and
4. review the listing of required voucher documentation to ensure BFO staff will have reference to complete requirements.

Management's Response

BFO has agreed to implement a statistical methodology to measure the quality of voucher preparation. They have also agreed to review and update the listing of required voucher documentation. The full text of management's response is presented as Attachment 1 to this memorandum.

OTHER MATTERS INVOLVING INTERNAL CONTROL

During our audit, we also noted certain other matters involving the RRB's internal control structure and its operation. Although these matters do not rise to the level of a material weakness or significant deficiency, either individually or in the aggregate, they represent areas in which control weaknesses increase the risk of error or mishandling.

The details of our observations and recommendations for corrective action follow.

Implementation of the Modified Cash Basis of Accounting

We previously recommended that BFO:

> review the applicable standard and make specific documented determinations concerning how the modified cash basis of accounting impacts the accounting and reporting of tax revenue.[7]

In response to our recommendation, BFO updated the RRB Accounting Procedures Guide, which cites Statement of Federal Financial Accounting Standard No. 7, *Accounting for Revenue and Other Financing Sources* and Concepts for Reconciling Budgetary and Financial Accounting, paragraphs 51 and 172 to support their current accounting treatment for tax refunds. While paragraph 51 does state that cash refunds should be based on repayments of taxes during the period, paragraph 52 calls for an accrual adjustment, which modifies collections and refunds to determine the amount of revenue recognized. Paragraph 57 goes on to explain that a payable for refunds should be recognized when amounts are measurable and legally payable.

During our audit we determined that the previously identified condition persists. BFO has not provided specific documented determinations as to whether or not the refund amount confirmed by Treasury meets the measurable and legally payable criteria.

A prior recommendation for corrective action is pending; the OIG has no additional recommendations to offer at this time.

---

[7] "Fiscal Year 2007 Financial Statement Audit Letter to Management," OIG Report #08-01, March 6, 2008, Recommendation 2.

Accounting for Employee Benefits Could Be Enhanced

BFO could improve compliance with U.S. Standard General Ledger (USSGL) requirements by accounting for certain employee benefits directly to the required account and eliminating the reclassification of that expense at year-end.

The USSGL provides guidance concerning when to charge expenses to a benefit expense account or an operating expense account. It also provides guidance on whether or not the expense should be considered Federal (transactions between Federal agencies) or non-Federal (transactions with the public).

During the audit, we observed that BFO initially charges employee benefit expenses to an operating expense account, classified as “Federal” and then reclassifies most of the expenses to a benefit expense account, classified as “non-Federal.”

<u>Recommendation</u>

We recommend that BFO:

5. review applicable guidance for the accounting treatment of employee benefits and revise the RRB’s accounting treatment as necessary to comply with USSGL requirements.

<u>Management’s Response</u>

BFO has agreed to review applicable guidance for the accounting treatment of employee benefits and revise the RRB’s accounting treatment as necessary. The full text of management’s response is presented as Attachment 1 to this memorandum.

Password Protection Not Fully Effective

During our audit we observed that password security over the electronic spreadsheets that comprise the financial statement working papers, including the financial statements, is not fully effective. The password structure for the spreadsheets is widely known and, as a result, is largely ineffective in protecting files from accidental erasure or unauthorized changes. GAO Standards for Internal Control in the Federal Government states that access to resources and records should be limited to authorized individuals, and accountability for their custody and use should be assigned and maintained.[8]

---

[8] “Standards for Internal Control in the Federal Government,” GAO/AIMD-00-21.3.1 (11/99) page 15.

Recommendation

We recommend that BFO:

6. review the password security for the BFO working papers and make changes as necessary to ensure that the working papers are adequately protected.

Management's Response

BFO has agreed to review the password security for the BFO working papers and make changes as necessary. The full text of management's response is presented as Attachment 1 to this memorandum.

Separation of Duties for Federal Financial System (FFS) Administration Sometimes Over-ridden

During our audit, we observed that BFO has not ensured adequate separation of duties. Separation of duties is a key element of internal control. Key duties and responsibilities need to be divided or segregated among different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and handling any related assets. No one individual should control all key aspects of a transaction or event.[9]

FFS System Administrator Approves Some Transactions

BFO is the organizational owner of FFS, and the FFS system administrator is an employee in the Accounting, Treasury and Financial Systems Division of that organization. During the audit, we observed that the FFS system administrator prepared or approved certain transactions in the FFS system. In addition, the FFS system administrator also cancelled transactions for someone else.

A similar issue regarding the FFS system administrator's approval of transactions in FFS was previously addressed in FY 2006.[10] In response to a previous OIG recommendation, BFO adjusted the FFS security setting to ensure that one individual cannot enter and approve the same transaction. In January 2007, BFO issued a policy prohibiting administrators of systems owned by BFO from entering, approving or modifying transactions. Although BFO has implemented controls to ensure separation of duties, we were advised that in special situations the controls are circumvented to allow overlapping responsibilities.

---

[9] "Standards for Internal Control in the Federal Government," GAO/AIMD-00-21.3.1 (11/99) page 14.
[10] "Fiscal Year 2006 Financial Statement Audit Letter to Management," OIG Report #07-01, February 9, 2007, Recommendation 14, page 23.

Separation of Duties Is Sometimes Circumvented

An employee in BFO had access privileges to both enter and approve transactions including the transfer of funds. The approval access has since been revoked, however during the time period in which it was allowed, it was inconsistent with the principle of separation of duties.

Although BFO has implemented FFS controls that provide for separation of duties, BFO management has advised us that in special situations the system administrator changes the FFS settings thus circumventing the controls.

Recommendations

We recommend that BFO:

7. enforce the existing policy prohibiting the FFS system administrator from entering, approving, or modifying transactions processed by that system; and
8. enforce separation of duties within FFS to prevent employees from approving transactions that they have entered.

Management's Response

BFO has agreed to train and provide FFS access to two additional BFO staff who will then be able to enter or approve FFS transactions as necessary if the usual staff are on leave or otherwise unavailable. The full text of management's response is presented as Attachment 1 to this memorandum.

Controls Over Social Insurance Reporting Needs Improvement

The Bureau of the Actuary has not implemented a documented review and approval process that includes all schedules delivered in connection with the annual audit of agency financial statements.

We also observed that the documented description of control objectives, risks and techniques prepared as part of the RRB's management control review program is not fully descriptive of the Bureau of the Actuary's process for social insurance reporting.

Recommendations

We recommend that the Bureau of the Actuary:

9. implement an expanded review and approval process to ensure that all statements and supporting schedules are accurate and consistent; and
10. review and update management control review documentation.

Management's Response

The Bureau of the Actuary concurred with the recommendations. The full text of management's response is presented as Attachment 2 to this memorandum.

Documentation for Legal Representation Process Needs Improvement

The Office of General Counsel has not fully implemented new controls intended to ensure the adequacy of support for legal representations offered in connection with the financial statement audit.

In response to a prior OIG recommendation, the Office of General Counsel has developed written procedures for the legal representation process. These procedures provide for the retention of documentation to support estimates of potential financial impact, the determination of likelihood of loss, and a brief description of the litigation. This documentation is to be collected and retained in a single file supporting the annual representation letter.

During our audit, we observed that the file for the current-year representation letter was not complete. The file documentation retained did not always address every required element for each pending lawsuit.

Recommendation

We recommend that the Office of General Counsel:

11. strengthen controls to ensure compliance with procedures for the collection and retention of support for the legal representations.

Management's Response

The Office of General Counsel has agreed to strengthen controls to ensure compliance with procedures for the collection and retention of support for legal recommendations. The full text of management's response is presented as Attachment 3 to this memorandum.

Medicare Premium Penalty Rates at Risk of Error

Sampling tests of Medicare premium accuracy identified a beneficiary who had been overcharged $5,600 as a result of examiner error in assessing a penalty for delayed enrollment.[11,12]

The RRB computes the premium paid by Railroad Retirement beneficiaries who are qualified to enroll in the Medicare Part B program. The premium may be increased by a penalty amount if the beneficiary does not enroll in Medicare Part B upon first becoming eligible. Among the exceptions to this rule are persons covered by group health insurance plans who may elect to delay enrollment without penalty.

The OIG reviewed a random sample of 200 annuitants with Medicare premiums. Four of the 200 sample annuitants had been charged a penalty because they did not enroll within the required timeframes. We asked the Office of Programs to recalculate the amount of the penalty that had been charged in each of the four cases. In one of the four cases, the RRB had assessed a 60% penalty which incorrectly increased the premium paid by the annuitant. The annuitant was overcharged a total of $5,600 during a period of more than 12 years.

[11] During FY 2008, the OIG's authority to audit the RRB's Medicare Program was restored permitting the OIG to audit premium collection activity for the first time since 1997.

[12] We tested the accuracy of Medicare Premiums by testing the premium paid by 200 randomly selected beneficiaries from a universe of approximately 570,000 as of April, 2008. We identified one error resulting from an incorrect assessment of a penalty due to delayed enrollment which was one of the four such penalty cases in the sample.

The incorrect penalty had been applied because the annuitant's group coverage had not been considered when the premium amount was originally determined even though evidence of group health insurance coverage had previously been filed in the claim folder.

The error identified by the audit disclosed a risk associated with late enrollment penalties. We estimate that approximately 1,063 beneficiaries may presently be affected with a cumulative potential monetary impact of approximately $600,000[13].

Recommendations

We recommend that the Office of Programs:

12. identify and correct cases in which an incorrect Medicare Part B penalty is being collected; and
13. assess the current control environment to determine what action may be necessary to minimize the risk of errors in Medicare Part B premiums.

Management's Response

The Office of Programs has agreed to review additional cases and determine the level of error in the universe of cases with penalty rates. If the rate of error falls below their standards, they will determine how to handle cases on the rolls as well as how to reduce the level of errors on future cases. The full text of management's response is presented as Attachment 4 to this memorandum.

[13] The RRB's Office of Programs reports that as of September 2008, there were 4,252 beneficiaries currently being charged a penalty. The estimated number of errors and related monetary impact are based on the error experience of the sample applied to the universe of penalty cases provided by the Office of Programs, which we relied on without further testing.

Attachment 1

UNITED STATES GOVERNMENT
MEMORANDUM

FORM G-115f (1-92)
RAILROAD RETIREMENT BOARD

MAR 17 2009

TO : Letty B. Jay
Assistant Inspector General for Audit

FROM : John M. Walter
Chief of Accounting, Treasury and Financial Systems
THROUGH: Kenneth P. Boehne
Chief Financial Officer

SUBJECT: Letter to Management – Fiscal Year 2008 Financial Statement Audit

Thank you for giving us the opportunity to comment on your draft Letter to Management. The financial reporting process has expanded responsibilities and shorter time frames. The process has expanded from preparation of financial statements within 6 months of the fiscal year-end, to publication of an annual Performance and Accountability Report within 45 days of the fiscal year-end. In addition, during approximately the same time period the agency is required to complete intragovermental reporting and provide the Department of the Treasury with detailed fiscal yearend data, via the Governmentwide Financial Report System, that is used to prepare the Financial Report of the United States Government.

We have reviewed the above draft memorandum dated March 3, 2009, and our comments on recommendations are as follows:

Recommendations:

We recommend that BFO:

1. ***reconcile benefit payments as recorded in the general ledger to the benefit payment subsystem.***

   Accounting is reviewing the Office of Inspector General identified cost-effective reconciliation process and plans to implement it. Target date: 8/31/09.

2. ***ensure that the procedure for voucher approval includes tests of voucher accuracy.***

   Accounting plans to ensure that the procedure for voucher approval includes tests of voucher accuracy. Target date: 9/30/09.

3. ***implement a statistical methodology to measure the quality of voucher preparation.***

   Financial Management plans to implement a statistical methodology to measure the quality of voucher preparation. Target date: 9/30/09.

4. ***review the listing of required voucher documentation to ensure BFO staff will have reference to complete requirements.***

   Accounting plans to review and update the listing of required voucher documentation. Target date: 8/31/09.

5. ***review applicable guidance for the accounting treatment of employee benefits and revise the RRB's accounting treatment as necessary to comply with USSGL requirements.***

   Accounting plans to review applicable guidance for the accounting treatment of employee benefits and revise the RRB's accounting treatment as necessary. Target date: 8/31/09.

6. ***review the password security for the BFO working papers and make changes as necessary to ensure that the working papers are adequately protected.***

   Accounting plans to review the password security for the BFO working papers and make changes as necessary. Target date: 8/31/09.

7. ***enforce the existing policy prohibiting the FFS system administrator from entering, approving, or modifying transactions processed by that system.***

   We understand that there were two instances found where the FFS Systems Administrator (SA) either prepared or approved transactions that were posted to the general ledger. In each of these instances, the SA said that he was asked to either prepare or approve transactions because the usual staff was not present and the timing of the transaction was critical. The SA is aware of the January 2007 policy and an FFS report has been prepared that shows since January 9, 2009, the SA has not prepared, approved or deleted transactions that were posted to the general ledger. The SA has forwarded copies of the report to your office and will submit additional reports as requested.

In addition, we will train and provide FFS access to two additional BFO staff who will then be able to enter or approve FFS transactions as necessary if the usual staff are on leave or otherwise unavailable. This should help eliminate any further problems with separation of duties. Our target completion date is 4/30/09.

8. ***enforce separation of duties within FFS to prevent employees from approving transactions that they have entered.***

We understand that there were four instances found where the preparer was also the approver of transactions. In these instances, the transactions occurred to satisfy immediate funding requirements for travel, medical exams and other services during periods of time when no other staff was available for data entry purposes. The SA is aware of the policy and an FFS report has been prepared that shows since October 1, 2008, staff have not prepared and approved the same transactions. The SA has forwarded copies of the report to your office and will submit additional reports as requested.

In addition, we will train and provide FFS access to two additional BFO staff who will then be able to enter or approve FFS transactions as necessary if the usual staff are on leave or otherwise unavailable. This should help eliminate any further problems with separation of duties. Our target completion date is 4/30/09.

cc: Ed Fleming, Accounting Officer
Rich Lannin, Senior Accountant
Liz Stubits, Accountant
Edie Natividad, Accountant
Kris Garmager, Financial Systems Manager
Hattie Fitzgerald, Financial Compliance Officer
Georgia Blalock, Budget Officer
Bill Flynn, Executive Assistant
Jill Roellig, Management Analyst

 FORM G-115f (1-92)

UNITED STATES GOVERNMENT
MEMORANDUM

RAILROAD RETIREMENT BOARD

March 9, 2009

TO: Letty Benjamin Jay
Assistant Inspector General for Audit

FROM: Frank J. Buzzi Frank J. Buzzi
Chief Actuary

SUBJECT: Draft Letter to Management
FY 2008 Financial Statement Audit

Thank you for the opportunity to review and comment on the subject draft letter to management.

We concur with recommendations 9 and 10. Our target completion date for these recommendations is July 31, 2009.

cc: Chief Financial Officer

Attachment 3

FORM G-115f(1-92)

UNITED STATES GOVERNMENT

MEMORANDUM

RAILROAD RETIREMENT BOARD

March 4, 2009

To: Letty Benjamin Jay
Assistant Inspector General for Audit

From: Steven A. Bartholow
General Counsel

Subject: Draft Letter to Management
FY 2008 Financial Statement Audit

In response to your memorandum dated March 3, 2009, I have reviewed the draft Letter to Management and, in particular, the recommendation concerning the Office of General Counsel.

I concur with your recommendation that the Office of General Counsel strengthen controls to ensure compliance with procedures for the collection and retention of support for legal representations.

I previously submitted written procedures covering this area which were accepted by your office. However, in reviewing materials in connection the audit of financial statements, you noted that supporting documentation concerning the estimate of potential financial impact and description of litigation was not sufficient in all cases. By memorandum issued March 4, 2009, I have directed all attorneys in the Office of General Counsel to submit to me by April 1, 2009 a report of all litigation each of them handles. The report is to include the name of the case, the court in which filed, the date of filing, a description of the case, a cost estimate with explanation of the basis for the estimate, the likelihood of loss, and the current status of the case. I also directed that the same information be reported to me on a monthly basis going forward.

With the action I have taken, I believe that your recommendation, numbered 11, will be resolved by May 1, 2009.

UNITED STATES GOVERNMENT
MEMORANDUM

FORM G-115f (1-92)
RAILROAD RETIREMENT BOARD

MAR 16 2009

TO: Letty Benjamin Jay
Assistant Inspector General for Audit

FROM: Catherine A. Leyser *Catherine A. Leyser*
Director of Assessment and Training

THROUGH: Dorothy Isherwood *D Isherwood*
Director of Programs

SUBJECT: **Draft Report – Letter to Management, FY 2008 Financial Statement Audit**

Recommendation 12 The Office of Programs should identify and correct cases in which an incorrect Medicare Part B penalty is being collected.

OP response The OIG reviewed 4 cases and found 1 error which was an examiner error that happened 12 years earlier. On that basis, 1,073 erroneous cases and $600,000 are projected to be incorrect. We will review additional cases and determine the level of error in the universe of approximately 4,300 cases with penalty rates. If the rate of error falls below our standards, we will determine how to handle the cases on the rolls as well as how to reduce the level of errors on future cases. If additional actions to review more cases are warranted, we will develop an action plan to complete that review as well as a mechanism to track the monetary impact of the audit recommendation. If no additional actions are warranted, we will indicate that in our report and provide any monetary impact attributable to cases found in the study to the audit recommendation. In that case, there would be no further monetary tracking.

We will complete the evaluation and determine if there will be additional actions by December 31, 2009.

Recommendation 13	The Office of Programs should assess the current control environment to determine what action may be necessary to minimize the risk of errors in Medicare Part B premiums
OP response	See response to Recommendation 12. We will complete the assessment by December 31, 2009.