Audit Report

OIG-08-010

Audit of the Financial Management Service's Fiscal Years 2007 and 2006 Schedules of Non-Entity Government-Wide Cash

November 15, 2007

Office of Inspector General

Department of the Treasury

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

November 15, 2007

MEMORANDUM FOR KENNETH R. PAPAJ, COMMISSIONER
FINANCIAL MANAGEMENT SERVICE

FROM: Michael Fitzgerald /s/
Director, Financial Audits

SUBJECT: Audit of the Financial Management Service's
Fiscal Years 2007 and 2006 Schedules of Non-Entity
Government-wide Cash

I am pleased to transmit the attached audited Financial Management Service's (FMS) Fiscal Years (FY) 2007 and 2006 Schedules of Non-Entity Government-wide Cash (the Schedules). Under a contract monitored by the Office of Inspector General, Clifton Gunderson LLP, an independent certified public accounting firm, performed an audit of the Schedules of Non-Entity Government-wide Cash for FY 2007 and 2006. The contract required that the audit be performed in accordance with generally accepted government auditing standards; applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*; and the *GAO/PCIE Financial Audit Manual*.

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

- Independent Auditor's Report;
- Independent Auditor's Report on Internal Control; and
- Independent Auditor's Report on Compliance and Other Matters.

In its audit of FMS' Schedules, Clifton Gunderson LLP found:

- the Schedules present fairly, in all material respects, the balance of Non-Entity Government-wide Cash as of September 30, 2007 and 2006, in conformity with accounting principles generally accepted in the United States of America,

- certain deficiencies in internal control over financial reporting that were considered collectively to be a significant deficiency[1] (described below), and

- no instances of reportable noncompliance with laws and regulations tested.

Clifton Gunderson LLP concluded that there were general control weaknesses that did not effectively (1) ensure that an adequate entity-wide security management program is in place; (2) prevent unauthorized access to programs and files that control computer hardware and secure applications; or (3) prevent unauthorized access to and disclosure of sensitive information. Collectively these information security control issues indicate the lack of a fully effective entity-wide security management program.

In connection with the contract, we reviewed Clifton Gunderson 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, an opinion on FMS' Schedules or conclusions about the effectiveness of internal control or compliance with laws and regulations. Clifton Gunderson LLP is responsible for the attached auditor's reports dated November 8, 2007 and the conclusions expressed in the reports. However, our review disclosed no instances where Clifton Gunderson 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 Mark S. Levitt, Audit Manager, Financial Audits at (202) 927-5076.

Attachment

cc: Kenneth E. Carfine
Fiscal Assistant Secretary

[1] A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects FMS's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the schedule that is more than inconsequential will not be prevented or detected.

U. S. DEPARTMENT OF THE TREASURY,
FINANCIAL MANAGEMENT SERVICE
Washington, DC

INDEPENDENT AUDITOR'S REPORTS AND SCHEDULES OF NON-ENTITY GOVERNMENT-WIDE CASH

September 30, 2007 and 2006

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Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report

To the Inspector General,
U. S. Department of the Treasury and the
Commissioner of the Financial Management Service

We have audited the accompanying Schedules of Non-Entity Government-wide Cash of the U. S. Department of the Treasury's Financial Management Service (FMS) as of September 30, 2007 and 2006. These schedules are the responsibility of FMS' management. Our responsibility is to express an opinion on these schedules 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 applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the schedule is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the schedule. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall schedule presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the Schedules of Non-Entity Government-wide Cash referred to above present fairly, in all material respects, the balance of Non-Entity Government-wide Cash managed by FMS as of September 30, 2007 and 2006 in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our reports dated November 8, 2007, on our consideration of FMS' internal control over financial reporting relating to Non-Entity Government-wide Cash and on our tests of FMS' compliance with certain provisions of laws and regulations and other matters relating to Non-Entity Government-wide Cash. The purpose of those reports is to describe the scope of our testing of internal control over

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financial reporting and compliance and the results of that testing and not to provide an opinion on internal control over financial reporting or compliance. Those reports are an integral part of our audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Clifton Gunderson LLP

Calverton, Maryland
November 8, 2007

Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report on Internal Control

To the Inspector General,
U. S. Department of the Treasury and the
Commissioner of the Financial Management Service

We have audited the Schedule of Non-Entity Government-wide Cash (the schedule) of the U. S. Department of the Treasury's Financial Management Service (FMS), as of September 30, 2007, and have issued our report thereon dated November 8, 2007. We conducted our audit 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 applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*.

In planning and performing our audit, we considered FMS' internal control over financial reporting for Non-Entity Government-wide Cash as a basis for designing our auditing procedures, we obtained an understanding of design effectiveness of internal controls, determined whether they have been placed in operation, assessed control risk, and performed tests of FMS's controls for the purpose of expressing our opinion on the schedule and to comply with OMB Bulletin No. 07-04, but not for the purpose of expressing an opinion on the effectiveness of internal control over financial reporting. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982, such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide assurance on internal control. Accordingly, we do not express an opinion on the effectiveness of FMS's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider collectively to be a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects FMS's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such

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that there is more than a remote likelihood that a misstatement of the schedule that is more than inconsequential will not be prevented or detected by the FMS's internal control. We consider the deficiencies described below to be collectively a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the schedule will not be prevented or detected by the FMS's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the second paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies or material weaknesses; however, we do not believe that the significant deficiency described below is a material weakness.

Effectiveness of Computer Controls

FMS relies on extensive information technology (IT) systems to administer Government-wide cash. Internal controls over these operations are essential to ensure the integrity, confidentiality, and reliability of critical data while reducing the risk of errors, fraud and other illegal acts.

Our review of information technology controls covered general and selected application controls. General controls are the structure, policies and procedures that apply to an entity's overall computer systems. They include entity-wide security management, access controls, system software controls, application software development and change controls, segregation of duties, and service continuity controls. Application information security controls involve input, processing, and output controls related to specific IT applications.

We performed a review of the computer controls at the Hyattsville Regional Operations Center (HROC) and Kansas City Regional Operations Center using the *Federal Information Systems Controls Audit Manual*. Our review included general and selected application control testing of the Ca$hlink II, Treasury Offset Program (TOP), Government Wide Accounting (GWA) and Secure Payment System (SPS) applications.

For several years there have been IT general controls weaknesses at FMS, and most recently it was focused on the HROC. FMS continues to make progress and we commend FMS for the effort and improvement in the IT controls environment. Our testing revealed that there are still existing general control weaknesses that do not effectively (1) ensure that an adequate entity-wide security management program is in place; (2) prevent unauthorized access to programs and files that control computer hardware and secure applications; or (3) prevent unauthorized access to and disclosure of sensitive information. Collectively these information security control issues indicate the lack of a fully effective entity-wide security management program. Our detailed findings and recommendations will be provided to management in a separate sensitive but unclassified management report dated November 8, 2007. A summary of the key general controls findings follows:

Entity-wide Security Management – An entity-wide program for security planning and management represents the foundation for an entity's security control structure and a reflection of senior management's commitment to addressing security risks. The program should establish a framework and continuing cycle of activity for assessing risk, developing and implementing effective security procedures, and monitoring the effectiveness of these procedures. Without a well designed program, security controls may be inadequate; responsibilities may be unclear, misunderstood, and improperly implemented; and controls may be inconsistently applied. Such conditions may lead to insufficient protection of sensitive or critical resources and disproportionately high expenditures for controls over low-risk resources. The true measure of an Entity-wide Security Management Program is the ability to implement enhancements to the controls environment entity-wide, on all existing systems and platforms in use. FMS has demonstrated its ability to remediate specific IT findings. However, our current year audit identified that while weaknesses were corrected in some systems and platforms, they still continue to exist in other areas. This is evidenced by the continued existence of previously identified problems in newly reviewed IT areas indicating a lack of consistent application of an agency-wide strategy.

System Software – System software coordinates and helps control the input, processing, output, and data storage associated with all of the applications that run on a system. System software includes operating system software, system utilities, file maintenance software, security software, data communications systems, and database management systems. Controls over access to and modifications of system software are essential to protect the overall integrity and reliability of information systems. Previously noted mainframe operating system support issues were identified again this year.

Access Controls – Access controls are designed to limit or detect access to computer programs, data, equipment, and facilities to protect these resources from unauthorized modification, disclosure, loss, or impairment. Such controls include logical and physical security controls. A comprehensive access control security program, including increased management oversight, is needed to fully address the administration of access controls in order to increase the reliability of computerized data and decrease the risk of destruction or inappropriate disclosure of data. Although prior access control findings have been substantially addressed, additional access control weaknesses were identified again this year.

Management Response and Our Comments

Management has responded to our report and the full response is included in the attachment to this report. Management stated that they did not concur with our finding that FMS lacks consistent application of an agency-wide strategy to remediate specific IT findings but recognized that there are areas for improvements and agreed that they will take appropriate corrective actions to address specific audit results.

We have carefully reviewed management's response, however we have not changed our conclusion that general controls weaknesses existed in access controls and system software, and the continued existence of previously identified problems in newly reviewed IT areas is evident of the lack of fully effective entity-wide security management. Further, we continue to conclude that these weaknesses are a significant deficiency.

****

This report is intended solely for the information and use of the management of FMS, the Department of the Treasury Office of Inspector General, OMB, the Government Accountability Office and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Clifton Gunderson LLP

Calverton, Maryland
November 8, 2007

Clifton Gunderson LLP
Certified Public Accountants & Consultants

Independent Auditor's Report on Compliance and Other Matters

To the Inspector General,
U. S. Department of the Treasury and the
Commissioner of the Financial Management Service

We have audited the Schedule of Non-entity Government-wide Cash of the U. S. Department of the Treasury's Financial Management Service (FMS), as of September 30, 2007, and have issued our report thereon dated November 8, 2007. We conducted our audit 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 applicable provisions of Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*.

The management of FMS is responsible for complying with laws and regulations applicable to Non-Entity Government-wide Cash. As part of obtaining reasonable assurance about whether the Schedule of Non-Entity Government-wide Cash is free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of schedule amounts and certain other laws and regulations specified in OMB Bulletin No. 07-04. We limited our tests of compliance to those provisions, and we did not test compliance with all laws and regulations applicable to FMS.

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

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

This report is intended solely for the information and use of the management of FMS, the Department of the Treasury Office of Inspector General, the OMB, the Government Accountability Office and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Clifton Gunderson LLP

Calverton, Maryland
November 8, 2007

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U. S. DEPARTMENT OF THE TREASURY,
FINANCIAL MANAGEMENT SERVICE
SCHEDULES OF NON-ENTITY GOVERNMENT-WIDE CASH
(In Thousands)

	September 30,	
	2007	**2006**
Cash, foreign currency and other monetary assets (Notes 1 and 2)	$ 70,491,723	$ 44,243,218

The accompanying notes are an integral part of these schedules.

U. S. DEPARTMENT OF THE TREASURY,
FINANCIAL MANAGEMENT SERVICE
NOTES TO SCHEDULES OF NON-ENTITY GOVERNMENT-WIDE CASH
September 30, 2007 and 2006

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Financial Management Service (FMS) is a bureau of the U. S. Department of the Treasury (Treasury). FMS' mission is to improve the quality of the Federal Government's financial management. FMS' commitment and responsibility is to help its customers achieve success. FMS does this by linking program and financial management objectives and by providing financial services, information, advice, and assistance to its customers. FMS serves taxpayers, Treasury, federal program agencies, and government policy makers.

Non-Entity accounts are those accounts that FMS holds but are not available to FMS in its operations. For example, FMS accounts for certain cash that the Federal Government collects and holds on behalf of the U. S. Government or other entities. This schedule includes the Non-Entity government-wide cash accounts.

Basis of Accounting

The standards used in the preparation of the accompanying schedule are issued by the Federal Accounting Standards Advisory Board, as the body authorized to establish generally accepted accounting principles for Federal Government entities. Accordingly, the accompanying schedules are prepared in accordance with generally accepted accounting principles.

The accompanying schedule is different from the financial reports, prepared by FMS pursuant to OMB directives that are used to monitor and control FMS' use of budgetary resources.

Intra-governmental Financial Activities

The financial activities of FMS are affected by, and are dependent upon, those of the Treasury and the Federal Government as a whole. Thus, the accompanying schedules do not reflect the results of all financial decisions and activities applicable to FMS as if it were a stand-alone entity.

Non-entity Government-wide Cash

The Treasury General Account (TGA) is maintained at the Federal Reserve Bank of New York (FRBNY) and functions as the government's checking account for deposit and disbursement of public funds. Agencies can deposit funds that are submitted to them directly into either a Federal Reserve TGA or a local TGA depositary. The balances in these TGA accounts are transferred to the FRBNY's TGA at the end of each day. The Treasury Tax and Loan (TT&L) program

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

includes about 9,000 depositaries that accept tax payments and remit them the day after receipt to FRBNY's TGA. Certain TT&L depositaries also hold Non-entity Government-wide Cash in interest bearing accounts. Cash in the TGA and the TT&L program is restricted for Government-wide operations.

NOTE 2 – NON-ENTITY CASH, FOREIGN CURRENCY, AND OTHER MONETARY ASSETS

Non-Entity Cash, Foreign Currency, and Other Monetary Assets include the Operating Cash of the U.S. Government, managed by Treasury and foreign currency maintained by various U. S. and military disbursing offices, at September 30, 2007 and 2006 as follows:

	September 30,	
	2007	**2006**
Operating Cash of the U.S. Government:		
Held in Depositary Institutions	$ 69,797,268	$ 46,676,384
Held in the Federal Reserve Banks	5,538,744	5,568,594
Subtotal	**75,336,012**	**52,244,978**
Outstanding Checks	(5,634,828)	(8,657,616)
Subtotal	**69,701,184**	**43,587,362**
Other Cash	699,419	587,697
Subtotal	**70,400,603**	**44,175,059**
Foreign Currency	91,120	68,159
Total	$ 70,491,723	$ 44,243,218

Operating Cash of the U.S. Government represents balances from tax collections, customs duties, other revenue, federal debt receipts, and other various receipts net of cash outflows for budget outlays and other payments held in the Federal Reserve Banks, foreign and domestic financial institutions, and in U. S. Treasury Tax and loan accounts. Checks outstanding are netted against operating cash until they are cleared by the Federal Reserve System.

U. S. Treasury Tax and Loan Accounts include funds invested through the Term Investment Option program and the Repo Pilot program. Under the Term Investment Option program Treasury agrees that funds will remain in the account for the specified period of time. Under the Repo Pilot program Treasury "guarantees" that invested funds will remain in the account for the predetermined term of each investment. However, under both programs Treasury reserves the right to call the funds prior to maturity under special circumstances. Other cash is mostly comprised of Automated Clearinghouse transfers and other deferred items.

NOTE 2 – NON-ENTITY CASH, FOREIGN CURRENCY, AND OTHER MONETARY ASSETS (CONTINUED)

Operating Cash of the Federal Government held by depositary institutions is either insured (for balances up to $100,000) by the Federal Deposit Insurance Corporation or collateralized by securities pledged by the depositary institution, or through securities held under reverse repurchase agreements.

ATTACHMENT

DEPARTMENT OF THE TREASURY
FINANCIAL MANAGEMENT SERVICE
WASHINGTON, D.C. 20227

COMMISSIONER

November 9, 2007

Mr. Bill Oliver, Partner
Clifton Gunderson, LLP
11710 Beltsville Drive, Suite 300
Beltsville, MD 20705

Dear Mr. Oliver:

This letter is in response to your reports to the Inspector General of the U.S. Department of the Treasury and the Commissioner of the Financial Management Service (FMS) on the Schedules of Non-Entity Government-wide Cash as of September 30, 2007 and 2006.

Once again, we are pleased to receive an unqualified audit opinion on the Schedules and that no material weaknesses related to internal controls over financial reporting were noted in your report. We also appreciate your statement that FMS continues to make progress and is to be commended for the effort and improvement in the information technology (IT) controls environment. We agree that there are areas in which we can make improvements; however, we would like to point out that we do not concur with your finding that FMS lacks consistent application of an agency-wide strategy to remediate specific IT findings as stated in the following paragraphs.

FMS has a comprehensive entity-wide IT security management program in place. The strength of this program is demonstrated by many factors, including:

1. Each system on the FMS portfolio has an Information System Security Officer (ISSO) who is appointed in writing by the accrediting official. Each ISSO signs a statement acknowledging their responsibilities, including the responsibility for meeting the FISMA and FMS IT Security Program requirements.

2. FMS submits monthly and semi-annual incident reports to the Treasury Computer Incident Response Center (TCIRC). These reports indicate that no incidents resulted in unauthorized access to programs and files that control computer hardware and secure applications disclosure of sensitive information in the HROC environment.

3. FMS has implemented an on-going risk assessment process. All systems complete annual security reviews, either by undergoing formal risk assessments as part of the certification and accreditation process or by conducting and documenting continuous monitoring.

4. FMS has a governance process in place that reviews and approves all IT investments that are in production and under development. This governance

process includes a comprehensive set of sub-processes intended to address the financial and technical well-being of FMS' IT environment. The capital planning and investment control process addresses both financial and technical criteria, including security controls. Security compliance is documented in the 300 budget documents for the IT investments.

5. FMS has an entity-wide business continuity program in place.

6. FMS has an IT oversight and compliance program in place.

7. This past year, FMS developed a pre-audit checklist to evaluate each system for FISMA compliance as well as to validate that previous audit issues do not exist. Each system owner completed this checklist and all potential issues were documented and discussed with the IT Security Oversight and Compliance Staff.

We consider the findings cited for Government-Wide cash to be either corrected or successfully managed from a risk management perspective:

1. The CASHLINK II Plan of Actions and Milestones (POA&M) has been developed in accordance with OMB, Treasury and FMS guidance. All outstanding findings have been prioritized and are being tracked to completion.

2. The specific statements, which had not yet been updated in the TOP and SPS security documents, posed no risks to the computer system or information and are considered housekeeping items. FMS reviews and updates its security plans annually and such adjustments are typically addressed as part of this change process.

3. The specific TOP Rules of Behavior, which had not yet been signed, did not put the system or its information at risk for not having them on file. FMS requires recertification for its applications on an annual basis and for its general support systems on a semi-annual basis.

4. FMS took immediate action to correct the finding identified for the TOP database server.

5. FMS has briefed the highest levels of management on the detailed audit findings and has assured management that appropriate and timely corrective actions will be taken. A draft plan of actions and milestones has been developed.

In addition, the auditors considered three of the twelve Government-Wide Cash Notice of Findings and Recommendations (NFRs) to be repeat findings. However, two of these findings were not identical to prior year findings and have mitigation strategies in progress.

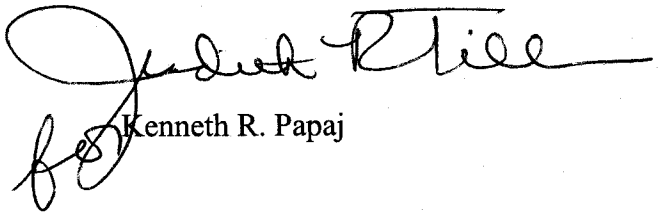
1. The repeat finding related to system software was similar to a finding from two years ago. FMS does not consider operating under zOS Version 1, Release 4 as putting our information and systems at unacceptable risk. FMS cited nine (9) mitigating controls in place to mitigate any residual risk. At no time during the fiscal year were mission critical systems unavailable for processing or compromised in any way.

2. The repeat finding related to physical access has an on-going corrective action that is subject to agreement and scheduling with the building owner as well as funding authorization. FMS is committed to mitigating any residual risk as evidenced by having the related work on schedule.

Following a detailed analysis, the third repeat finding related to logical access exceptions was minimal, i.e., access was removed one or two days later than FMS standards stated it should be. FMS feels the intent of the standard was clearly met.

FMS appreciates the feedback resulting from the audit on the implementation of our security controls and will take appropriate corrective actions to address the specific audit results. In addition, we will, as we have in the past, look at the effect of issues across the board for all of our systems and develop entity-wide corrective actions as appropriate. FMS will continue to actively implement, monitor, and correct computer-control deficiencies for individual systems as well as from an entity-wide perspective. Upon receipt of your limited official use management letter, FMS will give careful consideration to the recommendations and will continue to improve in the areas related to entity-wide security management, system software, and access controls. Specific corrective action plans and timetables will be formulated as soon as management determines the appropriate course of action.

Sincerely,



Kenneth R. Papaj