

U.S. International Trade Commission

Audit of Internal Controls Related to the PP&E Account



OIG-AR-08-10

July 7, 2010



Office of Inspector General

The U.S. International Trade Commission is an independent, nonpartisan, quasi-judicial federal agency that provides trade expertise to both the legislative and executive branches of government, determines the impact of imports on U.S. industries, and directs actions against certain unfair trade practices, such as patent, trademark, and copyright infringement. USITC analysts and economists investigate and publish reports on U.S. industries and the global trends that affect them. The agency also maintains and publishes the Harmonized Tariff Schedule of the United States.

Commissioners

Deanna Tanner Okun, Chairman

Charlotte R. Lane

Daniel R. Pearson

Shara L. Aranoff

Irving A. Williamson

Dean A. Pinkert

OFFICE OF INSPECTOR GENERAL



UNITED STATES INTERNATIONAL TRADE COMMISSION

WASHINGTON, DC 20436

July 7, 2010

OIG-HH-019

Chairman Okun:

This memorandum transmits the Office of Inspector General's final audit report *Audit of Internal Controls Related to the PP&E Account*. In finalizing the report, we analyzed your comments on our draft report and have included those comments in their entirety in Appendix A.

This report contains one recommendation for corrective action. In the next 30 days, please provide me with your management decisions describing the specific actions that you will take to implement the recommendation.

Thank you for the courtesies extended to the auditors during this audit.

Sincerely,

A handwritten signature in blue ink that reads "Philip M. Heneghan".

Philip M. Heneghan
Inspector General

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Results of Review

The purpose of this review was to confirm that the Commission has the appropriate internal controls in place to substantiate the balance of the Property, Plant, and Equipment (PP&E) account on the 2009 Financial Statement.

Management was unable to provide complete or accurate documentation to support the amounts recorded, as a result we were unable to obtain sufficient evidence to substantiate the amounts presented in the PP&E account on the 2009 Financial Statement.

Specifically, we were unable to find:

- Documentation to support an on-top adjustment (for reclassifying assets) in the PP&E account in the amount of \$1.4 million;
- Documentation to support an on-top adjustment (for accumulated depreciation) in the PP&E account in the amount of \$234 thousand;
- Documentation to define the rationale for calculating and monitoring the values reported in the PP&E account;
- Documentation to determine the useful life of an asset;
- Documentation to determine depreciation methods; and
- Documentation to determine the threshold for capitalization of bulk purchases.

Management did not have the appropriate internal controls in place to substantiate the balance of the PP&E account on the 2009 Financial Statement. The inability to substantiate the balances in the account puts the Commission at risk for potential misuse of government funds, an increased probability of reporting errors, and greater risk of noncompliance with applicable laws, regulations, and standards. The results of the review are described in further detail below.

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Problem Areas & Recommendations

Problem Area 1:

***On-Top Adjustments Recorded to the PP&E Account
Could Not be Substantiated***

The review identified material differences on the amount recorded by the Commission as an on-top adjustment to the PP&E account for the Internal-Use software (IUS) general ledger account and related contra asset account.

The Office of Finance was unable to provide complete and accurate documentation to support the costs associated with two of the on-top adjustments recorded in the PP&E account. As a result, the Commission was unable to substantiate the balance reported in the FY 2009 financial statement for the PP&E account.

We identified the following three conditions:

- Lack of procedures requiring that complete, valid, and accurate documentation be maintained to support each amount recorded in the PP&E account
- Lack of a policy requiring that a detailed review to reconcile and validate all on-top adjustments be conducted
- Lack of procedures requiring that a detailed review be conducted of all adjustments prior to posting to the general ledger and financial statements.

All three of these conditions were previously reported in *Independent Auditor's Report on Internal Control for Financial Statements*, OIG-AR-02-10. Management decisions have been agreed upon and final action is already underway. No further recommendations were identified in this area as a result of this review.

Problem Area 2:

***Lack of Established Property, Plant, and Equipment (PP&E)
Policies and Procedures***

During the review, we noted that the Commission did not have formal policies and procedures in place to support the rationale for calculating and monitoring the values reported in the PP&E account. For example policies were not in place to:

- Determine the useful life of an asset
- Calculate depreciation

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- Determine the threshold for capitalization of bulk purchases

The Commission has not documented or distributed formal policies or standardized procedures to support values reported in the PP&E account. As a result, the financial information reported in the PP&E account could be materially misstated. In addition, there is an increased risk that the Commission is not in compliance with applicable laws, regulations, and standards.

The following two conditions were reported:

- Lack of policies and standardized procedures that document the rationale for calculating and monitoring the values reported in the PP&E account in accordance with applicable standards, laws, and regulations,
- Lack of communication, dissemination, and training to relevant personnel within all levels of the organization on the policies and procedures for calculating and monitoring values reported in the PP&E account.

Both of these conditions were previously reported in *Independent Auditor's Report on Internal Control for Financial Statements*, OIG-AR-02-10. Management decisions have been agreed upon and final action is already underway. No further recommendations were identified in this area as a result of this review.

Problem Area 3:

Lack of Documentation Supporting Capital Acquisitions

Our review of acquisition files to support the leasing of equipment by the Commission found that documentation was missing to support the purchase versus lease decision. The Commission currently pays \$216,508 a year for two equipment leases. If the leases are carried through the lease life, the total cost would be \$966,052. The Commission could not provide any documentation to support the determination that purchasing the equipment would have been substantially more expensive and therefore not the best value for the government.

Documentation should be maintained that support the investment planning process for capital assets purchased or leased in order to document the decision on the best value for the government. Internal controls should be designed to provide reasonable assurance regarding prevention of or prompt detection of unauthorized acquisition, use, or disposition of assets. In addition, there was no documentation that a best value analysis was performed before a determination was made to lease the equipment.

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Documentation supporting the detailed analysis of the useful life used for the leases was not prepared. Our review of documentation provided in support of the assets which the Commission believed to be capital leases noted errors in the rationale used to record the leases as capital assets instead of operating expenses. The Commission used an estimated useful life of four and five years respectively for the leases, apparently using previous leasing timelines of similar equipment as the rationale for establishing the useful life. An asset's useful life is defined as a period over which an asset is expected to be usable, with normal repairs and maintenance, for the purpose it was acquired, rented, or leased.

In the case of the leased machines, research performed by the independent auditors, including discussions with the company that leased the assets, indicated that the useful life of similar machines was 15 to 20 years, not four or five years as indicated by the Commission. As a result, the financial statements liabilities were materially overstated by the decision to record the leases as capital assets rather than operating expenses.

In addition, errors on the financial statements should have been discovered and corrected before the revised financial statements were provided to us. We identified the following four conditions:

- Lack of a current organizational structure to ensure adequate resources are allocated to the Office of Finance
- Lack of training for financial staff on federal accounting and reporting requirements, as well as on the accounting servicer's financial system
- Lack of formal policies and procedures to ensure the Commission is in compliance with applicable accounting, financial management and reporting standards and regulations
- Lack of a policy that identifies which financial management decisions need to be reviewed outside the Office of Finance to ensure decisions are supported and in accordance with applicable accounting standards and OMB regulations.

All four of these conditions were previously reported in *Independent Auditor's Report on Internal Control for Financial Statements*, OIG-AR-02-10. Management decisions have been agreed upon and final action is underway. One additional recommendation was identified in this area as a result of this review.

Recommendation 1:

That the Commission establish documentation standards for acquisition files to support conclusions reached as to the best value for the government.

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Management Comments and Our Analysis

On June 28, 2010, Chairman Deanna Tanner Okun provided management comments to the draft audit report. The Chairman concurred with our assessment, and acknowledged the that the three problem areas identified in the report needed to be resolved and were now being actively addressed by management.

Objective, Scope, and Methodology

Objective:

The objective of this evaluation was to confirm that the Commission has sufficient internal controls in place to substantiate the balance of the PP&E account on the 2009 Financial Statements.

Scope:

This evaluation was limited to testing internal controls necessary to achieve the objectives described in the Office of Management and Budget Bulletin No. 07-04, Audit Requirements for Federal Financial Statement, as amended, in regards to the balance of the PP&E account as recorded on the 2009 Financial Statement.

Methodology:

We engaged the services of an independent public accounting firm to substantiate the balance on the PP&E account and review the related the internal controls such as, policies and procedures to support the rationale for calculating and monitoring the values reported in the PP&E account, and acquisition files to support capital planning decisions as reported on the Commission's 2009 balance sheet. The audit was limited in nature and therefore would not necessarily identify all deficiencies in internal control over financial reporting.

The auditors performed an examination of evidence to support the amounts for assets recorded in the PP&E account on the 2009 financial statements. The auditors also assessed the standards used to support the rationale and calculation of values reported for assets recorded in the PP&E account.

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The Office of Inspector General engaged the services of an Independent Public Accountant who performed this audit in accordance with Generally Accepted Government Auditing Standards (GAGAS). Those standards require that the audit be planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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Appendix A

Appendix A: Management Comments on Draft Report




UNITED STATES INTERNATIONAL TRADE COMMISSION

WASHINGTON, DC 20436
C076-HH-003

June 28, 2010

MEMORANDUM

TO: Philip M. Heneghan, Inspector General

FROM: Chairman Deanna Tanner Okun 

SUBJECT: Management Response to the Draft Audit Report, "Review of Internal Controls Related to PP&E"

I am in receipt of the Inspector General's draft audit report, *Review of Internal Controls Related to PP&E*, dated May 27, 2010. I appreciate the opportunity to review the draft report and to provide a response to the findings. The draft audit report concludes that the Commission does not have appropriate internal controls in place to substantiate the balance of the property, plant and equipment (PP&E) account on the 2009 financial statement, and identifies three problem areas and one recommendation. I concur with your assessment and acknowledge the importance of resolving the deficiencies identified in your report in order for the Commission to be in compliance with financial management laws and regulations, and successfully confirm PP&E balances for future audits.

Each of the problem areas and, with one exception, recommendations in the draft audit report were previously identified in *Independent Auditor's Report on Internal Control for 2009 Financial Statements* (OIG-AR-02-10.) The Commission is undertaking corrective actions in response to that audit report that will also address these problem areas and recommendations.

I also note that the Commission has retained a human capital contractor to evaluate the Commission's organizational structure and resources with respect to financial management, procurement, and other administrative functions. The Commission will use the results of this

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Appendix A

evaluation to ensure that it has skilled personnel in necessary positions, and that it allocates adequate resources to the financial management and procurement functions.

The Commission is taking the following actions with respect to each problem area:

Problem Area 1: On-Top Adjustments Recorded to PP&E Account Could Not be Substantiated

The on-top adjustments identified in this problem area could not be substantiated because the Commission lacked supporting documentation, and more broadly, lacked policies, procedures, and internal controls to ensure that such adjustments were properly supported and recorded. With the assistance of knowledgeable contract resources, the Commission is developing policies and procedures with respect to the acquisition, tracking, and accounting of internal use software and other capitalized assets, and on manual adjustments to the accounting system.

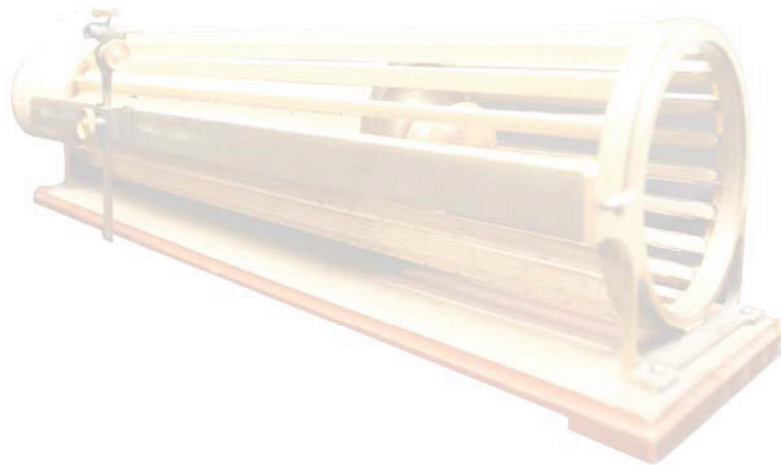
Problem Area 2: Lack of Established PP&E Policies and Procedures

I agree that the Commission has not maintained documentation to support values reported in the PP&E accounts. As noted above, with contractor assistance the Commission is developing necessary policies and procedures, and will compile these into a comprehensive accounting manual as a reference for staff. Staff will be trained in the new policies and procedures as they are implemented and updated. The Commission hopes to complete the policies and procedures relating to PP&E by September 30, 2010.

Problem Area 3: Lack of Documentation Supporting Capital Acquisitions

Policies, procedures, and training programs being developed will address the establishment of asset files, so that financial management and procurement decisions, such as best value analysis, are supported and in accordance with applicable accounting standards and OMB reporting requirements and regulations.

In addition, a review of all procurements over the past five years is underway to determine if assets are properly capitalized, and asset files are being established so that supporting documentation is complete and available. The Office of Finance expects that prior period adjustments made as a result of this review will eliminate on-top adjustments for fiscal year 2010.



“Thacher’s Calculating Instrument” developed by Edwin Thacher in the late 1870s. It is a cylindrical, rotating slide rule able to perform complex mathematical calculations involving roots and powers quickly. The instrument was used by architects, engineers, and actuaries as a measuring device.

To Promote and Preserve the Efficiency, Effectiveness, and Integrity of the U.S. International Trade Commission



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