Audit of NLRB's Fiscal Year 1999 Accounting and Reporting Systems Report No. OIG-F-8-01-01

INSPECTOR GENERAL

NATIONAL LABOR RELATIONS BOARD

WASHINGTON, DC 20570

December 12, 2000

I hereby submit an *Audit of NLRB's Fiscal Year 1999 Accounting and Reporting Systems,* Report No. OIG-F-8-01-01. This review was conducted to evaluate the Agency's capability to prepare audited financial statements.

The National Labor Relations Board (NLRB or Agency) is not required by law to prepare audited financial statements. However, choosing to prepare audited financial statements is a good business practice voluntarily adopted by several similarly sized agencies. NLRB's credibility would be enhanced if it could demonstrate, through audited financial statements, that the Agency's financial management is sound and in conformance with applicable government standards.

The Agency currently records most financial transactions that are needed to prepare the principal statements, and the data recorded is reasonably accurate. We identified five areas where transactions would have to be recorded or corrected. These were workers' compensation, imputed financing costs, a capitalized lease, amortization of computer software, and depreciation.

NLRB management is responsible for complying with laws and regulations applicable to the Agency. We found no instances of noncompliance with laws and regulations that would have to be reported in an audit of the financial statements. We found that the Agency's financial management systems substantially complied with the U.S. Government Standard General Ledger at the transaction level. The financial management systems did not substantially comply with the Federal financial management systems requirements or Federal accounting standards.

We considered one matter, information security, involving the internal control and its operation to be a material weakness. With respect to internal controls related to performance measures, we obtained an understanding of the design of significant internal controls but do not provide an opinion on such controls.

We identified two conditions that would be reported to management in a letter rather than in the report on internal control. One was on time and attendance issues, the other involved capitalized and sensitive property.

Recommendations addressing these findings are numbered consecutively throughout the report and can be found on pages 5 and 8 of this report. Management agreed with the findings and completed actions on all recommended actions but one, and that will be done by the end of the year.

We recommended that the Finance Branch Chief coordinate with the General Counsel and Board to obtain a decision on whether the Agency will prepare annual financial statements and have periodic audits. After due consideration, the Chairman and General Counsel decided that audited financial statements need not be prepared at this time, but that the matter would be revisited at a later date at the Inspector General's request or if circumstances change.

Although we continue to believe auditing the financial statements is a sound business policy, we understand this decision in light of the fact that the Agency may have a new Chairman and General Counsel within a year. We will reassess our recommendation when we evaluate the potential impact of the Reports Consolidation Act, enacted on November 22, 2000, on Agency operations. This Act allows agencies to consolidate and adjust the frequency and timing of financial and performance management reports.

An exit conference was held on October 23, 2000, with the Deputy Director of Administration, Finance Branch Chief, and other officials from the Division of Administration. The Director of Administration submitted written comments on the draft report. She agreed with the findings and recommendations made in the report. The Director of Administration's comments are presented in their entirety as an appendix to this report.

Jane E. Altenhofen
Inspector General

BACKGROUND

Increasing demands for Government accountability led to passage of the Chief Financial Officers (CFO) Act of 1990. The CFO Act established a position in designated agencies for an official who reports directly to the head of the agency to oversee all financial management activities. To help improve the integrity of financial information, in 1990, the Office of Management and Budget (OMB), the Department of Treasury, and the General Accounting Office (GAO) established the Federal Accounting Standards Advisory Board (FASAB) to develop accounting standards for the U.S. Government.

Several laws enacted in 1996 further strengthened accountability. The Government Management and Reform Act (GMRA) of 1996 amended the CFO Act to require, among other things, the annual preparation and audit of organization-wide financial statements of 24 executive departments and agencies. The Federal Financial Management Improvement Act (FFMIA) of 1996 requires that the report on these audits state whether agency financial management systems comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger (SGL) at the transaction level.

OMB Bulletin 97-01, *Form and Content of Agency Financial Statements*, defines the form and content of financial statements of executive departments and agencies that are required to prepare audited financial statements by 31 U.S.C. 3515(d). OMB Bulletin 97-01 incorporates the FASAB concepts and standards that are the basis for generally accepted accounting principles (GAAP) for the Federal Government. GAAP includes the Statements of Federal Financial Accounting Concepts and Statements of Federal Financial Accounting Standards (SFFASs) recommended by the FASAB and approved by the Secretary of the Treasury, Director of OMB, and the Comptroller General.

The National Labor Relations Board (NLRB or Agency) administers the principal labor-relations law of the United States, the National Labor Relations Act of 1935, as amended. Approximately 30,000 charges of unfair labor practices and 6,000 representation petitions are filed with the NLRB each year. For Fiscal Year (FY) 2000, the Agency was provided an appropriation of close to $206 million and authorized 1,947 full time equivalents to staff operations at Headquarters and 51 Regional, Subregional, and Resident Offices and 3 Division of Judges satellite offices.

Executive agencies, including the NLRB, are mandated by law to follow the accounting principles, standards, and requirements prescribed by the Comptroller General, and currently issued by FASAB. NLRB is not subject to the CFO Act; however, the Director of Administration serves as the Chief Financial Officer.

OBJECTIVES, SCOPE, AND METHODOLOGY

This review was conducted to evaluate the Agency's capability to prepare audited financial statements. To accomplish this we determined whether: current systems were capable of collecting and compiling information necessary to produce reliable financial reports; transactions were in compliance with applicable laws, regulations, and accounting principles; there was accountability over property; and internal controls were effective.

We interviewed Agency officials responsible for financial management, including program managers and Regional Office staff. On a test basis, we examined evidence supporting the amounts recorded in the financial reports during FY 1999. We tested internal controls and compliance with laws and regulations including: Anti-deficiency Act; Budget and Accounting Procedures Act; Federal Managers' Financial Integrity Act of 1982; Fair Labor Standards Act of 1938; Civil Service Retirement Act of 1930; Civil Service Reform Act of 1978; Federal Employees' Compensation Act; Federal Employees' Health Benefits Act of 1959; Prompt Payment Act; and Federal Travel Regulations.

We relied on several audit and inspection reports issued by the Office of Inspector General (OIG) as identified in the exhibit. We used these reports to form conclusions related to safeguarding of capitalized and sensitive property, predominately computers and related equipment, and internal controls and compliance with laws and regulations. During this audit we tested time and attendance (T&A) at the Division of Judges in Washington.

We tested items from the Payroll/Personnel System to determine whether employees were getting paid at the appropriate rate, that amounts charged for retirement, health insurance, and life insurance were correct, and entries into the system were authorized and appropriately documented. We reviewed official personnel files to determine whether they included forms: SF-61, Oath of Office; I-9, Employment Eligibility Verification; and SF-61B, Declaration of Appointee. We also reviewed administrative processing of the Federal Employee Compensation Act program.

We selected a sample of 15 pieces of capitalized property from the Agency's official property records and telephoned Regional Offices to confirm the property's existence, description, serial number, and bar code number.

We selected two statistical samples to test disbursement transactions: one for travel expenses and another that included transactions other than rent, travel, and compensation and benefits. Our testing determined whether disbursements were made in accordance with applicable laws and regulations, processed in accordance with Agency processes and procedures, supported by adequate documentation, and correctly classified. We analyzed space rental charges to identify unusual activity and determined if amounts were accurately recorded in the Agency's financial records.

We reviewed account balances as of September 30, 1999. Cash balances on the SGL were traced to Department of Treasury reports. We reviewed accounts receivable and liability accounts for reasonableness, tested items by tracing them to supporting documentation, reviewed the process for recording accounts receivable, and searched for unrecorded liabilities at year end. We reviewed unliquidated obligations to determine if they were valid obligations and recorded in the correct period. We reviewed the compensation and benefits accrual and unfunded annual leave balance for reasonableness. We reviewed the accuracy of capitalized property records and verified depreciation calculations.

The effectiveness of internal controls and information security over financial management systems was determined through a review performed by an independent certified public account firm under contract with the OIG.

This audit was performed in accordance with generally accepted government auditing standards during the period January through October 2000.

FINDINGS

AUDITED FINANCIAL STATEMENTS

The NLRB is not required to prepare audited financial statements under either GMRA or the CFO Act. However, choosing to prepare audited financial statements is a sound business practice voluntarily adopted by several similarly sized agencies. NLRB's credibility would be enhanced if it could demonstrate, through audited financial statements, that the Agency's financial management is sound and in conformance with applicable government standards.

An audit of financial operations results in an opinion on the financial statements, a report on compliance with laws and regulations, and a report on internal control. A management letter may also be prepared which discusses findings and recommendations for improvements in internal controls that were identified during the audit, but were not material enough to be in the report on internal control. Generally, preparing audited financial statements leads to the development of better financial information which, when provided to management and decision makers, will provide the basis for producing better decisions. Reliable financial information is essential for analyzing the Government's financial condition and providing additional information beyond that provided in the budget.

With a reasonable amount of effort, the Agency could prepare the required financial statements for an audit. The necessary data is mostly available in existing documents and financial systems. The Finance Branch staff would need training to prepare the financial statements, but this training could easily be provided in conjunction with the training needed for the staff to maintain current knowledge of FASAB standards. A cost would be incurred for the audits that could be done on an annual or bi-annual basis.

As set forth in OMB Bulletin 97-01, a financial statement includes:

(1) Overview of the Reporting Entity (also called Management's Discussion and Analysis); and

(2) Principal Statements and Related Notes, including the:

(a) Balance Sheet;
(b) Statement of Net Cost;
(c) Statement of Changes in Net Position;
(d) Statement of Budgetary Resources;
(e) Statement of Financing;
(f) Statement of Custodial Activity, if applicable; and
(g) Notes to Principal Statements.

The overview of the reporting entity addresses the mission and organization structure, performance goals and results, and limitations of the financial statements. This section would require some original writing, but much of the information is already available in the reports prepared to meet requirements of the Government Performance and Results Act.

NLRB is required to record transactions in accordance with the FASAB. This data would be the basis for preparing the first five principal statements and related notes. As discussed in the next section, additional data would need to be recorded in order to be in full compliance with FASAB. NLRB would not need to prepare a statement of custodial activity which is required for entities that collect non-exchange revenue for the General Fund of the Treasury, a trust fund (such as Social Security), or other recipient entities. Custodial collections are usually items such as taxes or duties collected by the Internal Revenue Service or the U.S. Customs Service.

We specifically reviewed how backpay funds would be treated in the financial statements. The preferred method for backpay is for the respondent to write a check to the discriminatee and provide it to the Regional Office to deliver to the discriminatee. These transactions would not need to be recorded into the general ledger or reported in the financial statements according to an official from the GAO who consulted with the FASAB. When the Agency is provided backpay funds from the respondent and is responsible for making disbursements though the Department of Treasury, the Agency currently records these amounts in the general ledger in a manner that would allow them to be appropriately identified in the financial statements.

Other agencies that voluntarily prepare audited financial statements include the United States International Trade Commission, Federal Trade Commission, Federal Communications Commission, and Farm Credit Administration. Three of these agencies were able to report to Congress that auditors had issued unqualified opinions on the FY 1999 financial statements.

Recommendation

We recommend that the Finance Branch Chief:

1. Coordinate with the General Counsel and Board to obtain a decision on whether the Agency will prepare annual financial statements and have periodic audits.

Management's Comments

Management agreed with the finding and took action to implement the recommendation. After due consideration, the Chairman and General Counsel decided that audited financial statements need not be prepared at this time.

PRINCIPAL STATEMENTS

The Agency currently records most financial transactions that are needed to prepare the principal statements, and the data recorded is reasonably accurate. We identified five areas where transactions would have to be recorded or corrected in the SGL for the Agency records to be in accordance with OMB Bulletin 97-01 and GAAP. These involved liability for future workers' compensation, imputed financing costs, a capitalized lease, amortization of computer software, and depreciation.

Workers' Compensation

Liabilities for future workers' compensation claims were not recorded. A liability for Federal accounting purposes, as defined by SFFAS No.5, is a probable future outflow or other sacrifice of resources as a result of past transactions or events. SFFAS No. 5 further states that general purpose Federal financial reports should recognize probable and measurable future outflows arising from past exchange transactions, government-related events, government-acknowledged events, or non-exchange transactions that, according to current law and applicable policy, are unpaid amounts due as of the reporting date.

The Finance Branch would need to calculate the amount of liability for workers' compensation. For comparison, the Federal Trade Commission, an agency with under 1,000 employees, recorded approximately $2 million in future workers' compensation in FY 1999 and FY 1998.

Imputed Financing Costs

The Agency did not record imputed financing costs related to retirement and post-employment benefits of more than $11 million.

SSFAS No. 5 states that the actuarial determined liability and expense of the plan, including all its provisions, is part of the pension plan's liability and expense estimate. SSFAS No.5 further states that the Federal employer entity should recognize a pension expense in its financial report that equals the service cost for its employees for the accounting period, less the amount contributed by the employees, if any.

The Finance Branch calculated the imputed financing costs and provided the amount to the Office of Personnel Management (OPM). The Finance Branch would need to establish the appropriate accounts in order to record the costs in the Agency's financial management system. The Agency calculated the "imputed" cost as $11 million, which is the difference between the true cost of providing future benefits to employees and the employer and employee contributions remitted to OPM.

Capitalized Lease

The Agency did not identify and record as a capital lease a photocopy machine that met applicable criteria. A portion of the lease amount (approximately $24,000 of the $36,600 total cost) should have been recorded as capitalized equipment as well as the related liability and depreciation.

The Agency policy is to capitalize equipment costing more than $10,000 and depreciate photocopy equipment over a period of five years. Capital leases, as defined by SFFAS No.6, transfer substantially all the benefits and risks of ownership to the lessee. Leases are capitalized, if at inception, the lease:

- Transfers ownership of the property to the lessee by the end of the lease term;
- Contains an option to purchase the leased property at a bargain price;
- The term is equal to or greater than 75 percent of the estimated economic life of the leased property; or
- The present value of rental and other minimum lease payments, excluding that portion of the payments representing executory cost, equals 90 percent of the fair value of the leased property.

In June 1999 the Agency entered into a lease agreement for a photocopy machine. The lease plan was for 60 months at $610 per month, for a total of $36,600, of which $27,600 related to leasing costs and $9,000 related to maintenance. Since the lease term equals the depreciation period used by the Agency for photocopy equipment, we concluded that the term of the lease is greater than 75 percent of the estimated economic life of the leased property and the machine should be capitalized.

Amortization of Computer Software

The Agency did not record nearly $78,000 in amortization of capitalized automated data processing software. Approximately $4,500 was applicable to FY 1999 and $73,500 was for prior years.

SFFAS No. 6 refers to the SGL for identification of capitalized software. The SGL definition of Information Technology Software includes the capitalized cost of purchased off-the-shelf software and provides for related amortization.

The Agency depreciates computer equipment over a period of 3 years. We applied the same basis for software. The Agency capitalized nearly $78,000 of computer software purchased in FY 1997 or before. This software should have been mostly amortized in prior fiscal years, and was fully amortized as of September 30, 1999. The portion applicable to FY 1999 of $4,529.63 was the final amortization expense for $13,588.88 of software purchased in FY 1997.

Depreciation

The Agency incorrectly recorded depreciation expense in FY 1998, which resulted in a $6,343 overstatement of accumulated depreciation in FY 1999.

SFFAS No. 6 states that depreciation expense shall be recognized. Depreciation is the systematic allocation of the cost of property over its useful life. Property is recognized when title passes or it is delivered to the entity.

The NLRB depreciates computer equipment over a period of 3 years. Computer equipment costing $19,030 was received in October 1998 and paid for in November 1998. Depreciation expense of $6,343 was incorrectly recorded in FY 1998, which then resulted in an overstatement of the accumulated depreciation in FY 1999. The accumulated depreciation on this equipment was recorded as $12,687 as of September 30, 1999, but should have been $6,343.

Recommendations

We recommend that the Finance Branch Chief:

2. Establish accounts to record workers' compensation and imputed financing costs in future years;

3. Record a capitalized lease and related liability and depreciation for the photocopy machine;

4. Record accumulated amortization on the computer software purchased in FYs 1995, 1996, and 1997; and

5. Adjust accumulated depreciation on computer equipment acquired in FY 1999 rather than FY 1998.

Management's Comments

Management agreed with the findings and took action to implement most recommendations. The accounts were established to record workers' compensation and imputed financing costs and the Finance Branch Chief is determining the amounts to be recorded. The capitalized lease and corresponding liability have been posted; the depreciation will be recorded by December 31, 2000. The appropriate entries were made to record the accumulated amortization on computer software and accumulated depreciation on computer equipment.

COMPLIANCE WITH LAWS AND REGULATIONS

Management of the NLRB is responsible for complying with laws and regulations applicable to the Agency. Exclusive of FFMIA, we found no instances of noncompliance with laws and regulations that would have to be reported in an audit of the financial statements. We found the Agency's financial management systems substantially complied with the SGL at the transaction level. The financial management systems did not substantially comply with the Federal financial management systems requirements or Federal accounting standards.

In an audit of the Agency's financial statements, a report on compliance with laws and regulations would be prepared to conclude whether or not the Agency was in compliance with laws and regulations that would materially impact the financial statements. For FFMIA, the auditor must report on whether the Agency's financial management systems substantially comply with the Federal financial management systems requirements, Federal accounting standards, and the SGL at the transaction level.

The financial management systems did not substantially comply with the Federal financial management systems requirements. The OIG *Review of Information Systems Security* reported the Agency was not in full compliance with government-wide policy requirements.

The financial management systems did not substantially comply with Federal accounting standards. As discussed previously in this report, the Agency did not record workers' compensation and imputed financing costs. Federal accounting standards require that these items be recorded in the SGL regardless of whether financial statements are prepared.

INTERNAL CONTROL

We considered one matter, information security, involving the internal control and its operation to be a material weakness. With respect to internal controls related to performance measures, we obtained an understanding of the design of significant internal controls but do not provide an opinion on such controls.

A report on internal control identifies reportable conditions and material weaknesses. Reportable conditions are matters relating to sufficient deficiencies in the design or operation of the internal controls that could adversely affect the Agency's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

We identified material weaknesses in the Agency's financial management systems. The OIG *Review of Information Systems Security* reported access controls over financial systems need improvement and raised significant concerns about the reliability, accuracy, integrity, and completeness of the information maintained in the financial systems. The report further stated the Finance Branch had not developed adequate segregation of duty controls to prevent one person from performing incompatible functions, and service continuity controls did not provide sufficient protection against the impact of a local or national disaster or significant business disruptions.

MANAGEMENT LETTER

We identified several conditions that would be reported to management in a letter rather than in the report on internal control. These involved T&A and capitalized and sensitive property.

Time and Attendance

The Agency did not maintain adequate control over T&A in accordance with GAO Office Policy and Procedures Manual for Guidance of Federal Agencies, Title 6 - Pay, Leave, and Allowances, dated March 22, 1996, and Agency policy.

We found the following results in our inspections of four Regional Offices.

- Sick leave in all four offices was not advanced in accordance with Agency policy.
- Bi-weekly T&A reports were either not regularly approved or a significant number were not approved in three offices.
- Accurate work schedules evidencing supervisory approval did not exist in three offices.
- Credit hours earned by employees were not recorded into the Agency's official records in two offices.

- A significant number of leave slips were not maintained in two offices.
- One office had an inappropriate person performing T&A activities.

We performed comparable procedures at the Division of Judges in Washington.

Of the 50 sick leave transactions reviewed we found: 10 were not supported by a leave slip; 14 leave slips were not approved by the supervisor; and 1 was not signed by the employee. Of the 50 annual leave transactions reviewed we found: 3 were not supported by a leave slip; 23 were not approved by a supervisor; and 1 was not signed by the employee. We reviewed the bi-weekly T&A reports related to the sick leave and annual leave transactions tested, 100 transactions in total. We found that: 93 were not initialed by the timekeeper; 2 were not initialed by the employee; and 42 were not signed by the supervisor.

These results were comparable to the findings reported in the OIG *Evaluation of Time and Attendance Practices*. We made multiple recommendations in that audit report for Agency-wide improvements. Management agreed to implement all but one of the recommendations. On June 19, 2000, the Director of Personnel issued a memorandum to all Agency employees that addressed many of the recommendations. When the remaining recommendations are implemented, T&A deficiencies in the Regions and the Division of Judges should be addressed.

Capitalized and Sensitive Property

Results obtained in three of the four Regional Offices we inspected showed that: official property records did not accurately reflect computer equipment at Regional Offices or the locations within the offices; records maintained by Regional Office staff did not accurately identify computer equipment in their office; and that computer property records maintained by Regional Offices were not in agreement with the official property records maintained at Headquarters by the Information Technology Branch. We also found that controls over computer equipment sent from Regional Offices to Headquarters for repair were not sufficient.

We selected a judgmental sample of 15 pieces of capitalized property from Agency records to verify the equipment's existence and the accuracy of the records. We found problems with six items, 40 per cent of the items reviewed. Serial numbers provided by Regional Offices did not match property records for three items. Two of these three did not have a bar code number. We also had one occurrence of three other errors: the property description in official Agency records was inconsistent with information provided by the Regional Office, property that was excessed was not annotated as such on Agency property records, and the bar code number provided by the Regional Office did not match official Agency property records.

OIG plans to schedule an audit of controls over automated data processing equipment in FY 2001.

EXHIBIT

Reports Relied Upon in the Audit of NLRB's FY 1999 Accounting and Reporting Systems

Title	Report Number	Date Issued
Accounting and Reporting Systems in the Brooklyn Regional Office	OIG-INS-06-00-03	July 6, 2000
Accounting and Reporting Systems in the Cleveland Regional Office	OIG-INS-07-00-04	July 6, 2000
Accounting and Reporting Systems in the Seattle Regional Office	OIG-INS-08-00-05	July 6, 2000
Accounting and Reporting Systems in the Chicago Regional Office	OIG-INS-09-00-06	July 6, 2000
Evaluation of Time and Attendance Practices	OIG-AMR-29-00-01	February 23, 2000

Review of Information Systems Security	OIG-AMR-30-00-03	September 29, 2000

APPENDIX

UNITED STATES GOVERNMENT
National Labor Relations Board

Memorandum

November 30, 2000

TO: Jane Altenhofen
Inspector General

FROM: Gloria Joseph
Director of Administration

SUBJECT: Draft Report (OIG-F-8-00-xx)

This is in response to your memorandum, dated October 24, 2000, regarding the Draft Report "Audit of NLRB's Fiscal Year 1999 Accounting and Reporting Systems".

Attached are five action plans that outline the specific actions, which have been taken with regard to each of the five recommendations. Actions in response to four of the five recommendations have been completed. Recommendation 3 of 5 has a target completion date of December 31, 2000.

We have no comment on any other aspect of the report. Please contact me on 273-3890 if you have any questions.

Attachment

Cc: Chairman
General Counsel
Finance Branch Chief