February 8, 2008

LYNN MALCOLM
VICE PRESIDENT, CONTROLLER

SUBJECT: Fiscal Year 2007 Postal Service Financial Statements Audit – Eagan Information Technology and Accounting Service Center (Report Number FT-AR-08-007)

This report presents the results of our audit of selected financial activities and accounting records at the U.S. Postal Service Information Technology and Accounting Service Center (IT/ASC) in Eagan, Minnesota, for the fiscal year (FY) ended September 30, 2007 (Project Number 07BM003FT000). The Postal Reorganization Act of 1970, as amended, requires annual audits of the Postal Service's financial statements. We conducted this audit in support of the independent public accounting firm's overall audit opinion on the Postal Service's financial statements. Please refer to Appendix A for additional information about this audit.

Overall Audit Conclusion

- Financial accounting policies and procedures provided for an adequate internal control structure and complied with accounting principles generally accepted in the U.S.
- Accounting transactions at the Eagan IT/ASC impacting the general ledger account balances were stated in accordance with accounting principles generally accepted in the U.S.
- General ledger account balances conformed to the general classification of accounts on a basis consistent with that of the previous year.
- The Postal Service complied with laws and regulations that have a direct and material effect on the financial statements.
- No adjustments were proposed.
- An internal control deficiency regarding account reconciliations was identified. This item was not significant to the financial statements and did not affect the overall adequacy of internal controls.

Account Reconciliations

- The Postal Service did not always timely clear reconciling items for two liability accounts.[1] One reconciling item dated back to at least October 2003.

Criteria

- Postal Service Handbook F-20, *General Ledger Accounting and Financial Reporting,* Chapter 9, dated December 2004.
- Financial Reporting Standards.[2]

Cause

- The Postal Service listed funds each month as part of an automated journal voucher[3] on the account reconciliation form;[4] however, the funds were adjusting items and did not post with this journal voucher. Adjusting items must be posted using a manual journal voucher because they require human interaction.[5]
- Although approvers signed the reconciliation forms as evidence of review and approval, oversight was not adequate to ensure management resolved adjusting items, employees reported revenue timely, and employees made entries to correct balances in the general ledger.
- Guidelines did not address specific timeframes for resolving reconciling items that cannot be resolved by the end of the next reconciling period.

Effect

- Management understated revenue by $2.7 million.

Corrective Action

- St. Louis IT/ASC personnel recognized the understated revenue.

We plan to report $2,706,979 as monetary impact, Recoverable Revenue Loss, in our *Semiannual Report to Congress.* Please refer to Appendix B for our detailed analysis of this issue.

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[1] Account [redacted] – Miscellaneous Other and Account [redacted] – Federal Tax Withholding.
[2] Statement on Auditing Standards, Section 326, Evidential Matter; Statement of Financial Accounting Concepts No. 2 – Qualitative Characteristics of Accounting Information – Timeliness, paragraph 56; Statement of Financial Accounting Concepts No. 6 – Elements of Financial Statements – Recognition, Matching, and Allocation, paragraph 145.
[3] Automated journal vouchers are mechanisms used to post financial transactions to the general ledger automatically, requiring no human interaction.
[4] IT/ASC personnel use Postal Service form 3131, *Standard Reconciliation of Accounts*, to perform reconciliations. Refer to Appendix C for an example of this form.
[5] Manual journal vouchers are mechanisms used to post financial transactions that require human interaction to the general ledger.

We recommend the Vice President, Controller:

1. Reiterate to accounting service center personnel the proper presentation of adjusting items on the monthly account reconciliation form.

2. Enhance oversight activities to include detailed reviews of reconciliations and all supporting documentation.

3. Coordinate with the Manager, Accounting Services, to enhance accounting service center procedures to include timeframes for resolving reconciling items that cannot be resolved within a reconciling period, and consider a requirement to date all reconciling items.

Management Comments

- Management agreed with the recommendations and plans to discuss the issues and update procedures to improve controls over account reconciliations by the end of FY 2008. Management also agreed with the monetary impact of $2,706,979 but not the category of Recoverable Revenue Loss. However, they realize we are limited in our categories. We have included management's comments, in their entirety, in Appendix D

Evaluation of Management's Comments

- Management's comments are responsive to the recommendations and the actions taken or planned should correct the issues identified in the finding.

Progress on Prior Year's Recommendations

We followed up on prior years' recommendations related to our financial statement audits at the Eagan IT/ASC.[6]

The Postal Service did not always follow Internal Revenue Service (IRS) employment tax regulations for reporting salary overpayments. We recommended that management revise policy to comply with IRS tax regulations, establish accounts receivable for gross amounts due, and inform employees of tax implications.

Progress

- Management is in the process of enhancing the payroll and accounts receivable system.
- The Postal Service is evaluating alternative solutions because previously proposed mechanical solutions resulted in more complications.
- The target completion date for system enhancements, including associated notifications, is December 31, 2008.

[6] *Fiscal Year 2005 Postal Service Financial Statement Audit – Eagan Information Technology and Accounting Service Center* (Report Number FT-AR-06-009, dated January 10, 2006).

Audit Comment

- The U.S. Postal Service Office of Inspector General (OIG) will continue to monitor this area as part of our annual financial statement audit work.

We appreciate the cooperation and courtesies provided by your staff. If you have any questions or need additional information, please contact Lorie Nelson, Director, Financial Reporting, or me at (703) 248-2100.

John E. Cihota
Deputy Assistant Inspector General
for Financial Operations

Attachments

cc: H. Glen Walker
Stephen J. Nickerson
Vincent H. DeVito, Jr.
Jo Ann E. Mitchell
Katherine S. Banks

APPENDIX A: ADDITIONAL INFORMATION

BACKGROUND

The Eagan IT/ASC is one of three accounting service centers Postal Service-wide.[7] It functions as a large, centralized accounting and disbursement center and its employees are responsible for processing payroll, maintaining the general ledger, reconciling financial data, and maintaining cash and receivable accounts.

We will issue separate financial statement audit reports for Headquarters and the San Mateo and St. Louis IT/ASCs. Further, in addition to the overall opinion on the Postal Service's financial statements, the Board of Governors' independent public accounting firm, contracted to express an opinion on the financial statements, will issue separate reports on the Postal Service's internal controls and compliance with laws and regulations. Finally, we will issue a separate report for the audit of the FY 2007 information system controls at the Eagan, Minnesota; San Mateo, California; and St. Louis, Missouri IT/ASCs and the Raleigh, North Carolina Information Technology Service Center.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of the audit were to determine whether:

- The financial accounting policies and procedures provide for an adequate internal control structure and comply with accounting principles generally accepted in the U.S.
- Accounting transactions at the Eagan IT/ASC impacting the general ledger account balances for assets, liabilities, equity, income, and expenses of the Postal Service are fairly stated in accordance with accounting principles generally accepted in the U.S.
- General ledger account balances conform to the general classification of accounts of the Postal Service on a basis consistent with that of the previous year.
- The Postal Service complies with laws and regulations that have a material and direct effect on the financial statements as a whole.

To accomplish our objectives, we conducted fieldwork from November 2006 through November 2007. As part of our audit, we assessed internal controls, tested transactions, and verified account balances. We conducted this audit from November 2006 through February 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient audit evidence to limit audit risk to a low level that is, in our professional judgment, appropriate for supporting the overall audit opinion on the financial

[7] The other IT/ASCs are located in San Mateo, California, and St. Louis, Missouri.

statements. Those standards also require considering the results of previous engagements and following up on known significant findings and recommendations that directly relate to the objectives of the audit. An audit also includes obtaining a sufficient understanding of internal control to plan the audit and to determine the nature, timing, and extent of audit procedures to be performed. We supported the external auditors in obtaining reasonable assurance about whether the financial statements are free of material misstatement (whether caused by error or fraud). Absolute assurance is not attainable because of the nature of audit evidence and the characteristics of fraud. Therefore, an audit conducted in accordance with generally accepted government auditing standards may not detect a material misstatement. However, the external auditors and the OIG are responsible for ensuring that appropriate Postal Service officials are aware of any significant deficiencies that come to our attention. We discussed our observations and conclusions with management officials on October 26 and December 11, 2007, and included their comments where appropriate.

We relied on computer-generated data from several Postal Service financial systems, including the Accounting Data Mart, General Ledger, Time and Attendance Collection System, Pay Calculation, Complement Management and Selection System, and Employee Master File. We performed specific internal control and transaction tests on these systems' data, to include tracing selected financial information to supporting source records. For example, we traced payroll system reports to original journal voucher transactions.

PRIOR AUDIT COVERAGE

Report Title	Report Number	Final Report Date	Results
Fiscal Year 2006 Postal Service Financial Statements Audit – Eagan Information Technology and Accounting Service Center	FT-AR-07-007	December 29, 2006	No significant issues reported. Corrective action was taken on the two interim issues on disbursing activities reported prior to year's end.
Fiscal Year 2005 Postal Service Financial Statement Audit – Eagan Information Technology and Accounting Service Center	FT-AR-06-009	January 10, 2006	See the "Progress on Prior Year's Recommendations" section of this report.

APPENDIX B: DETAILED ANALYSIS

Account Reconciliation

The Postal Service did not always timely clear reconciling items.[8] Specifically, we identified two liability accounts, reconciled monthly, where items remained on the form from previous fiscal years. In one account, the reconciling item, dating back to at least October 2003, related to payments of $2,706,979 from foreign countries; however, no support was provided at the time for the transactions. Using a conservative approach, the Postal Service posted the amount as a liability while waiting for proper documentation. The other account had a reconciling item dating back to August 2006. The reconciling item represented a misclassification between general ledger accounts of $345,984, with no monetary impact.

Account reconciliations identify and correct differences between subsidiary (detail) ledger totals and the general ledger balance of an account. IT/ASC personnel use Postal Service form 3131, *Standard Reconciliation of Accounts*, to perform reconciliations. Refer to Appendix C for an example of this form. Financial reporting standards require that assets and liabilities be valued properly and adjustments to values be realized as soon as they are quantifiable.

This occurred for one general ledger liability account ([redacted] – Miscellaneous Other) because the Postal Service listed these funds each month as part of an automated journal voucher on the account reconciliation form, although the funds were adjusting items. Adjusting items must be posted using a manual journal voucher because they require human interaction. For the other liability account ([redacted] – Federal Tax Withholding), the reconciling item was listed on the supporting detail schedule but was not reflected on the reconciliation form. The Postal Service stated these items were not resolved timely because of staff transitions. Further, although approvers signed the reconciliation forms as evidence of review and approval, oversight activity was not adequate to ensure that adjusting items were resolved, revenue was reported timely, and entries were recorded in the general ledger accounts. Finally, Postal Service policy states that (1) an integral part of the reconciliation process is making the necessary correcting entries before the end of the next reconciliation period and (2) supervisors must correct errors and omissions timely.[9] However, the policy does not give specific timeframes for resolving reconciling items when this is not feasible.

As a result, the Postal Service did not record $2.7 million in revenue timely. The risk of a material misstatement is increased when reconciling items are not resolved timely. After our discussion with management, they recognized the revenue and reclassified

[8] A reconciling item is a transaction reflected differently in the subsidiary (detail) ledger than in the general ledger (outstanding checks, unrecorded deposits, or checks that clear for amounts different from what was recorded).
[9] Postal Service Handbook F-20, *General Ledger Accounting and Financial Reporting System*, Chapter 9, dated December 2004.

the reconciling items in the other liability accounts. We plan to report $2,706,979 as monetary impact, Recoverable Revenue Loss, in our *Semiannual Report to Congress.*

APPENDIX C: POSTAL SERVICE FORM 3131, *STANDARD RECONCILIATION OF ACCOUNTS*

U. S. Postal Service	Month and FY	Primary Account Number	
Standard Reconciliation of Accounts		Subaccount Number	
Account Title		End Date	
Balance Sheet Category		**DEBIT**	**CREDIT**
1. Balance Per General Ledger			
2. Adjustments Affecting Above General Ledger Balance to Reconcile			
3. Adjusted General Ledger Balance (Net of lines 1 and 2)			
4. Subsidiary Ledger Balance (Sum of supporting detail)			
5. Adjustments to Subsidiary Ledger			
6. Adjusted Subsidiary Ledger Balance			

Preparer's Name and Title (Print or type)	Signature of Preparer	Date
Approving Official's Name and Title (Print or type)	Signature of Approving Official	Date
System Accountant's Name and Title (Print or type)	Signature of Systems Accountant	Date

PS Form **3131**, September 2005

APPENDIX D: MANAGEMENT'S COMMENTS

LYNN MALCOLM
VICE PRESIDENT, CONTROLLER

UNITED STATES POSTAL SERVICE

January 9, 2008

LUCINE M. WILLIS

SUBJECT: Draft Audit Report—Fiscal Year 2007 Postal Service Financial Statements Audit—Eagan Information Technology and Accounting Service Center (Report Number FT-AR-08- DRAFT)

Attached are postal management's responses to each of the recommendations contained in the subject audit report. We appreciate the opportunity to review and provide comments.

Although we do not agree with the categorization of lost revenue for the monetary impact, we understand that you are limited in your descriptions and do not dispute the dollar amount.

Lynn Malcolm
Lynn Malcolm

Attachment

cc: H. Glen Walker
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The following are the recommendations to the Controller from Report Number FT-AR-08-DRAFT and postal management's response to each.

Recommendation #1

Reiterate to accounting service center personnel the proper presentation of adjusting items on the monthly account reconciliation form.

Response

Management agrees with this recommendation and will review this issue with all three accounting service centers at the January 2008 joint meeting.

Recommendation #2

Enhance oversight activities to include detailed reviews of reconciliations and all supporting documentation.

Response

Management agrees with this recommendation and will incorporate oversight activities into the current procedures by the end of FY 2008.

Recommendation #3

Coordinate with the Manager, Accounting Services, to enhance accounting service center procedures to include timeframes for resolving reconciling items that cannot be resolved within a reconciling period, and consider a requirement to date all reconciling items.

Response

Management agrees with this recommendation and will work with Corporate Accounting Policy to develop timeframes dependent upon the reconciliation. We also agree that a reconciling item should be dated. The target for enhancing these procedures is the end of FY 2008.