Written Testimony of
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Chairman Roe, Ranking Member Andrews, and Members of the Subcommittee; thank you for the invitation to come before you today to discuss the two audit engagements of the U.S. Department of Labor's (DOL) fiscal year (FY) 2010 consolidated financial statements.

KPMG LLP (KPMG), under contract to the DOL Office of Inspector General (OIG), was engaged to audit DOL's FY 2010 consolidated financial statements. During FY 2010, DOL encountered significant functionality and operational issues related to its new financial accounting and reporting system, the New Core Financial Management System (NCFMS), which was implemented in January 2010. These issues hindered DOL's ability to assure the accuracy and completeness of consolidated financial statement balances and to provide us the critical financial data necessary to complete our testing over DOL's FY 2010 consolidated financial statements during our initial audit engagement. The significant areas that were impacted by these issues are discussed in more detail below.

<u>Unemployment Trust Fund (UTF)</u> – We were unable to complete testing over the UTF significant accounts (i.e., unemployment benefit expenses, accrued benefits, revenue, accounts receivables, advances and transfers) because DOL was unable to timely provide us complete and accurate populations of the related data that reflected the balances recorded in the general ledger. This situation was caused by errors in recording UTF transactions and failure to perform certain reconciliations to the general ledger.

<u>Gross Costs (Non-Payroll, Non-Benefits)</u> – In addition to unemployment benefit expenses, we were unable to complete testing over certain other expenses because a complete and accurate population of these expenses that agreed to the related balances recorded in the general ledger could not be provided timely. In addition, because we could not test these expenses, our testing over the grant accrual could not be completed.

<u>Budget Accounts</u> – The final *Report on Budget Execution and Budgetary Resources* (SF-133) for the fourth quarter was not provided to us prior to the November 15, 2010 Office of Management and Budget (OMB) reporting deadline. Therefore, we were unable to complete our testing over the fourth quarter reconciliations of the Statement of Budgetary Resources (SBR) to the SF-133s and reconciliations of the SF-133s to the *Apportionment and Reapportionment Schedule* (SF-132s). As a result, we were unable to conclude on budgetary resources, the status of budgetary resources, the change in obligated balance, and net outlays reported in the SBR. Further, a complete and accurate population of undelivered orders recorded in the general ledger as of September 30, 2010 could not be provided for testing, and we were unable to complete the

procedures necessary to conclude on borrowing authority related to repayable advances to the UTF.

Fund Balance with Treasury – DOL was unable to reconcile the net differences that were identified between its fund balance with Treasury account as of September 30, 2010 and the U.S. Department of the Treasury's records, which prevented us from completing our testing of this balance.

Financial Reporting – DOL management was unable to provide certain representations regarding consistency with U.S. generally accepted accounting principles with respect to the presentation of the FY 2010 consolidated financial statements that it issued on November 15, 2010.

It was impractical to extend our procedures sufficiently to determine the extent, if any, to which DOL's FY 2010 consolidated financial statements may have been affected by the aforementioned issues. As such, our initial audit engagement resulted in a disclaimer of an opinion on the FY 2010 consolidated financial statements issued by DOL on November 15, 2010. A disclaimer of opinion states that the auditors do not express an opinion on the financial statements as they were unable to form or have not formed an opinion as to the fairness of presentation of the financial statements in conformity with generally accepted accounting principles.

In planning and performing our initial FY 2010 audit engagement, we considered DOL's internal control over financial reporting by obtaining an understanding of DOL's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls as required by auditing standards generally accepted in the United States and *Government Auditing Standards*. These procedures were designed to assist us in planning our auditing procedures and contribute to the evidence supporting the auditors' report on the financial statements. However, the objective of our engagement was not to express an opinion on the effectiveness of DOL's internal control over financial reporting and therefore our procedures were not designed to identify all deficiencies in internal control. A deficiency in internal control 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 and correct misstatements on a timely basis.

Under *Government Auditing Standards,* we are required to report material weaknesses and significant deficiencies identified during the audit engagement. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

During our initial FY 2010 audit engagement, we identified the following deficiencies in internal control over financial reporting that we considered to be material weaknesses or significant deficiencies.

Material Weaknesses

1. Lack of Sufficient Controls over Financial Reporting
2. Lack of Sufficient Controls over Budgetary Accounting
3. Improvements Needed in the Preparation and Review of Journal Entries
4. Lack of Adequate Controls over Access to Key Financial and Support Systems

Significant Deficiencies

5. Weakness Noted over Payroll Accounting
6. Untimely and Inaccurate Processing of Property, Plant, and Equipment Transactions

DOL recognized the need for, at minimum, an audited consolidated balance sheet as of September 30, 2010, in order to receive an opinion on all its consolidated financial statements in FY 2011. Therefore, DOL decided to revise and reissue its FY 2010 consolidated financial statements once certain analyses were performed, errors were identified, and adjusting journal entries were recorded to correct the previously reported amounts, as necessary.

As a result, DOL requested that the OIG perform audit procedures necessary to report on its revised FY 2010 consolidated financial statements, in anticipation of receiving an updated audit report. In December 2010, the OIG engaged KPMG to audit these revised financial statements.

Because of the aforementioned control deficiencies, our planned audit approach for the second FY 2010 audit engagement did not include additional tests of controls, and we did not rely on internal controls in the areas requiring audit work. Therefore, we focused our efforts on testing the details of each significant account during the second FY 2010 audit engagement. As required by *Government Auditing Standards* for financial statement audits, we will determine during our FY 2011 audit of DOL's consolidated financial statements whether DOL management has taken appropriate corrective action to address the findings and recommendations identified during our FY 2010 audit engagement.

DOL was ultimately able reconcile accounts and record necessary adjusting entries to correct its consolidated financial statement balances. In addition, DOL was able to provide the necessary data for testing and the relevant evidence to support the balances reported in the consolidated financial statements. As a result, we were able to complete our audit procedures, and we issued an updated audit report with an unqualified opinion on DOL's FY 2010 consolidated financial statements on May 20, 2011.

Thank you for the opportunity to discuss the results of these two FY 2010 audit engagements. I would be happy to answer any questions the Subcommittee may have.