



## UNITED STATES RAILROAD RETIREMENT BOARD

OFFICE OF INSPECTOR GENERAL

### AUDITOR'S REPORT

To the Board Members:

We have audited the accompanying consolidated balance sheet of the Railroad Retirement Board (RRB) for the fiscal years ended September 30, 2002 and 2001; and the related: consolidated statements of net cost, changes in net position, and financing; the combined statement of budgetary resources; and the statement of custodial activity (hereinafter referred to as the "principal financial statements") for the years then ended. These financial statements are the responsibility of the RRB's management. Our responsibility is to express an opinion on the principal financial statements based on our audit.

We conducted our audit in accordance with: generally accepted auditing standards; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and, Office of Management and Budget (OMB) Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements." Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the principal financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

#### Opinion on the Financial Statements

In our opinion, the principal financial statements, audited by us and appearing on pages 42 through 59 of this report, present fairly, in all material respects, the financial position of the RRB as of September 30, 2002 and 2001; its consolidated net cost of operations and change in net position; combined budgetary resources; reconciliation of net cost to budgetary resources; and custodial activity for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

#### Emphasis of Matters

As discussed in Note 20, the Railroad Retirement and Survivors' Improvement Act of 2001 (Public Law 107-90) directed the establishment of the National Railroad Retirement Investment Trust (NRRIT). The law directed the RRB to transfer "that portion of the Railroad Retirement Account that is not needed to pay current

administrative expenses” and “the balance of the Social Security Equivalent Benefit Account not needed to pay current benefits and administrative expenses” to the NRRIT. As disclosed in Note 20, the RRB transferred \$1.5 billion to the NRRIT during fiscal year 2002. The transfer of cash to the NRRIT is treated as an outlay; the assets of the NRRIT are not reported as assets on the RRB's consolidated balance sheet.

The RRB's consolidated balance sheet reports total assets of \$22.8 billion as of September 30, 2002. As discussed in Note 20, the agency transferred an additional \$10.25 billion to the NRRIT between October 1, 2002, and January 24, 2003. The amount and timing of future transfers are not available for disclosure at the present time.

As shown on the statement of changes in net position and disclosed in Note 21, transfers-in from the Social Security Administration's Old Age and Survivor, and Disability Insurance trust funds; and transfers-out to the Federal Health Insurance Trust Fund represented \$3.3 billion (net), or approximately 40%, of the \$7.9 billion in total financing sources reported.

#### Consistency of Other Information

Our audit was conducted for the purpose of forming an opinion on the principal financial statements of the RRB taken as a whole. The required supplementary information included on pages 1 through 32, 75 and 79 are not a required part of the principal financial statements. This is supplementary information required by OMB Bulletin 01-09 “Form and Content of Federal Financial Statements,” and/or the Federal Accounting Standards Advisory Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and, accordingly, express no opinion on it.

The required supplementary stewardship information included on pages 81 through 92 is not a required part of the principal financial statements. This is supplementary information required by OMB Bulletin 01-09 “Form and Content of Federal Financial Statements,” and the Federal Accounting Standards Advisory Board. We did not audit and do not express an opinion on such information. However, we have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. As a result of such limited procedures, we have concluded that the statement of social insurance for the Railroad Retirement program does not fully conform to the guidelines established by the Financial Accounting Standards Advisory Board because the demographic groupings do not conform to those specified in the applicable standard and the related narrative presentation over-emphasizes individual program components.

Our audit was conducted for the purpose of forming an opinion on the principal financial statements of the RRB taken as a whole. The supplementary information presented on pages 61 through 74 and 76 through 78 includes supplementary financial data for individual program operations and trust funds as well as consolidating statements. This supplementary information is presented for purposes of additional analysis of the principal financial statements rather than to present the financial position, net cost of operations, changes in net position, budgetary resources and custodial activity of those programs and funds. That information has been subjected to the auditing procedures applied in the audit of the principal financial statements and, in our opinion, is fairly stated in all material respects in relation to the principal financial statements taken as a whole.

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This report is intended solely for the information and use of the management of the RRB, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Martin J. Dickman  
Inspector General

January 24, 2003



## UNITED STATES RAILROAD RETIREMENT BOARD

OFFICE OF INSPECTOR GENERAL

### REPORT ON INTERNAL CONTROL

To The Board Members:

We have audited the accompanying consolidated balance sheet of the Railroad Retirement Board (RRB) for the fiscal years ended September 30, 2002 and 2001; and the related: consolidated statements of net cost, changes in net position, and financing; the combined statement of budgetary resources; and the statement of custodial activity (hereinafter referred to as the "principal financial statements") for the years then ended and have issued our report thereon dated January 24, 2003. We conducted our audit in accordance with: generally accepted auditing standards; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and, Office of Management and Budget (OMB) Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements."

In planning and performing our audit, we considered the RRB's internal control over financial reporting by obtaining an understanding of the agency's internal controls, determining whether these internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the principal financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin 01-02. 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 and, accordingly, we do not express such an opinion.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, 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.

During our audit we noted certain matters involving internal control and its operation that we consider reportable conditions; we have classified two of them as material weaknesses. A discussion of these matters is attached.

Finally, with respect to internal control related to performance measures reported on pages 7 to 19, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions, as required by OMB Bulletin No. 01-02. Our procedures were not designed to provide assurance on internal control over reported performance measures and, accordingly, we do not provide such an opinion.

The conditions discussed in this report were considered in determining the nature, timing, and extent of the audit tests applied during our audit of the fiscal year (FY) 2002 and FY 2001 financial statements. This report does not modify our report on the principal financial statements dated January 24, 2003, referred to in the first paragraph of this report. We have not considered internal control since the date of our report.

This report is intended solely for the information and use of the management of the RRB, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Martin J. Dickman  
Inspector General

January 24, 2003

## **MATERIAL WEAKNESSES**

### Overall Control Environment

The RRB's overall control environment is not adequate to ensure that agency financial statements will be free of material misstatements and prepared in accordance with applicable guidance. As a result, each financial statement audit since FY 1993 has cited the agency for a material weakness in this area.

This weakness in internal control is the result of an organizational structure that does not provide proactive top-down leadership in addressing financial reporting issues. Management in the agency's various operating components does not seek assistance across organizational lines to resolve problems related to financial accounting and reporting. The OIG presented its findings regarding the RRB's overall control environment in OIG audit report # 02-08. Agency management does not agree with the OIG's assessment.

OMB has established a timetable for acceleration of financial statement reporting in the Federal government. The RRB has met previously established deadlines; however, this new timetable, which requires submission of audited financial statements for FY 2004 by November 15, 2004, represents a major challenge to existing agency resources. The OIG believes that the challenge of submitting audited financial statements in accordance with OMB's accelerated timetable will provide a significant test of the effectiveness of the agency's control environment over financial statement preparation and reporting.

Barring any new evidence to the contrary, the OIG will consider successful compliance with accelerated reporting deadlines as evidence of the adequacy of the agency's overall control environment with respect to financial statement reporting only.

### Information System Security

During FYs 2001 and 2002, the OIG conducted evaluations of information security pursuant to the provisions of the Government Information Security Reform Act. Our reviews disclosed weaknesses in most areas of the RRB's information security program. Significant deficiencies in program management and access controls make the agency's information security program a source of material weakness in internal control over financial reporting.

Agency management has begun the process of strengthening information security. However, corrective action has not been sufficient to eliminate the most significant weaknesses. Program management continues to be significantly undermined by a lack of training among key personnel. Access controls cannot be considered fully effective because of the weaknesses in account management in both the mainframe and end-user computing environments. The details of our findings concerning information security were presented to management in OIG audit reports # 02-04, "Review of

Information Security at the RRB”, February 5, 2002; and #02-12, “Fiscal Year 2002 Evaluation of Information Security at the Railroad Retirement Board,” August 27, 2002.

RRB management has reported a material weakness in its information security program in the agency’s annual report on internal control and financial systems issued pursuant to the Federal Managers’ Financial Integrity Act.

## **REPORTABLE CONDITION**

### Accounting for Benefit Overpayment Recoveries

Financial accounting for benefit payments and related accounts receivables are not integrated with the agency’s general ledger. In addition, the automated systems that support benefit payment operations account directly only for cash disbursed. Payments withheld in satisfaction of outstanding debt are accounted for indirectly through other systems.

The OIG performed a review of internal control over financial accounting for debt recoveries and reported our findings in OIG audit report #00-16 dated September 29, 2000. During that review, we identified errors in the recording of debt recovery transactions that included: returned benefit payments that were not credited to debtor accounts; benefit payments that had been erroneously credited to debtor accounts as recoveries; and delayed recording of certain Railroad Unemployment Insurance Act debt recoveries.

An examination of the related internal controls disclosed that the present control structure does not provide for the review and reconciliation of general ledger controlling accounts for benefit payments; does not include reviews of all systems output; and is inadequate to prevent the recording of unauthorized, unsupported transactions. In addition, the present internal control environment does not provide management with sufficient information concerning the number and value of non-conforming transactions to provide the basis for an evaluation of potential financial impact.

The OIG’s review of accounts receivable at September 30, 2001, OIG audit report #02-10, disclosed additional weaknesses including an automated process that recognizes some debts prematurely and establishes erroneous receivables in some cases. We also noted that the several automated systems that support Railroad Retirement Act benefit payment operations do not provide complete, consistent information about returned, reclaimed and cancelled benefit payments.

Agency management has implemented some of the OIG’s recommendations for corrective action. However, they have not taken the recommended action in several key areas, including the implementation of controlling accounts for benefit payments, citing the inability of existing benefit payment sub-systems to support a cost-effective control and reconciliation process.



## UNITED STATES RAILROAD RETIREMENT BOARD

OFFICE OF INSPECTOR GENERAL

### REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

To The Board Members:

We have audited the accompanying consolidated balance sheet of the Railroad Retirement Board (RRB) for the fiscal years ended September 30, 2002 and 2001; and the related: consolidated statements of net cost, changes in net position, and financing; the combined statement of budgetary resources; and the statement of custodial activity (hereinafter referred to as the "principal financial statements") for the years then ended and have issued our report thereon dated January 24, 2003. We conducted our audit in accordance with: generally accepted auditing standards; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and, Office of Management and Budget (OMB) Bulletin No. 01-02, "Audit Requirements for Federal Financial Statements."

The management of the RRB is responsible for complying with laws and regulations applicable to the agency. As part of obtaining reasonable assurance about whether the agency's principal financial statements are 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 financial statement amounts, and certain other laws and regulations specified in OMB Bulletin 01-02. We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to the RRB.

The results of our tests of compliance with laws and regulations, as described in the preceding paragraph, disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards or OMB Bulletin 01-02.

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 does not modify our report dated January 24, 2003, on the RRB's principal financial statements referred to in the first paragraph of this report.

This report is intended solely for the information and use of the management of the RRB, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Martin J. Dickman  
Inspector General

January 24, 2003