

U.S. ELECTION ASSISTANCE COMMISSION OFFICE OF INSPECTOR GENERAL



Management Letter:

Issues Identified During the Audit of the U.S. Election Assistance Commission's Fiscal Year 2008 Financial Statements

**No. I-PA-EAC-01-08(A)
MARCH 2009**



U.S. ELECTION ASSISTANCE COMMISSION
OFFICE OF INSPECTOR GENERAL
1225 New York Ave. NW - Suite 1100
Washington, DC 20005

March 31, 2009

To: Gineen B. Beach
Chair, U.S. Election Assistance Commission

From: Curtis W. Crider *Curtis W. Crider*
Inspector General

Subject: Management Issues Identified During the Audit of the U.S. Election Assistance Commission's Fiscal Year 2008 Financial Statements
(Assignment No. I-PA-EAC-01-08(A))

We contracted with Clifton Gunderson LLP (Clifton Gunderson), an independent certified public accounting firm, to audit the U.S. Election Assistance Commission's (Commission) financial statements as of September 30, 2008 and for the year then ended. In conjunction with its audit, Clifton Gunderson noted certain matters involving internal control and other operational matters that should be brought to management's attention. These matters, which are discussed in the attached letter, are in addition to those reported in Clifton Gunderson's audit report on the Commission's financial statements (Assignment No. I-PA-EAC-01-08) and do not constitute significant deficiencies as defined by the American Institute of Certified Public Accountants.

Based on the information provided in the February 20, 2009 response to the draft management letter, we consider all of the suggestions implemented. The Office of Inspector General will follow-up on the suggestions as a part of the Fiscal Year 2009 financial statement audit.

The Inspector General Act of 1978, as amended, requires semiannual reporting to Congress on all reports issued, actions taken to implement recommendations, and recommendations that have not been implemented. Therefore, we will include the information in the attachment in our next semiannual report to Congress. The distribution of this report is not restricted, and copies are available for public inspection.

We appreciate the cooperation and assistance of EAC personnel during the audit. If you or your staff has any questions, please contact me at (202) 566-3125.

Attachment

Cc: Commissioners Hillman, Davidson
Executive Director
Chief Operating Officer
Chief Financial Officer

November 7, 2008

To the Executive Director
To the Inspector General
Election Assistance Commission
Washington, DC

We were engaged to audit the financial statements of the Election Assistance Commission (EAC) as of and for the year ended September 30, 2008, and have issued our reports dated November 7, 2008, which included reports on internal control and compliance with laws and regulations. During the course of the engagement, we noted certain matters which we would like to bring to your attention related to internal control and operations at the EAC that are not considered "Significant Deficiencies" as defined by the standards issued by the American Institute of Certified Public Accountants, but are important to the overall internal control structure of the EAC. Therefore, we offer the following observations and suggestions which are intended to improve internal control and operational effectiveness at the EAC.

I. Management Representation Letter

Observation: The management representation letter serves to document representations explicitly or implicitly made by management in response to the auditors' specific inquiries or through the financial statements. Management's representations complement the auditors' other audit procedures and are an essential component of the audit evidence the auditor needs to afford a reasonable basis for an opinion regarding the financial statements under audit. The evidentiary value of the management representation letter is of such significance that a failure to obtain written representations precludes the auditor from issuing an unqualified opinion and will usually cause the auditor to disclaim an opinion.¹ In addition, *Generally Accepted Auditing Standards* (GAAS) considers management representations to be of such importance that GAAS requires auditors to consider whether reliance on all of management's representations is appropriate and justified if any of the representations made are contradicted by other audit evidence.

We made the following observations regarding the representations made by EAC's management:

- The representation letter was signed by a consultant in addition to management. The GAO/PCIE *Financial Audit Manual* Section 1001.04 states, "The auditor should obtain the management representation letter from the highest level of the audited entity." FAM 1001.04 further states, "Signers should be officials who are responsible for and knowledgeable, directly or through others, about the matters in the representation letter. These officials generally should be the head of the federal entity and the CFO, or equivalent."

¹ AU Section 333, *Management Representations*, paragraph .13

- The representations did not include the possible non-compliance with the Anti-deficiency Act related to transactions charged against the Election Reforms Payments (ERP) Fund that EAC is investigating. AU §333.06 states, “In connection with an audit of financial statements presented in accordance with generally accepted accounting principles, specific representations should related to....Violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis...”
- Management represented that to the best of their knowledge and belief that the financial statements are fairly presented in conformity with U.S. generally accepted accounting principles. Although we could not determine whether EAC’s financial statements are fairly presented, we noted several control deficiencies that raise doubts as to their fair presentation. These deficiencies are discussed in detail in our *Independent Auditor’s Report on Internal Control over Financial Reporting*.

Suggestions:

- We suggest that management ensures the representations it makes to auditors are not contradictory with other information in EAC’s reports or to information provided during the audit.
- We suggest that only members of EAC management who are responsible for and knowledgeable, directly or through others, about the matters in the representation letter sign the management representation letter.
- We suggest that EAC provide appropriate representations regarding any possible violation of the Anti-deficiency Act that it identifies in future representation letters.
- EAC management informed CG it plans to hire an experienced Federal financial manager to serve as the Chief Financial Officer of the EAC. AU §333.10 requires auditors to obtain representations from management for the entire period under audit even if current management was not present during all periods covered under the auditor’s report. We suggest that EAC take the necessary steps to provide its CFO, when hired, the information necessary to be able to make the required representations to the auditors.

II. Implementation of Financial Reporting and Performance and Accountability Requirements

Observation: FY08 was the first year in EAC's five-year history that the agency was subject to the requirements of the Office and Management and Budget (OMB) Circular A-136 *Financial Reporting Requirements*. In its response to our reports EAC management recognized the challenge it faced in producing auditable financial statements during its first audit and acknowledged improvements are necessary to its internal control structure in order to meet the requirements of OMB A-136. EAC outlined key aspects of its improvement plan in its response to our report which included the following "next steps:"

- Hire a Chief Financial Officer,
- Evaluate the existing accounting system and correct accounting data,
- Restructure accounting operations; and
- Implement performance-based budgeting.

Suggestion: As EAC executes these next steps and continues to refine its improvement plan we suggest that EAC management consider utilizing the following "best practices" guides produced by the Government Accountability Office (GAO):

- *Executive Guide: Creating Value Through World-class Financial Management*, April 2000, GAO/AIMD-00-134, and
- *Executive Guide: Effectively Implementing the Government Performance and Results Act*, June 1996, GAO/GGD-96-118
- *2010-Checklist for Federal Accounting*
- *2020-Checklist for Federal Reporting*

III. Payroll

Observation: Supervisory authorization and approval is a key internal control for ensuring the propriety of Time and Attendance (T&A) information. The GAO's *Maintaining Effective Control over Employee Time and Attendance Reporting* states "the supervisor has primary responsibility for authorizing and approving T&A transactions. To help ensure proper recording of T&A information, completed T&A records should be reviewed and approved by the supervisor or other equivalent official." Timecards submitted to EAC's payroll service provider are not approved by the supervisor.

Suggestion: EAC management should revise current policy to require timecards be approved by the official, normally the immediate supervisor, most knowledgeable of the time worked by and absence of the employee involved. Approval of the document should be based on personal observation, work output or similar activities.

AUDITOR'S EVALUATION OF EAC MANAGEMENT'S RESPONSE

In commenting on a draft of this report (Exhibit 1), EAC management disagrees with the observation related to the management representation letter but agrees with the observations and suggestions related to the implementation of financial reporting and accountability requirements and the payroll.

We agree with EAC management that the appropriate EAC officials signed the management representation letter. Our observation highlighting the additional consultant's signature on the management representation letter is for the purpose of communicating to EAC management that internal control is management's responsibility and the financial statements are management's representation. We also would like to state that the auditor provided a management representation template and communicated to EAC management the officials that we identified as appropriate signatories.

We disagree with EAC management's response on the observation related to the non-representation of the possible non-compliance with the Anti-Deficiency Act. It is management's responsibility, not the auditors, to determine violation of the Anti-Deficiency Act. EAC management could not provide adequate, complete, and appropriate documentation to enable the auditor to perform the procedures necessary to propose an audit adjustment, if necessary.

We also disagree with EAC management's response on the observation related to management representation on the fair presentation of the financial statements. Internal control, as defined in the GAO's *Standards for Internal Control for the Federal Government*, is an integral component of an organization's management that provides reasonable assurance of the reliability of financial reporting [underlined for emphasis]. In response to the Independent Auditor's Report on Internal Control over Financial Reporting, EAC management stated that "The EAC recognized that it would be a challenge for the agency to produce auditable financial statements this year."

This letter is intended solely for the information and use of management of the EAC, the Inspector General of the EAC, the Office of Management and Budget and Congress and is not intended to be and should not be used by anyone other than these specified parties.



Calverton, Maryland
November 7, 2008

EXHIBIT 1 – ELECTION ASSISTANCE COMMISSION MANAGEMENT’S RESPONSE

**See Auditor’s Evaluation of Election Assistance Commission Management’s Response
on page 4 of the Management Letter**



U.S. ELECTION ASSISTANCE COMMISSION
1225 New York Ave. NW – Suite 1100
Washington, DC 20005

February 20, 2009

To: Curtis W. Crider
Inspector General

From: Gineen Bresso Beach 
Chair, U.S. Election Assistance Commission

Subject: Draft Management Letter

In response to your letter, dated February 4, 2009, regarding the report findings and recommendations of the Clifton Gunderson, LLP (Clifton Gunderson) audit of the U.S. Election Assistance Commission (EAC), we are providing comments and responses. As requested, the comments indicate whether or not EAC Management agrees or disagrees with the comment. Also, basis and support for disagreements are included.

It is the hope of the EAC that the final management letter will benefit from this reply. If you have any questions, please contact Alice Miller, our Chief Operating Officer, at (202) 566-3110 or Annette Lafferty, our Chief Operating Officer, at (202) 566-0355.

Attachment

CC: Commissioners Davidson, Hillman, Rodriguez
Tom Wilkey, Executive Director
Alice Miller, Chief Operating Officer
Annette Lafferty, Chief Financial Officer

I. Management Representation Letter

Comment

“The representation letter was signed by a consultant in addition to management. The GAO/PCIE *Financial Audit Manual* Section 1001.04 states “The auditor should obtain the management representation letter from the highest level of the audited entity.” FAM 1001.04 further states, “Signers should be officials who...are responsible for and knowledgeable, directly or through others, about the matters in the representation letter. These officials generally should be the head of the federal entity and the CFO, or equivalent.”

Response

The representation letter was signed by officials who are responsible for and directly through others and about the matters in the representation letter. Those officials included the agency Commission Chair and the Chief Executive Officer. The GAO Audit manual states:

- The auditor should obtain the management representation letter from the highest level of the audited entity. The auditor should decide who to ask to sign the management representation letter. Signers should be officials who, in the auditor’s view, are responsible for and knowledgeable, directly or through others, about the matters in the representation letter. These officials generally should be the head of the federal entity and the CFO, or equivalent.

It is clearly the responsibility of the auditor to make the determination of who should sign the letter. To our knowledge, no such written direction was given. Additionally, the guidance, does not indicate who should not sign the letter, only who should. The consultant had been required by auditors of another client in a similar situation to sign the management letter. He discussed management’s decision to include him as a signer verbally with Clifton Gunderson’s auditors on the week of November 10, 2008 and no objection was raised by Clifton Gunderson at that point.

Considering the Consultant’s significant level of involvement in the financial statement preparation it is his professional opinion that it is both proper and necessary for him to have signed the letter. Accordingly, we disagree with this finding.

With regards to future management letters, management suggests that the auditors clearly designate who should sign the letter, and approve the list of signers before the process is completed.

Comment

The representations did not include the possible non-compliance with the Anti-deficiency Act related to transactions charged against the Election Reforms Payments (ERP) Fund that EAC is investigating. AU §333.06 states, “In connection with an audit of financial statements presented in accordance with generally accepted accounting principles, specific representations should related to...Violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis...”

Response

The full text of the AU §333.06 citation is as follows:

- “Violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency”.

The relevance and importance of this section has to do with the impact of the effects of the possible violation either in the financial statements themselves, notes to the financial statements or both. The matter identified to the auditors by the IG as a potential violation of the Anti-Deficiency act was clearly known to the auditors. Management responded to this issue during the audit by maintaining it would conduct a reconstruction of the books necessary to evaluate what impact (effects) if any, the matter had on the financial statements. On November 7, 2008, the consultant sent an email to the Clifton Gunderson's Chief Auditor asking her to identify all adjusting entries:

Consultant's email:

Attached is a recomputation of the amount indicated in PBC 605 as of 6/30/08 plus a similar calculation for 9/30/08. Based on the recalculation, we do not believe an adjustment is required to the financial statements for \$49,220.68.

As management representations are somewhat dependent on whether or not CG has proposed audit adjustments, EAC needs your response to this and any other proposed adjustments in order to respond in a complete and accurate way in the management letter.

Accordingly, please indicate in your response, all outstanding audit adjustments which CG has proposed. EAC would like this information COB today in order to evaluate the entries and to allow us to comply with the 11/9/08 management letter delivery deadline.

Thanks,
(consultant)

Auditor's Response
[Consultant]

Just wanted to let you know that I've received your email. I'm unable to review the analysis right now but will get back to you as soon as I can.

Thanks,
[Auditor]

EAC Consultant received no additional response from Clifton Gunderson's Auditors to whom the email was forwarded .

The relevance of this to the matter at hand is that there was no loss contingency adjustment proposed by the auditors which should have been included on the financial statements. With regard to any disclosure of the item on the financial statements, this too was not identified as a deficiency or required disclosure during specific review and comments submitted by the auditor on November 7.

Furthermore, the audit standard requires the "effects" be considered in the financial statements or notes. We cannot adjust the financial statements if we cannot discern the effects, if any. Any disclosure would have the potential of being misleading.

In practice, the preparation and signature of the management representation letter is usually a much more corroborative effort between the auditor and the client. It is the auditor's responsibility to obtain the representations they feel are necessary in the circumstances:

From the GAO FAM Section 1001.03:

"The specific representations obtained will depend on the circumstances of the engagement and the nature and basis of presentation of the financial statements. These representations apply to all the financial statements and all periods covered by the audit report. In addition to the representations in the AICPA standards, the auditor generally should determine the need to obtain representations on other matters based on the circumstances of the audited entity. Also, the auditor should delete inapplicable representations in the example representation letter in FAM 1001 A and should customize the letter to the situation of the entity being audited."

From GAO FAM Section 1001.10

"The auditor should determine the need for additional customizing of the example representation letter in FAM 1001 A and for the additional representations in FAM 1001.09. Many of the representations may have to be qualified, especially in an initial audit or in later audits where significant problems remain. For instance, where the example representation letter states that there are no violations of laws or regulations, the entity may need to add at the end of the statement, "except as follows:" and describe the violations."

In our opinion, there was a lack of guidance by Clifton Gunderson in obtaining the required management representations. We disagree with their characterization of this issue and vigorously maintain that the representations are proper.

In the future, management will be aware of the process required by the GAO FAM, and insist that the auditors provide an applicable sample letter for review and signature. Any discrepancies should be resolved prior to signing the letter so that the representations made are what are both expected and required.

Comment

"Management represented that to the best of their knowledge and belief that the financial statements are fairly presented in conformity with U.S. generally accepted accounting principles. Although we could not determine whether EAC's financial statements are fairly presented, we noted several control deficiencies that raise doubts as to their fair presentation. These deficiencies are discussed in detail in our *Independent Auditor's Report on Internal Control over Financial Reporting*."

Response

Financial statements can be in conformity with GAAP even though internal control weaknesses may exist. The question is whether the nature of the internal control weaknesses would prevent management from making the representation that "...to the best of their knowledge..." the financial statements were fairly presented. The internal control issues identified by the auditors which may have an impact on the financial statements have to do with accounting related issues. As indicated above, the auditors did not propose any adjusting entries. Furthermore, they were unable to quantify the impact (if any) of the accounting issues. To our knowledge, they did not modify the language in a sample management letter to revise the language as

required by the audit standards. Accordingly, we disagree with this comment and maintain that the representations were proper.

Comment

EAC management informed CG it plans to hire an experienced Federal financial manager to serve as the Chief Financial Officer of the EAC. AU §333.10 requires auditors to obtain representations from management for the entire period under audit even if current management was not present during all periods covered under the auditor's report. We suggest that EAC take the necessary steps to provide its CFO, when hired, the information necessary to be able to make the required representations to the auditors.

Response

EAC management agrees with this comment and will take the necessary steps to make the required representations to the auditors.

II. Implementation of Financial Reporting and Performance and Accountability Requirements

Comments

As EAC executes these next steps and continues to refine its improvement plan we suggest that EAC management consider utilizing the following "best practices" guides produced by the Government Accountability Office:

- *Executive Guide: Creating Value Through World-class Financial Management*, April 2000, GAO/AIMD-00-134, and
- *Executive Guide: Effectively Implementing the Government Performance and Results Act*, June 1996, GAO/GGD-96-118
- *2010- Checklist for Federal Accounting*
- *2020-Checklist for Federal Reporting*

Response

EAC is in agreement with the recommendation and will consider utilizing the above referenced "best practices" guides.

III. Payroll

Comment

EAC management should revise current policy to require timecards be approved by the official, normally the immediate supervisor, most knowledgeable of the time worked by and absence of the employee involved. Approval of the document should be based on personal observation, work output or similar activities.

Response

EAC agrees with this comment and will consider the best way to implement this recommendation in connection with its overall financial management improvement plan.

OIG's Mission

The OIG audit mission is to provide timely, high-quality professional products and services that are useful to OIG's clients. OIG seeks to provide value through its work, which is designed to enhance the economy, efficiency, and effectiveness in EAC operations so they work better and cost less in the context of today's declining resources. OIG also seeks to detect and prevent fraud, waste, abuse, and mismanagement in these programs and operations. Products and services include traditional financial and performance audits, contract and grant audits, information systems audits, and evaluations.

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1225 New York Ave. NW - Suite 1100
Washington, DC 20005

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Office of Inspector General
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E-mail: eacoig@eac.gov

OIG Hotline: 866-552-0004 (toll free)

FAX: 202-566-0957

