The U.S. International Trade Commission is an independent, nonpartisan, quasi-judicial federal agency that provides trade expertise to both the legislative and executive branches of government, determines the impact of imports on U.S. industries, and directs actions against certain unfair trade practices, such as patent, trademark, and copyright infringement. USITC analysts and economists investigate and publish reports on U.S. industries and the global trends that affect them. The agency also maintains and publishes the Harmonized Tariff Schedule of the United States.

Commissioners

Deanna Tanner Okun, Chairman
Irving A. Williamson, Vice Chairman
Charlotte R. Lane
Daniel R. Pearson
Shara L. Aranoff
Dean A. Pinkert
Chairman Okun:

This memorandum transmits the Independent Auditor’s Report on Internal Controls (OIG-AR-11-03) associated with the audit the Commission’s financial statements for fiscal year 2010. We contracted with the independent certified public accounting firm, Castro & Company LLC, to conduct this audit. The contract required that the audit be conducted in accordance with U.S. generally accepted government auditing standards. These standards require a Report on Internal Control.

My office has policies and procedures that are designed to provide assurance that work performed by non-Federal auditors complies with U.S. generally accepted government auditing standards. These procedures follow the guidelines provided in the GAO/PCIE Financial Audit Manual (FAM650). In connection with this contract, we reviewed Castro & Company’s report and related documentation and made inquiries of its representatives. Our involvement in the audit process consisted of monitoring audit activities; reviewing auditor independence and qualifications; attending meetings; participating in discussions; and reviewing audit planning, working papers, conclusions, and results. Our review disclosed no instances where Castro & Company did not comply, in all material respects, with U.S. generally accepted government auditing standards. However, our review cannot be construed as an audit in accordance with the U.S. generally accepted government auditing standards. It was not intended to enable us to express, and we do not express, any opinion on the effectiveness of the Commission’s internal controls. Castro & Company is solely responsible for the audit report dated November 8, 2010 and the conclusions expressed in the report.

Castro & Company’s report contains twenty recommendations for corrective action. In the next 30 days, please provide me with your management decisions describing the specific actions that you will take to implement each recommendation.

Thank you for the cooperation and courtesies extended to both Castro & Company and my staff during this audit.

Sincerely,

Philip M. Heneghan
Inspector General
Independent Auditor’s Report on Internal Control

Inspector General
U.S. International Trade Commission

We have audited the financial statements of the U.S. International Trade Commission (ITC) as of and for the year ended September 30, 2010, and have issued our report thereon dated November 8, 2010. The report states except for undelivered orders and other related accounts discussed therein, we expressed an opinion on the balance sheet as of September 30, 2010, and the related statements of net cost, changes in net position, and budgetary resources for the fiscal year then ended.

In planning and performing our work, we considered ITC's internal control over financial reporting by obtaining an understanding of the design effectiveness of ITC's internal control, determining whether controls had been placed in operation, assessing control risk, and performing tests of ITC's controls as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not to express an opinion on the effectiveness of ITC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of ITC's internal control over financial reporting. We limited our internal control testing to those controls necessary to achieve the objectives described in the Office of Management and Budget (OMB) Bulletin No. 07-04, Audit Requirements for Federal Financial Statements, as amended. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to ensuring efficient operations.

Our consideration of internal control over financial reporting was for the limited purposes described in the preceding paragraphs and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a deficiency in internal control, or a combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles (GAAP) such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected.

A material weakness is a significant deficiency, or combination of significant deficiencies, that result in a more than remote likelihood that a material misstatement of the financial statements will not be prevented or detected.
Our consideration of the internal control over financial reporting was for the limited purpose described above and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we also consider the first four deficiencies described below to be material weaknesses.

We also noted less significant matters involving internal control and its operations which we have reported to ITC management in a separate letter dated November 8, 2010.

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

November 8, 2010
Alexandria, VA
MATERIAL WEAKNESSES

I. Inadequate Internal Controls over Financial Reporting (Repeat Condition)

The Accountability of Tax Dollars Act of 2002 (ATDA) extends to ITC the requirement to submit to Congress and the Director of OMB audited financial statements. OMB Circular No. A-136, *Financial Reporting Requirements*, defines the form and content of financial statements to be prepared by the Commission. To accomplish the objective of complying with the ATDA, the agency is required to develop a system to prepare a complete set of financial statements on a timely basis in accordance with U.S. generally accepted accounting principles. The statements are to result from an accounting system that is an integral part of an integrated financial management system containing sufficient structure, effective internal control and reliable data. Financial reporting also consists of policies and procedures related to the processing and summarizing of accounting entries, and the preparation of financial statements.

During testing of ITC’s financial statements preparation, we noted that improvement is needed to ensure that ITC can accurately produce its quarterly financial statements and perform related analyses. The errors we noted related to incorrect accumulation of account balances, incorrect identification of general ledger accounts, and incorrect postings to the financial reporting system. As a result, management provided several versions of the September 30, 2010 trial balance, along with seven different versions of financial statements and related notes, with the latest version provided on November 2, 2010. Each version provided consistently reflected significant errors. These errors occurred because of ineffective management reviews and approvals to ensure that transactions and adjustments were accurate and properly supported. However, ITC made the necessary corrections to the final issued financial statements.

A major objective of internal control is to ensure the integrity of the underlying accounting data supporting the financial statements. A key control is performing reconciliations of significant account balances. An adequate reconciliation provides assurances that transactions are properly processed and recorded in the accounting records in a timely manner. Management indicated that reconciliations of material financial statement line items were not performed on a routine basis.

During our review of ITC's financial statement preparation process, we identified certain issues, as summarized below, impacting ITC's ability to effectively accumulate, assemble, and analyze information presented in its financial statements in accordance with applicable guidance. Specifically, we noted the following:

- A significant number of transactions were processed through the use of manual journal vouchers, which were not adequately reviewed or did not contain sufficient detail to support the reason for the manual journal voucher. Although manual journal vouchers in and of themselves are not considered an issue, they do increase the risk for errors.

- The financial statements included accounts that should not have been reported on the face of the financial statements (e.g., Fiduciary Assets) as outlined by the accounting standards.
The Notes to the financial statements did not include certain disclosures required by OMB Circular No. A-136.

Numerous numerical errors and typographical errors were included throughout the financial statements.

OMB Circular No. A-123, *Management’s Responsibility for Internal Control* states:

Management has a fundamental responsibility to develop and maintain effective internal control. Federal employees must ensure that Federal programs operate and Federal resources are used efficiently and effectively to achieve desired objectives. Programs must operate and resources must be used consistent with agency missions, in compliance with laws and regulations, and with minimal potential for waste, fraud, and mismanagement.

Effective internal control provides assurance that significant weaknesses in the design or operation of internal control, that could adversely affect the Commission’s ability to meet its objectives, would be prevented or detected in a timely manner. However, based on the issues noted above, ITC management needs to strengthen its internal control surrounding financial management to ensure compliance with applicable laws and regulations throughout the year.

**Recommendations**

We recommend that ITC management:

1. Develop an accounting manual documenting the procedures needed to ensure ITC complies with applicable accounting, financial management and reporting standards and regulations.

2. Review its organizational structure to ensure financial management is adequately staffed with individuals that possess current experience in compiling Federal financial statements.

3. Provide training to financial management personnel on federal accounting and reporting requirements to enhance ITC’s ability to compile financial statements and the Performance and Accountability Report in accordance with applicable standards.

**II. Insufficient Monitoring, Analysis and Oversight of Financial Operations**

ITC does not have adequate policies or procedures, including an accounting manual, in place to sufficiently monitor, analyze, oversee and reconcile its financial operations. During our testing, we noted the following:

- Key management reports (e.g., status of funds/budget execution, open obligations, etc.) were not provided to program managers on a regular basis for review and analysis.
Reconciliations between the subsidiary listings and the general ledger on key financial accounts were not performed on a regular basis.

Development of ITC’s operating budget was hampered by the lack of actual expense information from prior years. The lack of such data limited ITC’s ability to critically evaluate whether current budget amounts are reflective of the Commission’s needs, and undermined management’s allocation of funds among programs.

ITC did not fully comply with the Government Accountability Office (GAO) *Principles of Federal Appropriations Law*, Chapter 4, Section J (pages 271 – 274). In addition, ITC’s Transit Benefit program provides a parking subsidy to its employees, which is inconsistent with the requirements of 5 U.S.C. Section 7905, *Programs to encourage commuting by means other than single-occupancy motor vehicles*, Executive Order 13150, *Federal Workforce Transportation*. We also noted this to be an instance of noncompliance in the Independent Auditor’s Report on Compliance with Laws and Regulations, dated November 8, 2010.

**Recommendations:**

We recommend that ITC management:

4. Identify key management reports needed to enhance ITC’s ability to effectively and efficiently manage its operations.
5. Develop and document procedures to assist management in monitoring, analyzing, overseeing, and reconciling financial data; thereby strengthening internal controls and encouraging a more collaborative management environment.

6. Train employees on how to generate and analyze management reports to ensure there is a comprehensive understanding of management’s role and responsibilities surrounding the monitoring and analysis of financial information.

III. Inadequate Controls over Undelivered Orders (i.e., Open Obligations) Accounts Payable, and Expenditures (Repeat Condition)

During our testing, we noted several issues surrounding the accounting for open obligations, accounts payable, and expenditures as summarized below:

- ITC maintained inadequate accounting records to sufficiently support open obligations. We noted several open obligations which were unsupported or invalid as of September 30, 2010. ITC attempted to correct the balance by posting an adjustment in the amount of $1.2 million to reduce its open obligations for invalid obligations. However, the projected error of the unsupported and invalid open obligations indicated that the balance was materially overstated and could not be relied upon for financial reporting purposes.

- A routine and consistent review of obligations was not performed on a regular basis to ensure that obligations incurred were valid as of September 30, 2010.

- ITC does not have any formal policy or procedures specific to its accrual methodology for accounts payable.

- ITC does not perform a sufficient review and analysis of its expenditures to determine if payments are properly supported, classified, or reported in the proper period. Specifically, several expenditures were recorded in FY 2010 that related to the prior year.

- Management was unable to provide subsidiary ledgers for open obligations and accounts payable in a timely manner.

GAO’s Standards for Internal Control in the Federal Government states:

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Internal control and all transactions and other significant events need to be clearly documented, and the documentation should be readily available for examination. The documentation should appear in management directives, administrative policies, or operating manuals and may be in paper or electronic form. All documentation and records should be properly managed and maintained.
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The Statement of Federal Financial Accounting Standards (SFFAS) No. 1, *Accounting for Selected Assets and Liabilities* states:

Accounts payable are amounts owed by a Federal entity for goods and services received from, progress in contract performance made by, and rents due to other entities…When an entity accepts title to goods, whether the goods are delivered or in transit, the entity should recognize a liability for the unpaid amount of the goods. If invoices for those goods are not available when financial statements are prepared, the amounts owed should be estimated.

Section I.A. of OMB Circular No. A-123, states:

The control environment is the organizational structure and culture created by management and employees to sustain organizational support for effective internal control. When designing, evaluating or modifying the organizational structure, management must clearly demonstrate its commitment to competence in the workplace. Within the organizational structure, management must clearly: define areas of authority and responsibility; appropriately delegate the authority and responsibility throughout the agency; establish a suitable hierarchy for reporting; support appropriate human capital policies for hiring, training, evaluating, counseling, advancing, compensating and disciplining personnel; and uphold the need for personnel to possess and maintain the proper knowledge and skills to perform their assigned duties as well as understand the importance of maintaining effective internal control within the organization.

By not performing a review of open obligations, expenditures, and accounts payable on a routine basis, financial data used to generate management reports or financial reports required by applicable laws and regulations may be over or understated. As noted above, the projected error related to open obligations indicated that the balance was materially overstated as of September 30, 2010 and could not be relied upon for financial reporting purposes.

**Recommendations:**

We recommend that ITC management:

7. Establish policies for monitoring obligations, operating expenses, and related accounts payable on a routine basis.

8. Document procedures to implement the policies.

9. Train responsible personnel on how to monitor obligations, operating expenses, and accounts payable to enhance compliance with the applicable requirements.

10. Perform a data clean–up for all open obligations and accounts payable documents to ensure that the balances are properly reported, with appropriate adjustments posted at the detailed general ledger level.
IV. Insufficient Resources and Personnel with Appropriate Skill Sets

ITC did not have adequate resources and personnel with appropriate skill sets and expertise to perform financial management accounting and reporting. Furthermore, ITC has not developed a program to cross train finance personnel in performing day-to-day financial management accounting and financial reporting tasks. For example, the Director of Finance performs the majority of the accounting and reporting responsibilities, which prevents an adequate review and approval process of the financial reporting process.

To address previously identified internal control weaknesses, ITC augmented its staffing through the use of consultants to assist in performing its financial management operations. As a result of these efforts, ITC was able to improve its financial reporting accordingly. However, we noted that ITC placed significant reliance on the consultants for financial management expertise. Although the reliance on consultants may be necessary, in the short-term, to expedite the resolution of the weaknesses identified, ITC needs to ensure that it has the skills and expertise on staff going-forward.

In addition, the Director of Administration had to take on additional responsibilities for information systems, contracting, and facilities management because ITC encountered turnover in these positions throughout the fiscal year. As a result, the quality assurance procedures surrounding the financial reporting environment were adversely affected.

The lack of resources was aggravated by the conversion of the financial system in FY 2009. Specifically, ITC did not have a systems accountant on staff with the expertise of the accounting system. Accordingly, an understanding of the system’s key processes did not exist, which impeded ITC’s ability to process accounting transactions accurately and generate financial data and reports in a consistent or timely manner.

GAO’s Standards for Internal Control in the Federal Government states:

People are what make internal control work. The responsibility for good internal controls rests with all managers. Management sets the objectives, puts the control mechanisms and activities in place, and monitors and evaluates the control. However, all personnel in the organization play important roles in making it happen. All personnel need to possess and maintain a level of competence that allows them to accomplish their assigned duties, as well as understand the importance of developing and implementing good internal control. Management needs to identify appropriate knowledge and skills needed for various jobs and provide needed training, as well as candid and constructive counseling, and performance appraisals.

The need for employees with analytical and federal accounting and reporting competencies will only increase as ITC further integrates its financial management system. Without the adequate staffing levels and the proper skill sets, the ITC will continue to encounter challenges in the financial reporting process including preparing reliable financial reports in a timely manner, and consistent with applicable laws and regulations.
**Recommendations:**

We recommend that ITC management:

11. Perform an assessment of current finance staff to ensure that the individuals possess analytical, federal accounting and financial reporting knowledge and experience to enhance the ITC’s ability to comply with accounting and financial reporting standards.

12. Evaluate the resources and appropriate skills needed throughout the agency to meet ITC’s financial management and reporting responsibilities and implement a plan on achieving the results and recommendations of the evaluation.

13. Provide on-going training to ITC employees on federal accounting and reporting requirements, including training on the accounting service provider’s financial system.

**SIGNIFICANT DEFICIENCIES**

V. Inadequate Controls Surrounding the Identification, Recording, and Reporting of Property, Plant and Equipment (Repeat Condition)

We noted that ITC made significant improvements over the prior fiscal year surrounding the documentation maintained to support balances of property, plant and equipment (PP&E) recorded in the financial statements. However, we noted that ITC did not have sufficient policies or procedures in place throughout the majority of the current fiscal year to account for PP&E in accordance with applicable accounting standards. Specifically, ITC did not:

- Maintain adequate documentation to support the acquisition cost, useful life and in-service date for the majority of the assets recorded by ITC during the first six months of the fiscal year. As a result, ITC had to perform an in-depth review and clean up of its PP&E balances and previously expensed transactions throughout the fiscal year in order to properly state PP&E balances as of September 30th. This effort entailed reviewing all assets acquired since FY 2005 and verifying whether the asset should be capitalized or expensed in accordance with applicable accounting standards. The fact that the Commission was able to accomplish this task in a matter of months is a credit to the Commission.

As a result of the clean-up efforts from June through September of the current fiscal year, ITC identified and recorded an increase of approximately $3.5 million to PP&E, resulting in a net increase of 115 percent from the PP&E reported in the prior fiscal year. Of this net increase, approximately $3.1 million related to assets which should have been recognized in prior fiscal years; therefore, ITC had to record a prior period adjustment for FY 2009 to recognize the asset’s costs and related depreciation.
• Establish a reimbursable work authorization upfront with the General Services Administration (GSA) to effectively and properly capture leasehold improvements associated with the second floor build-out.

• Clearly document the transactions associated with the prior period adjustment for the restatement of PP&E from expenses to capitalized equipment.

ITC did not have written policies and procedures in place for the majority of the fiscal year to adequately monitor purchases to ensure expenditures were properly expensed or capitalized in accordance with applicable accounting standards.

OMB Circular No. A-123, states:

Management has a fundamental responsibility to develop and maintain effective internal control. Programs must operate and resources must be used consistent with agency missions, in compliance with laws and regulations, and with minimal potential for waste, fraud, and mismanagement. Internal control should be designed to provide reasonable assurance regarding prevention of or prompt detection of unauthorized acquisition, use or disposition of assets.

Section II.4.3.3 of OMB Circular No. A-136, Financial Reporting Requirements, outlines the FASAB standards applicable to the financial reporting of PP&E to include: SFFAS No. 6, Accounting for Property, Plant, and Equipment, SFFAS No. 11, Amendments to Accounting for Property, Plant, and Equipment-Definitional Changes-Amending SFFAS 6 and SFFAS No. 35, Estimating the Historical Cost of General Property, Plant, and Equipment.

Federal Accounting Standards Advisory Board (FASAB) defines general PP&E as: “Tangible assets that (1) have an estimated useful life of 2 or more years, (2) are not intended for sale in the ordinary course of operations, and (3) are intended to be used or available for use by the entity.”

ITC was able to properly state PP&E as of September 30, 2010 as a direct result of a major clean-up effort performed during FY 2010, not as a result of adequate policies and procedures being in place throughout the entire year to effectively monitor, document and record PP&E on a timely basis. Without adequate policies and procedures in place throughout the entire year to effectively monitor, track and document expenditures on an ongoing basis, ITC increased its risk that PP&E or expenditures may be misclassified, causing the amounts reported on the financial statements to be misstated.

**Recommendations:**

We recommend that ITC management:

14. Review its current policy regarding PP&E to ensure it meets the intended objectives of the accounting standards.
15. Update documented procedures to ensure adequate monitoring and review of purchases to allow for proper recording and reporting as required by applicable accounting standards.

16. Train personnel on the policy and procedures surrounding PP&E to enhance their ability to identify items that should be capitalized rather than expensed.

VI. Inadequate Controls Surrounding the Procurement Process

During testing of procurement, we noted numerous instances where procurement documents were not adequately documented to consistently demonstrate compliance with the requirements of the Federal Acquisition Regulation (FAR). For example, we noted instances where the procurement documents:

- Insufficiently explained the purpose of the services to be provided;
- Were inconsistent and contained numerical errors; and
- Were lacking documentation to support the reason or amount for modifications.

Section 4.801 General of the FAR states:

(a) The head of each office performing contracting, contract administration, or paying functions shall establish files containing the records of all contractual actions.
(b) The documentation in the files (see 4.803) shall be sufficient to constitute a complete history of the transaction for the purpose of—
   (1) Providing a complete background as a basis for informed decisions at each step in the acquisition process;
   (2) Supporting actions taken;
   (3) Providing information for reviews and investigations; and
   (4) Furnishing essential facts in the event of litigation or congressional inquiries.

ITC did not have an adequate understanding of the Contracting Officer’s role and responsibilities, which included a sufficient review of the procurement documents prior to the release of the documents. In addition to the lack of skill sets and adequate training, ITC did not have written policies and procedures specific to procurement throughout the majority of the fiscal year, which further contributed to the lack of adequate internal controls over the processing, approval, and documentation surrounding procurement efforts.

The FAR is the primary regulation for use by all Federal Executive agencies in their acquisition of supplies and services with appropriated funds. Section 1.602 Contracting Officers, 1.602-1 Authority, of the FAR states, “(b) No contract shall be entered into unless the contracting officer ensures that all requirements of law, executive orders, regulations, and all other applicable procedures, including clearances and approvals, have been met.”

ITC increases its risk of noncompliance with the FAR by not requiring the Contracting Officer to possess (1) sufficient experience in Government contracting and administration, and commercial purchasing; (2) sound knowledge of acquisition policies and procedures, including the FAR and
other applicable regulations; and (3) maintaining satisfactory completion of acquisition training courses.

Furthermore, without written policies and specific procedures for ITC individuals responsible for procurement efforts to follow, ITC increases the risks of noncompliance with applicable laws and regulations, and the possibility that a material error or fraud may not be prevented or detected and corrected timely.

**Recommendations:**

We recommend that ITC management:

17. Establish a policy that requires the Contracting Officer and any other personnel involved in the procurement efforts (e.g., Contracting Officer’s Technical Representatives) to adhere to the education and experience requirements outlined by the FAR.

18. Establish procedures related to the procurement process, including proper file documentation to support contract actions.

19. Prepare a detailed checklist to be completed by the Contracting Officer and personnel involved with the procurement action to ensure that for all future procurement actions, the contract file includes all the required documentation to support the contract actions and its compliance with the FAR.

20. Train personnel responsible and accountable for procurement files on the written policies and procedures, and provide additional training to ensure the requirements of the FAR and ITC’s policies over procurement are achieved.

**Management Response:**

ITC’s management concurs with the deficiencies identified and described within this report. See attached response from the Commission’s Chairman.
Dear Mr. Castro:

The draft Report on Internal Controls identified four material weaknesses and two significant deficiencies. I concur with your assessment that the Commission has inadequate internal controls over financial reporting; insufficient monitoring, analysis and oversight of financial operations; inadequate controls over undelivered orders, accounts payable, and expenditures; and insufficient resources and personnel with appropriate skill sets. I also concur that we have inadequate controls surrounding the identification, recording, and reporting of property, plant and equipment and inadequate controls surrounding the procurement process.

Beginning with your reports on our 2009 financial statements, which highlighted the financial management deficiencies and challenges that the Commission faced, we began developing an aggressive and comprehensive strategy to address the findings. As a result, during fiscal year 2010 the Commission made significant progress in a number of areas that we believe will result in achieving our goal of accountability over Commission assets and operations. For example, we gained visibility and accountability over the Commission’s property accounts. We also drafted the first accounting manual that describes in detail the Commission’s policies and procedures.

We recognize that we have much more to do and plan to implement each of your recommendations.

Sincerely,

Deanna Tanner Okun

cc: Philip M. Heneghan
Inspector General
"Thacher’s Calculating Instrument" developed by Edwin Thacher in the late 1870’s. It is a cylindrical, rotating slide rule able to quickly perform complex mathematical calculations involving roots and powers quickly. The instrument was used by architects, engineers, and actuaries as a measuring device.