U.S. DEPARTMENT OF THE TREASURY,
OFFICE OF THRIFT SUPERVISION

FINANCIAL STATEMENTS
December 31, 1992 and 1991

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Clifton,
Gunderson & Co.
Certified Public Accountants & Consultants

The Inspector General,
U.S. Department of the Treasury
Washington, D.C.

INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying statement of financial position of the U.S. Department of the Treasury, Office of Thrift Supervision as of December 31, 1992, and the related statements of operations and retained earnings, cash flows and budget and actual expenses for the year then ended. These financial statements are the responsibility of the Agency's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the U.S. Department of Treasury, Office of Thrift Supervision as of December 31, 1991 were audited by other auditors whose report dated June 26, 1992, expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with generally accepted auditing standards, Governmental Auditing Standards, and the provisions of the Office of Management and Budget Bulletin 93-06 "Audit Requirements for Federal Financial Statements". Those standards and provisions require that we plan and perform the audit to obtain reasonable assurance about whether the 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.

In our opinion, the 1992 financial statements referred to above present fairly, in all material respects, the financial position of the U.S. Department of the Treasury, Office of Thrift Supervision as of December 31, 1992, and the results of its operations, its cash flows and its budget and actual operating expenses for the year then ended in conformity with generally accepted accounting principles and the provisions of the Office of Management and Budget Bulletin 93-02 "Form and Content of Agency Statements".

Clifton, Gunderson & Co.

Baltimore, Maryland
May 4, 1993

Statement 1

U.S. DEPARTMENT OF THE TREASURY, OFFICE OF THRIFT SUPERVISION STATEMENTS OF FINANCIAL POSITION December 31, 1992 and 1991 (in thousands)

	1992	1991
ASSETS		
Cash and cash equivalents	$ 95,220	$106,834
Accounts receivable	4,228	1,962
Land, building and equipment	47,646	51,199
Prepaid expenses	3,557	5
Total assets	$150,651	$160,000
LIABILITIES		
Accounts payable	$ 2,014	$ 1,347
Employees' accrued annual leave	8,596	8,684
Other accrued liabilities	7,865	10,601
Deferred rent credit	2,635	2,076
Total liabilities	21,110	22,708
CAPITAL		
Assumed capital	41,037	41,037
Retained earnings	88,504	96,255
Total capital	129,541	137,292
Total liabilities and capital	$150,651	$160,000

These financial statements should be read only in connection with the accompanying summary of significant accounting policies and notes to financial statements.

Statement 2

U.S. DEPARTMENT OF THE TREASURY, OFFICE OF THRIFT SUPERVISION STATEMENTS OF OPERATIONS AND RETAINED EARNINGS Years Ended December 31, 1992 and 1991 (in thousands)

	1992	1991
INCOME		
Industry assessments	$186,072	$207,181
Application/security filing fees	9,344	9,454
Interest	4,802	7,497
Other	6,408	4,274
Total income	206,626	228,406
EXPENSES		
Personnel compensation	124,702	131,575
Personnel benefits	37,997	40,908
Travel and transportation	16,270	18,108
Rent, communication and utilities	14,225	15,260
Printing and reproduction	498	846
Data processing	4,452	5,892
Training	627	1,240
Professional services	2,037	3,477
Building expenditures	3,997	5,121
Non-capitalized expenditures	1,862	1,774
Depreciation	3,267	2,727
Supplies and materials	1,102	2,012
Other services	1,068	1,159
Total expenses	212,104	230,099
LOSS FROM OPERATIONS	5,478	1,693
Loss on disposal of equipment	2,273	
NET LOSS	7,751	1,693
RETAINED EARNINGS, BEGINNING OF YEAR	96,255	97,948
RETAINED EARNINGS, END OF YEAR	$ 88,504	$ 96,255

These financial statements should be read only in connection with the accompanying summary of significant accounting policies and notes to financial statements.

Statement 3

U.S. DEPARTMENT OF THE TREASURY, OFFICE OF THRIFT SUPERVISION STATEMENTS OF CASH FLOWS
Years Ended December 31, 1992 and 1991
(in thousands)

	1992	1991
OPERATING ACTIVITIES		
Net loss	($ 7,751)	($ 1,693)
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss on disposal of equipment	2,273	
Depreciation	3,267	2,727
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable	(2,267)	1,920
(Increase) decrease in prepaid expenses	(3,552)	5
(Decrease) increase in accrued annual leave	(88)	1,033
Decrease in accounts payable and accrued liabilities	(2,069)	(7,041)
Increase in deferred rent	559	1,008
Decrease in due to FHFB		(8,920)
Net cash used by operating activities	(9,628)	(10,961)
INVESTING ACTIVITIES		
Acquisition of capital assets	(1,986)	(792)
Net decrease in cash and cash equivalents	(11,614)	(11,753)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	106,834	118,587
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 95,220	$106,834

These financial statements should be read only in connection with the accompanying summary of significant accounting policies and notes to financial statements.

Statement 4

U.S. DEPARTMENT OF THE TREASURY, OFFICE OF THRIFT SUPERVISION
STATEMENT OF BUDGET AND ACTUAL OPERATING EXPENSES
Year Ended December 31, 1992
(in thousands)

	Resources	Actual Obligations	Actual Expenses
Compensation	$127,282	$124,483	$124,702
Benefits	39,568	38,427	37,997
Travel and transportation	16,981	15,576	16,270
Rent, communication and utilities	14,634	14,053	14,225
All other	24,987	19,897	18,910
Totals	$223,452	$212,436	$212,104

These financial statements should be read only in connection with the accompanying summary of significant accounting policies and notes to financial statements.

U.S. DEPARTMENT OF THE TREASURY, OFFICE OF THRIFT SUPERVISION SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES December 31, 1992 and 1991

HISTORY AND ORGANIZATION

The U.S. Department of the Treasury, Office of Thrift Supervision (OTS) was created when the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) abolished the Federal Home Loan Bank Board and transferred all examination and supervisory activities to OTS under the Department of Treasury. OTS' primary functions are to: (1) charter federal savings and loan associations; (2) adopt regulations governing the operation of the thrift industry; (3) conduct examinations of federal and state chartered savings institutions and their holding companies; and (4) supervise compliance with federal laws and regulations and OTS directives (i.e., take measures as needed to enforce such compliance and rehabilitate troubled institutions).

FIRREA provided that OTS make assessments to recapture its operating costs. Assessments are based on OTS's budget and are collected from savings and loans.

Assumed capital in the financial statements is the net assets assumed from the Federal Home Loan Bank Board by OTS at inception, October 8, 1989, in accordance with FIRREA.

GENERAL

OTS is operated substantially as a commercial enterprise and records its calendar year transactions on an accrual basis in accordance with generally accepted accounting principles (GAAP). It receives no appropriated monies from the federal government. Its financial activities are recorded on an agency-wide basis versus a program or fund basis. Thus, certain accounting standards outlined in Title 2 of the General Accounting Office's (GAO) <u>Policy and Procedures Manual for Guidance for Federal Agencies</u> relating to appropriations, entitlements, fund accounting, fund control, grants and cooperative agreements, and rate regulated accounting are not applicable to OTS.

DEPRECIATION AND AMORTIZATION

Fixed assets in excess of $5,000 are capitalized. Depreciation is computed on a straight-line basis over the estimated useful lives as follows:

Building	50 years
Furniture, fixtures and equipment	5 years

Leasehold improvements are amortized on a straight-line basis over the life of the related leases.

INCOME TAXES

As an agency of the U.S. Department of the Treasury, OTS is exempt from all federal and state taxes based on income.

This information is an integral part of the accompanying financial statements.

U.S. DEPARTMENT OF THE TREASURY,
OFFICE OF THRIFT SUPERVISION
NOTES TO FINANCIAL STATEMENTS
December 31, 1992 and 1991

NOTE 1 - CASH AND CASH EQUIVALENTS

OTS invests its cash in overnight Treasury Securities. They are stated at cost (in thousands):

	1992	1991
Cash	$ 820	$ 2,034
Cash equivalents	94,400	104,800
Total cash and cash equivalents	$ 95,220	$106,834

NOTE 2 - LAND, BUILDING AND EQUIPMENT

The land and building owned by the Federal Home Loan Bank Board was transferred to OTS under FIRREA. OTS also assumed all furniture, fixtures, and equipment associated with personnel transferred to OTS. These assets were carried over at their existing value as recorded in the Federal Home Loan Bank Board's accounting records.

Other fixed assets acquired subsequent to that date are recorded at cost when acquired.

OTS's land, building and equipment is comprised of the following at December 31, 1992 and 1991 (in thousands):

	1992	1991
Land	$ 7,101	$ 7,101
Office building	49,596	49,596
Furniture, fixtures and equipment	11,014	19,819
Accumulated depreciation:		
Office building	(13,948)	(12,863)
Furniture, fixtures and equipment	(6,117)	(12,454)
Property and buildings, net	$ 47,646	$ 51,199

U.S. DEPARTMENT OF THE TREASURY, OFFICE OF THRIFT SUPERVISION NOTES TO FINANCIAL STATEMENTS December 31, 1992 and 1991

NOTE 3 - DUE TO FEDERAL HOME LOAN BANK BOARD

In dissolving the Federal Home Loan Bank Board (FHLBB) affairs, Sections 401 and 725 of FIRREA identified how the funds and other property of the FHLBB were to be used and distributed. As a result of these provisions, OTS and Federal Housing Finance Board (FHFB) officials agreed that OTS owed an additional $8,920,000 to the FHFB. This amount was recorded as a liability in 1989 and paid in 1991.

NOTE 4 - RENTAL INCOME

OTS leases a portion of its building space to retailers under noncancelable operating leases expiring at various dates through 2009. The leases provide for annual base rent, some of which are subject to annual increases based upon changes in the Consumer Price Index and/or a percentage of sales in excess of a specified amount.

OTS also subleases some of its existing unused leased facilities and these amounts are included below. The future minimum rentals to be received under noncancellable operating leases are as follows (in thousands):

Year ending December 31,	
1993	$ 1,721
1994	1,457
1995	1,018
1995	905
1997	476
Thereafter	2,325
	$ 7,902

NOTE 5 - RETIREMENT PLAN

OTS has three retirement systems. Two are administered by the federal government's Office of Personnel Management. The third is a private plan administered by the Financial Institutions Retirement Fund (FIRF).

The Civil Service Retirement System (CSRS), is currently two-tiered. For employees hired prior to January 1, 1984, OTS withholds approximately 7 percent of their gross earnings. This contribution is then matched by OTS and the sum is transferred to the Civil Service Retirement Fund, from which this employee group will receive retirement benefits.

NOTE 5 - RETIREMENT PLAN (continued)

For employees hired on or after January 1, 1984, with more than five years of service (not necessarily continuous), OTS withholds, in addition to Social Security withholdings, .80 percent of their gross earnings, but matches such withholdings with a 7 percent contribution. At the point such earnings exceed the FICA maximum wages of $55,500 for 1992, employees covered under this tier of CSRS are required to have 7 percent of their earnings withheld while the agency expense remains a 7 percent contribution. This second employee group will receive retirement benefits from the CSRS along with the Social Security System, to which they concurrently contribute.

Beginning in January 1987, all employees hired since January 1, 1984, either as new employees or as having less than 5 years of accumulated service (with a break in service over one year) are included in the new Federal Employee Retirement System (FERS). For such employees, OTS withholds .80 percent of their gross earnings and matches those withholdings with a 12.9 percent contribution. This group of employees will receive benefits from the FERS as well as the Social Security System to which they concurrently contribute.

Pursuant to FIRREA, the Office of Regulatory Activities and the twelve examination districts became part of OTS and OTS assumed the costs of their retirement system, which is part of FIRF. Under this private retirement system, OTS contributes a percentage of total FIRF salary. This percentage varies from year to year and was approximately 10 percent during 1992. Employees do not contribute to FIRF, but do contribute to Social Security. The percentage changes based on the number of active FIRF OTS employees, the number of people that have retired, and the benefits paid out.

The retirement expenses incurred for all plans during 1992 and 1991 was $10,833,631 and $12,396,445, respectively, which is included in personnel benefits on the accompanying statement of operations and retained earnings.

Although OTS funds either all (FIRF) or a portion (CSRS and FERS) of pension benefits under any of the above retirement systems relating to its employees and makes the necessary payroll withholdings, OTS does not account for the assets of either retirement plan, nor does it have actuarial data with respect to accumulated plan benefits or the unfunded pension liability relative to its employees. These amounts are reported by the Office of Personnel Management for both government retirement systems and are not allocated to the individual agencies. Except for 66 retired employees who had health insurance through OTS' own health plan, the Office of Personnel Management accounts for all health and life insurance programs for retired federal employees.

NOTE 6 - LEASE COMMITMENTS

The OTS conducts a majority of its regional operations in leased facilities under noncancellable operating leases expiring at various dates through 2005. Many of the leases contain a provision to renew at the end of the initial term for an additional one to ten years. The rental payments are based on a minimum rental plus a proportional share of building operating expenses and taxes.

Some of the operating leases provide for rental escalations and/or stated annual rental increases in the amount of base rent over the lives of the leases. In addition, pursuant to one of the lease agreements, the lessor agreed to provide an allowance to OTS for a portion of the build-out costs up to $1,904,850. Of this amount, $658,000 was not used and the cash was received by OTS in 1990. Such increases and allowances are reflected as a net deferred credit in the accompanying balance sheet and amortized on a straight-line basis over the life of the related leases.

The minimum rental commitments, excluding sublease income, under noncancellable operating leases are as follows (in thousands):

Year ending December 31,	
1993	$ 9,732
1994	8,759
1995	8,032
1996	2,796
1997	2,754
Thereafter	15,824
	$ 47,897

Rent expense was approximately $10,032,000 in 1992 and $10,172,000 in 1991. Sub-lease income was approximately $563,000 in 1992.

NOTE 7 - COMBINING STATEMENTS

The Combining Statement described in OMB Bulletin 91-15 and 93-02 is designed to present the information found in the financial statements by major program activities or funds. As the financial activities of OTS are not allocated by programs or funds, but rather on an agency-wide basis, a combining statement is not applicable and is not presented.

NOTE 8 - POST-RETIREMENT BENEFITS

The Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 106 "Employers' Accounting for Postretirement Benefits Other Than Pensions" in December 1990. This Statement will significantly change the Organization's practice of accounting for non-pension postretirement benefits from a pay-as-you-go (cash) basis to an accrual basis. The Organization does not intend to adopt this Statement until the required implementation date of 1993. Management has not quantified the effect of implementing this statement as yet.

NOTE 9 - COMMITMENTS AND CONTINGENCIES

There are numerous legal actions pending in the U.S. Court of Federal Claims where the claims are based on actions taken by OTS. The Department of Justice will defend these cases, and in the event that a judgment is issued against the United States or OTS, payment will be made by a U.S. Government "Judgment Fund", and not by OTS, once the judgment is final and payment is certified for disbursement by the U.S. General Accounting Office (GAO). Therefore, no loss accrual has been made for these cases.

AUDITOR'S REPORT ON

INTERNAL CONTROL STRUCTURE

Clifton,
Gunderson & Co.
Certified Public Accountants & Consultants

The Inspector General,
U.S. Department of the Treasury
Washington, D.C.

AUDITOR'S REPORT ON INTERNAL CONTROL STRUCTURE

We have audited the general-purpose financial statements of U.S. Department of the Treasury, Office of Thrift Supervision (OTS), as of and for the year ended December 31, 1992, and have issued our report thereon dated May 4, 1993.

We conducted our audit in accordance with generally accepted auditing standards, Government Auditing Standards, issued by the Comptroller General of the United States, and OMB Bulletin 93-06. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the general-purpose financial statements are free of material misstatement.

In planning and performing our audit of the financial statements of OTS for the year ended December 31, 1992, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control structure.

The management of OTS is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

- Financial reporting
- Cash
- Revenue and accounts receivable
- Expenses and accounts payable
- Payroll and related liabilities
- Fixed assets
- Data processing
- Administrative controls over compliance with laws and regulations
- Performance measures

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk. For all of the internal control structures categories listed above, except for performance measures, we also performed tests of the internal control structure.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the organization's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements.

DETAILED FIXED ASSET RECORDS

OTS has not maintained a reliable detailed fixed asset ledger since its inception. A physical inventory of furniture and equipment was taken during 1993; however, the resulting listing could not be reconciled to the general ledger control account. This initial discrepancy resulted in a write off of $5,123,287 in cost and $5,060,950 in accumulated depreciation and, accordingly, a charge to operations was needed in the amount of $62,337. The listing was to serve as a perpetual record of furniture and equipment. However, when an updated listing was compared to the general ledger control account again at December 31,1992, unreconciled differences still remained. We were informed that these differences were the result of transfers of equipment to GSA and various trade-ins of computer equipment. The general ledger was again adjusted to the amount shown in the perpetual listing. Such adjustment resulted in reductions in cost of $5,729,764 and accumulated depreciation of $3,346,574 and, accordingly, an additional charge to operations was needed for $2,273,190. In addition, many of the items in the listing did not have adequate documentation supporting cost and acquisition dates.

The aforementioned adjustments resulted in furniture and equipment declining from 1991 to 1992 as follows:

	1991	1992
Cost	$19,818,268	$10,975,275
Accumulated depreciation	$12,452,678	$ 6,111,847
Net book value	$ 7,365,590	$ 4,863,428

RECOMMENDATIONS

1. We recommend that a complete physical inventory be taken again and reconciled to the general ledger control. Also, each item should have appropriate supporting documentation of its cost and acquisition date. For older equipment this information can be obtained from vendors which specialize in this area.

2. In order to monitor and account for transfers and disposals more accurately, we recommend that such activity not be completed until the Controllers office approves such activity. This will assist the Controllers' office in recording such transactions in a timely manner.

AUDITEE RESPONSE

1. & 2. The OTS policy is to conduct a physical inventory of all FF&E every year. We will take another inventory in the late fall which will involve the use of accounting personnel who will monitor the process. We expect to resolve any outstanding issues raised by the audit during the next inventory.

ELECTRONIC DATA PROCESSING SYSTEM

ACCESS CONTROLS

Access controls for the accounting, payroll, time activity and reporting system and billing applications are not adequate. We found:

- <u>A non descriptive user ID in the accounting application</u>. The user or owner of the account could not be easily identified. Accordingly, management has not been able to determine the user responsible for the initiating certain transactions.

- <u>Security tables in several applications contain employees that are no longer employed in the department</u>. Employees transferred to another department, employees with a change in duty assignments, and employees leaving OTS have not always been deleted from security tables.

- <u>Security tables in several applications contain individuals with incompatible access rights</u>.

- <u>Access to the payroll and personnel applications are governed by group access identifications</u>. These group access identifications do not provide for individual accountability.

RECOMMENDATION

3. We recommend that the access controls for the accounting, payroll, time activity and reporting system and billing applications be revised to ensure that only appropriate employees have access to computer applications.

AUDITEE RESPONSE

3. This recommendation is apparently based on four issues. We don't agree with the first item which indicates that an accounting system user could not be identified. Each accounting user is given a unique accounting identification granting them access to specific functions. As transactions are entered into the system they are batched with a unique batch number assigned dynamically by the system. This batch number can be traced back to the individual accounting user for a given transaction by identifying the transaction date and reviewing the transaction entries for the specified period. The user identification is not attached to the individual transaction record but the batch number is. In the voucher payment function, the ALLIN1 name of the accounting user who releases the payment is attached to the transaction (paid) record. This provides the identification of the individual responsible for the actual voucher disbursement.

   The second point states that the security tables for the Payroll/Personnel and Accounting systems contain employees that are no longer employed in these capacities. Measures are being taken to correct this problem. The Payroll/Personnel table and Accounting table are each one part of a two part security check which is required prior to accessing the system. A user's ID must reside on both the system table and the VAX interface menu table in order to gain access to the system. These two tables will be closely monitored in the future. For the employees in question, the VAX interface menu option was removed but not the user's ID on the system table. Despite this oversight, the employees could not have accessed the systems they had previously accessed.

   The third point stated that security tables in several applications contain individuals with incompatible access rights. The Controller's division has consistently promoted the separation of responsibilities to enhance each system's integrity and reduce the opportunity for the systems to be compromised. However, this requirement has not always been followed because some offices have undergone significant staff reductions which limit their ability to adequately divide the system responsibilities. We believe there are sufficient overall controls that mitigate these weaknesses and as we continue to downsize we will look for further ways to not only ensure that internal controls are cost effective but also represent an adequate separation of duties.

   Finally, the fourth point states that access to the Payroll/Personnel application is governed by group access identifications. Our research shows that access to the Payroll/Personnel system is divided into seven main groups. Of these, only the Washington Payroll staff enables more than two users to access the system by utilizing the same entry identification code. This item will be corrected by July so as to provide each user a unique entry identification code.

APPLICATION SECURITY POLICES AND PROCEDURES

There is no written policy and procedure to approve, change and delete access privileges and passwords for the accounting, payroll, personnel, assessment billing, and time activity reporting system applications. Without written application security policies and procedures, management has no control of application security. Management does not know if owners are in compliance or if application security is enforced.

RECOMMENDATION

4. We recommend that written policies and procedures be developed for all applications specifying:

   - Access approval process and documentation
   - Access modifications and deletion process and documentation.
   - Periodic review of users' access privileges.
   - Method of notifying system owner of employees' change of duties, department transfers and employee terminations.

AUDITEE RESPONSE

4. The access control capability is a recent addition to the system ownership concept and corresponding responsibilities. Due to other priority work, the drafting of a set of policies and procedures regarding system access has not been developed. However we agree with the recommendation and a new policies and procedures instruction will be developed and added to the Controller's division's Policy and Procedures manual by the end of 1993. This new policy and procedures document will cover the Payroll/Personnel and Accounting systems.

EDP PROJECT LEADERS HAVE ACCESS TO LIVE DATA AND PROGRAM FILES.

There is lack of segregation of duties between the EDP Project Leaders and Production Control personnel. The EDP Project Leader has access to live data and production programs. This matter was previously reported in the prior auditor's management letter for 1990 and 1991 and in the Federal Managers' Financial Integrity Act of 1992 Assurance Report. Pursuant to an OTS memorandum dated April 27, 1992, the Quality Assurance Unit was created in order to provide adequate separation of duties between the EDP Project Leaders and Production Control personnel. However, the Quality Assurance Unit has not yet been created.

RECOMMENDATION

5. We recommend that OTS setup the Quality Assurance unit as soon as possible.

AUDITEE RESPONSE

5. We agree with the recommendation to establish a Quality Assurance Unit. We have begun to staff it with two full-time people. One person has been selected and the other position will be posted and filled during the third quarter of 1993. With respect to the specific observation on the project leaders having access to production code, we will evaluate alternatives to the present methodology after establishing the quality assurance unit.

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A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities 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.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe none of the reportable conditions described above is a material weakness.

We also noted other matters involving the internal control structure and its operation that we have reported to the management of OTS in a separate letter dated May 4, 1993.

This report is intended for the information of the Office of Inspector General and management. However, this report is a matter of public record and its distribution is not limited.

Clifton, Gunderson & Co.

Baltimore, Maryland
May 4, 1993

AUDITOR'S REPORT ON

COMPLIANCE

Clifton,
Gunderson & Co.
Certified Public Accountants & Consultants

The Inspector General,
U.S. Department of the Treasury,
Washington, D.C.

AUDITOR'S REPORT ON COMPLIANCE

We have audited the financial statements of U.S. Department of the Treasury, Office of Thrift Supervision (OTS) as of and for the year ended December 31, 1992, and have issued our report thereon dated May 4, 1993.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States and OMB Bulletin 93-06. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws and regulations applicable to OTS is the responsibility of the Office of Thrift Supervision's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of OTS's compliance with certain provisions of laws and regulations. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests indicate that, with respect to the items tested, OTS complied, in all material respects, with the provisions referred to in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that OTS had not complied, in all material respects, with those provisions.

This report is intended for the information of the Office of Inspector General and management. However, this report is a matter of public record and its distribution is not limited.

Clifton, Gunderson & Co.

Baltimore, Maryland
May 4, 1993

Clifton,
Gunderson & Co.
Certified Public Accountants & Consultants

May 4, 1993

U.S. Department of the Treasury,
The Office of Thrift Supervision
Washington, D.C.

We have completed the audit of U.S. Department of the Treasury, Office of Thrift Supervision (OTS) for the year ended December 31, 1992. In connection with our audit, we issued communications of internal control structure related matters noted in our audit dated May 4, 1993. During the course of our audit, we had the opportunity to observe the various accounting, operating and procedural matters as they related to the OTS. Based on our audits, we would like to make the following observations and suggestions.

A. ELECTRONIC DATA PROCESSING

1. **Existing Condition:** The Disaster Recovery Plan does not include procedures for classifying the severity of the disaster nor does the plan include strategy for continuing business operations.

   Recommendation: The disaster recovery plan should be expanded to include the classification of level of emergencies and actions required at each level. The underlying purpose of contingency planning is the resumption of all business operations, not just Information Resource Management (IRM). Policies and procedures should be developed for recovering critical and vital user functions in accordance with the planned strategy.

2. **Existing Condition:** OTS has not performed periodic risk analysis and certifications as specified in OMB Circular No. A-130 Appendix, "Security of Federal Automated Information Systems". The security officer informed us that OTS has just started the security reviews.

   Recommendation: OTS should perform a periodic review and recertification every three years of sensitive applications in accordance with OMB Circular A-130. The certifications should be fully documented and maintained in official agency records.

B. COMPLIANCE WITH FMFIA

3. **Existing Condition:** There is limited documentation to reconcile the determination of assessable units to the OTS organization chart. The number of assessable units has grown from 35 to approximately 150 in OTS's three-year history. The manager of each division determines what should be considered an assessable unit, and although there is a

E. YEAR-END ACCRUAL ACCOUNTING

8 **Existing Condition:** We understand that the Controllers department solicited information from various departments to assist them in making year-end accruals. However, we noted instances where budgets or payment schedules were used as the basis for accruals.

Recommendation: The premise and rationale for the accrual of expenses should be re-emphasized to those assisting in the gathering of information. That premise is that an accrual should only be made for management's best an estimate of the cost of goods or services received as of a particular date.

We would be happy to further discuss with you the items contained in this letter.

Sincerely,

CLIFTON, GUNDERSON & CO.

//S//

William H. Oliver
Partner

cc: The Inspector General,
U.S. Department of the Treasury