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Independent Auditors' Report

Secretary and Acting Inspector General
United States Department of Labor

Report on the Financial Statements

The accompanying financial statements of the United States Department of Labor (DOL) comprise the consolidated financial statements and the sustainability financial statements.

We have audited the consolidated financial statements, which comprise the consolidated balance sheets as of September 30, 2020 and 2019, and the related consolidated statements of net cost and changes in net position, and combined statements of budgetary resources for the years then ended, and the related notes to the consolidated financial statements.

We have audited the 2020 sustainability financial statements, which comprise the statements of social insurance as of September 30, 2020, 2019, 2018, and 2017; the statements of changes in social insurance amounts for the years ended September 30, 2020 and 2019; and the related notes to the 2020 sustainability financial statements.

Further, we were engaged to audit the 2016 sustainability statement, which comprises the statement of social insurance as of September 30, 2016, and the related notes to this financial statement (2016 statement of social insurance).

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements, 2020 sustainability financial statements, and the 2016 statement of social insurance in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express opinions on the consolidated financial statements and the 2020 sustainability financial statements based on our audits. We conducted our audits of the consolidated financial statements and the 2020 sustainability financial statements in accordance with auditing standards generally accepted in the United States of America, in accordance with the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and in accordance with Office of Management and Budget (OMB)

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Bulletin No. 19-03, *Audit Requirements for Federal Financial Statements*. Those standards and OMB Bulletin No. 19-03 require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements and the 2020 sustainability financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the consolidated financial statements and the 2020 sustainability financial statements.

Our responsibility is also to express an opinion on the 2016 statement of social insurance based on conducting an audit in accordance with auditing standards generally accepted in the United States of America, in accordance with the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and in accordance with OMB Bulletin No. 19-03, *Audit Requirements for Federal Financial Statements*. Because of the matter described in the Basis for Disclaimer of Opinion paragraph, however, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the statement of social insurance as of September 30, 2016.

Basis for Disclaimer of Opinion on the Statement of Social Insurance as of September 30, 2016

As described in Note 1.W.2, DOL refined its methodology for estimating future excise tax income in fiscal year 2016. DOL was unable to provide sufficient analyses or other documentation to evidence that its methodology and certain underlying assumptions used in the determination of the present value of estimated future excise tax income for the current and new participants in the statement of social insurance as of September 30, 2016 were prepared and fairly presented in accordance with U.S. generally accepted accounting principles. Therefore, we have not been able to obtain sufficient appropriate audit evidence for the present value of estimated future excise tax income for the current and new participants.

Disclaimer of Opinion on the Statement of Social Insurance as of September 30, 2016

Because of the significance of the matter described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the U.S. Department of Labor's social insurance information as of September 30, 2016. Accordingly, we do not express an opinion on the statement of social insurance as of September 30, 2016.

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Opinions on the Financial Statements

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the U.S. Department of Labor as of September 30, 2020 and 2019, and its net costs, changes in net position, and budgetary resources for the years then ended in accordance with U.S. generally accepted accounting principles.

Also, in our opinion, the 2020 sustainability financial statements referred to above present fairly, in all material respects, the U.S. Department of Labor's social insurance information as of September 30, 2020, 2019, 2018, and 2017; and its changes in social insurance amounts for the years ended September 30, 2020 and 2019, in accordance with U.S. generally accepted accounting principles.

Emphasis of a Matter

As discussed in Notes 1-W and 1-Y to the financial statements, the sustainability financial statements are based on management's assumptions. These sustainability financial statements present the actuarial present value of DOL's future expenditures to be paid to or on behalf of participants, the present value of estimated future income to be received from excise taxes, and the present value of estimated future expenditures for administrative costs during a projection period sufficient to illustrate long-term sustainability. The sustainability financial statements are intended to aid users in assessing whether future resources will likely be sufficient to sustain public services and to meet obligations as they come due. The statements of social insurance and changes in social insurance amounts are based on income and benefit formulas in current law and assume that scheduled benefits will continue after the related trust fund is exhausted. The sustainability financial statements are not forecasts or predictions. The sustainability financial statements are not intended to imply that current policy or law is sustainable. In preparing the sustainability financial statements, management considers and selects assumptions and data that it believes provide a reasonable basis to illustrate whether current law or policy is sustainable. Assumptions underlying such sustainability information do not consider changes in policy or all potential future events that could affect future income, future expenditures, and sustainability. Because of the large number of factors that affect the sustainability financial statements and the fact that future events and circumstances cannot be estimated with certainty, even if current policy is continued, there will be differences between the estimates in the sustainability financial statements and the actual results, and those differences may be material. Our opinion on the 2020 sustainability financial statements is not modified with respect to this matter.

Other Matters

Interactive Data

Management has elected to reference to information on websites or other forms of interactive data outside the *Agency Financial Report* to provide additional information for the users of its financial statements. Such information is not a required part of the basic financial statements or supplementary information required by the Federal Accounting Standards Advisory Board. The information on these websites or the other interactive data has not been subjected to any of our auditing procedures, and accordingly, we do not express an opinion or provide any assurance on it.

Required Supplementary Information

U.S. generally accepted accounting principles require that the information in the Management's Discussion and Analysis and Required Supplementary Information sections be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Federal Accounting Standards Advisory Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audits were conducted for the purpose of forming an opinion on the basic financial statements as a whole. The information in the Message from the Secretary of Labor, Message from the Chief Financial Officer, and Other Information sections is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audits of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements as of and for the year ended September 30, 2020, we considered DOL's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of DOL's internal control. Accordingly, we do not express an opinion on the effectiveness of DOL's internal control. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material

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weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in Exhibit I, that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether DOL's financial statements as of and for the year ended September 30, 2020 are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 19-03.

We also performed tests of its compliance with certain provisions referred to in Section 803(a) of the *Federal Financial Management Improvement Act of 1996* (FFMIA). Providing an opinion on compliance with FFMIA was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances in which DOL's financial management systems did not substantially comply with the (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level.

DOL's Response to the Finding

DOL's response to the finding identified in our audit is described in Exhibit II. DOL's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

Purpose of the Other Reporting Required by Government Auditing Standards

The purpose of the communication described in the Other Reporting Required by *Government Auditing Standards* section is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of DOL's internal control or compliance. Accordingly, this communication is not suitable for any other purpose.

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November 16, 2020

1. Improvements Needed in the Review of Estimates

The preparation of the United States Department of Labor's (DOL) financial statements requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities as of September 30, 2020, and the associated revenues and expenses during the reporting period. These estimates include the present value of the estimated future Black Lung excise tax income, Energy Employees Occupational Illness Compensation (EEOIC) benefits actuarial liability, and the Unemployment Trust Fund (UTF) benefit overpayment and reimbursable receivables, among others.

During our fiscal year (FY) 2020 audit of DOL's financial statements, we identified certain deficiencies in the management review controls over the estimates noted above. Specifically, we noted that the management review controls were not designed to perform at a sufficient level of precision to ensure that errors in the development of the estimates were identified and corrected or to properly consider the impact of the most recently available data on the estimates. In addition, certain management controls were not sufficiently documented to support the specific items reviewed, analyses performed, and conclusions reached.

Collectively, these deficiencies increase the risk that material errors in the estimates could occur and not be prevented or detected and corrected in a timely manner. We have included below a summary of the specific issues noted for each estimate.

Present Value of Estimated Black Lung Excise Tax Income

Management was unable to provide sufficient documentation to support their position for not updating the future excise tax income estimate developed in August 2020 with the updated coal economic data as of September 30, 2020, including the production and exports data, reported by the U.S. Energy Information Administration (EIA).

In addition, we noted instances in which the peer reviewer did not follow procedures outlined within the Actuary Checklist, and as a result, did not identify incorrect application of the model's functionality. As a result, management did not identify two formula errors in the model. One of the errors caused the model to populate certain information for the incorrect year while the other incorrectly created a growth rate rather than a decline rate.

As a result of these errors, the present value of estimated future excise tax income was understated by $125 million as of September 30, 2020.

EEOIC Benefits Liability

Office of Workers' Compensation Programs' (OWCP) controls to perform a peer review of the model by an individual other than the preparer did not operate at a sufficient level of precision to verify the accuracy of certain formulas within the model. We noted that the formulas within the model that aggregate the historical quarterly medical payments into fiscal year totals, which are the starting point from which future payments are projected in the model, contained hardcoded values that required annual updates. However, the accuracy of these formulas was not explicitly reviewed as part of management’s controls over the FY 2020 model. Management noted that compensating controls were in place to review the reasonableness of the average medical cost per eligible individual assumption used in the model; however, these controls were not sufficiently documented to support the specific items reviewed, analysis performed, or the conclusions reached.

The formula error noted above resulted in a potential overstatement of $920 million in the EEOIC benefits liability as of September 30, 2020.

UTF Overpayment and Benefit Accounts Receivable

Employee and Training Administration (ETA) management review controls did not identify that currently available information was not considered in the estimates for non-exchange revenue from reimbursable employers, and reimbursable and overpayments accounts receivable. Specifically, we noted that management did not consider the impact of certain increased activity, such as collections and disbursements, during the fourth quarter of FY 2020 that was reported through the monthly ETA-2112 and 902-P forms or the quarterly ETA 227. As a result, reimbursable and overpayments receivables as of September 30, 2020 were initially understated by $1.09 billion and $1.24 billion, respectively. Management did subsequently record a correcting entry to overpayment receivables in the amount of $486 million. In addition, reimbursable revenue was understated by $200 million as it was misclassified as unemployment taxes. This misclassification was subsequently corrected by management.

The deficiencies noted above occurred because the risk assessment processes for OWCP and ETA did not sufficiently identify and assess the accounting and reporting risks that currently impacted their accounting estimates and implement the necessary controls to address those risk. Furthermore, management’s policies and procedures did not require the individuals responsible for the controls to sufficiently document the specific items reviewed, analysis performed, or the conclusions reached. Without appropriate controls in place that operate at a sufficient level of precision, there is an increased risk that management will not prevent, or detect and correct misstatements in their accounting estimates in a timely manner.

The following criteria are relevant to the conditions noted above:

- The Government and Accountability Office *Standards for Internal Control in the Federal Government* (the Standards), Section 7.03 states:

> To identify risks, management considers the types of risks that impact the entity. This includes both inherent and residual risk. Inherent risk is the risk to an entity in the absence of management’s response to the risk. Residual risk is the risk that remains after management’s response to inherent risk. Management’s lack of response to either risk could cause deficiencies in the internal control system.

Section 10.02 of the Standards states:

> Management designs control activities in response to the entity's objectives and risks to achieve an effective internal control system. Control activities are the policies, procedures, techniques, and mechanisms that enforce management's directives to achieve the entity's objectives and address related risks. As part of the control environment component, management defines responsibilities, assigns them to key roles, and delegates authority to achieve the entity's objectives. As part of the risk assessment component, management identifies the risks related to the entity and its objectives, including its service organizations; the entity's risk tolerance; and risk responses. Management designs control activities to fulfill defined responsibilities and address identified risk responses.

Section 10.03 of the Standards states:

> Management clearly documents internal control and all transactions and other significant events in a manner that allows the documentation to be readily available for examination. The documentation may appear in management directives, administrative policies, or operating manuals, in either paper or electronic form. Documentation and records are properly managed and maintained.

To address the deficiencies noted above, we recommend that the Director, Office of Workers' Compensation Programs and the Assistant Secretary for Employment and Training, in coordination with the Chief Financial Officer:

1. Design and implement controls over their respective estimates to ensure management's review of the estimates are performed at a sufficient level of detail, including the underlying data, assumptions, and formulas used to determine the estimates;

2. Design and implement controls to evaluate changes in assumptions occurring between the measurement date and the valuation and update the estimates, as appropriate;

3. Amend policies and procedures to provide specific steps to be performed during the reviews and the documentation requirements, which should include the specific items reviewed, analyses performed, and conclusions reached;

4. Formally document the level of precision used in the reviews to ensure that the review occurs at an appropriately precise level to identify errors within model functionality and data input, which would allow the reviewer to identify material errors in the estimates;

5. Maintain documentation of the reviews performed to assess the reasonableness of the underlying data, assumptions, and formulas used in the models that is sufficiently

detailed to evidence the specific items reviewed, analysis performed, and conclusions reached; and

6. Provide additional training to the reviewers of the estimates to reinforce established policies and procedures, as necessary.

Management's Response:

See Exhibit II for management's response.

Auditors' Response:

We will conduct follow-up procedures in FY 2021 to determine whether corrective actions have been developed and implemented.

U.S. Department of Labor

Office of the Chief Financial Officer
Washington, D.C. 20210

November 13, 2020

MEMORANDUM FOR: ELLIOT P. LEWIS
Assistant Inspector General for Audit

FROM: JAMES WILLIAMS
Chief Financial Officer

SUBJECT: FY 2020 Independent Auditors' Report on DOL's Financial Statements
Draft Report Number: 22-21-004-13-001

Please find the attached management's response to Draft Report No. 22-19-004-13-001, FY 2020 Independent Auditors' Report on DOL' Financial Statements.

We appreciate the opportunity to provide input and look forward to continued collaboration with the OIG audit team.

Please contact me if you have any questions.

Attachment

cc: Kevin Brown, Deputy Chief Financial Officer
John Pallasch, Assistant Secretary for Employment and Training Administration
Julia Hearthway, Director for Office of Workers' Compensation Programs

Management's Response

Fiscal Year 2020 Independent Auditors' Report

1. Improvements Needed in the Review of Estimates

Management agrees that several of the findings cited in the report must be addressed. However, as in previous audit engagements, management reiterates our request that significant matters for discussion be raised early, so that detailed conversations around mitigating factors, compensating controls, and professional judgement can be presented by management with enough time for meaningful consideration by the auditors.

OWCP recognizes its responsibility for controls over estimates related to the Energy Employees Occupational Illness Compensation Program Act (EEOICPA) Benefits Liability, and the Present Value of Estimated Black Lung Excise Tax Income. OWCP believes that the stated deficiencies have not in any significant way increased the risk that material errors in the estimates could occur and not be prevented, or detected and corrected in a timely manner. OWCP has in place compensating controls which identify any unreasonable result in its formulas and spreadsheets. Management believes that OWCP was able to provide sufficient documentation to support its position for not utilizing updated coal economic data as of September 30, 2020. OWCP provided extensive documentation related to both its methodology and application of professional judgment in determining not to utilize the September data. While there are inherent uncertainties involved in the estimation of actuarial liability models, management continuously seeks to improve the estimate and takes seriously its responsibility to prevent, detect, and correct errors that could lead to material misstatements. To this end, management has worked closely with its internal and external actuaries to correct the errors identified in the model by monitoring all results for reasonableness and consistency with other available data in order to produce the best and most reasonable estimates possible. Moving forward, management will continue to review its internal controls and review procedures over the estimates to more accurately identify errors in the models.

Regarding the UTF Overpayment and Benefit Accounts Receivable, management believes the methodology is sound and the large fluctuation is due to unprecedented circumstances caused by the COVID-19 pandemic and the actions taken to mitigate the impact on the economy. The timing of when state reported data was available was a contributing factor to errors noted by the independent auditors. Management will consider modifying procedures to account for unique situations in the future. Management also updated the methodology to include an additional control for review. Staff involved in the production and review of the UTF disbursement submission have thoroughly reviewed and discussed the new Standard Operating Procedure. The section in the operating procedures addressing steps for reviewing estimates to ensure accuracy has been emphasized.

Management of the Department of Labor continually seeks to improve its policies and procedures to address issues identified during the audit. During FY 2021, DOL will review and update corrective action plans and develop remediation activities to address these noted improvements. Management appreciates the opportunity to provide input and looks forward to the continued collaboration with the OIG audit team.