

U.S. Department of Labor

Office of Inspector General—Office of Audit

OFFICE OF WORKERS' COMPENSATION PROGRAMS



LONGSHORE AND HARBOR WORKERS' COMPENSATION ACT SPECIAL FUND FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT

September 30, 2012 and 2011

This report was prepared by KPMG, LLP, under contract to the U.S. Department of Labor, Office of Inspector General, and by acceptance, it becomes a report of the Office of Inspector General.

Elizabeth P. Lewis

Assistant Inspector General for Audit

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**LONGSHORE AND HARBOR WORKERS'
COMPENSATION ACT SPECIAL FUND**

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**LONGSHORE AND HARBOR WORKERS'
COMPENSATION ACT SPECIAL FUND**

Acronyms

AUP	Agreed Upon Procedures
DCCA	District of Columbia Workmen's Compensation Act
DLHWC	Division of Longshore and Harbor Workers' Compensation
DOL	Department of Labor
Fund	Longshore and Harbor Workers' Compensation Act Special Fund
FY	Fiscal Year
LHWCA	Longshore and Harbor Workers' Compensation Act
OMB	Office of Management and Budget
OWCP	Office of Workers' Compensation Programs
Program	Longshore and Harbor Workers' Compensation Act Program
SBR	Statement of Budgetary Resources
SFFAS	Statements of Federal Financial Accounting Standards
U.S.C.	United States Code
USSGL	United States Standard General Ledger

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**LONGSHORE AND HARBOR WORKERS'
COMPENSATION ACT SPECIAL FUND**

Management's Discussion and Analysis (unaudited)
Years ended September 30, 2012 and 2011

Mission and Organizational Structure

The Longshore and Harbor Workers' Compensation Act (LHWCA) provides medical benefits, compensation for lost-wages and rehabilitation services for job-related injuries, diseases or death of private-sector workers in certain maritime and related employment. Generally, benefits are paid directly from private funds by an authorized self-insured employer or through an authorized insurance carrier. Cases meeting the requirements of the Longshore and Harbor Workers' Compensation Act are paid from the LHWCA Special Fund (the Fund) comprised primarily of employer contributions (assessments). In fiscal years (FY) 2012 and 2011, 3,943 and 4,071 injured workers and dependents received compensation benefits from the Fund.

The reporting entity is the Fund. Organizationally the Fund is administered by the Department of Labor (DOL), Office of Workers' Compensation Programs (OWCP), Division of Longshore and Harbor Workers' Compensation (DLHWC). The DLHWC has direct responsibility for administration of the Fund. The Fund supports the program mission by providing compensation, and in certain cases, medical care payments to employees disabled from injuries which occurred under the Longshore and Harbor Workers' Compensation Act or its extensions. The Fund also extends benefits to dependents if any injury resulted in the employee's death.

Additionally, Section 10(h) of the LHWCA provides annual wage increase compensation (cost of living adjustments) for pre-1972 compensation cases entitled due to total permanent disability or death. Fifty percent of this annual wage increase compensation is paid by Federal appropriated funds, and fifty percent is paid by the Fund through the annual assessment. Appropriated funding for Section 10(h) is not reflected in the accompanying financial statements. Appropriated funding is reflected in the Federal Employees' Compensation Act Special Benefit Fund.

Administrative services for operating the Fund are provided by OWCP on behalf of the Fund. Funding for these costs is primarily provided by Federal Appropriations to OWCP's Salaries and Expense account, which is not part of the Fund. The Fund reimburses OWCP for certain direct expenses associated with administrative support of the Fund and for rehabilitation services provided to eligible claimants.

**LONGSHORE AND HARBOR WORKERS'
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Management's Discussion and Analysis (unaudited)

Years ended September 30, 2012 and 2011

Financial Highlights

The majority of the revenue of the Fund is generated through annual recurring assessments paid by self-insured employers and insurance carriers and totaled \$124,486,637 in FY 2012 and \$126,360,567 in FY 2011. Other sources of payments into the Fund include fines and penalties levied under the LHWCA (section 44c), payments by employers of \$5,000 for each death case where there is no survivor entitled to the benefits, and interest payments on Fund investments.

Investment interest income for the Fund was \$18,628 for FY 2012 compared to \$24,791 for FY 2011. The average interest rate earned during FY 2012 was 0.05% compared to 0.07% for FY 2011.

The Fund's costs remained relatively stable compared to FY 2011; \$124,313,279 for FY 2012 compared to \$124,345,106 for FY 2011. Proceeds of the Special Fund are used for payments under: section 8(f) for second injury claims; section 10(h) for initial and subsequent annual adjustments in compensation for permanent total disability or related death from injuries which occurred prior to the effective date of the 1972 LHWCA amendments; sections 39(c) and 8(g) for the procurement of medical and vocational rehabilitation services for permanently disabled employees and to provide a maintenance allowance to workers undergoing rehabilitation; section 18(b) for compensation to injured workers in cases of employer default; and section 7(e) for the cost of certain medical examinations.

Performance Goals and Results

The DLHWC's administration of the Fund supports DOL's Strategic Goal 4 – *Secure health benefits and, for those not working, provide income security*. This goal broadly promotes the economic security of workers and families. In particular, the DLHWC's administration of the Fund supports Strategic Goal 4 – "*Secure health benefits and, for those not working, provide income security*" and Outcome Goals 4.1, Facilitate return to work for workers experiencing workplace injuries or illnesses who are able to work and income and medical care for those who are unable to work, and 4.2, Ensure income support when work is impossible or unavailable. DOL plays a large role in ensuring that worker benefits are protected and that employers administer benefit programs in an appropriate way. The DLHWC assists in meeting these outcome goals by ensuring sufficient funds are assessed to fund the benefit payments, and payments to the

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Management's Discussion and Analysis (unaudited)

Years ended September 30, 2012 and 2011

beneficiaries are made promptly. In FY 2012, assessments were sufficient to cover the costs, and performance goals targeting the timeliness of initial claims processing and benefit delivery outcomes were achieved.

Internal Controls

The Longshore and Harbor Workers' Compensation Division's Branch of Financial Management, Insurance and Assessment is comprised of four employees and one supervisor. It guards against unethical behavior by segregating duties and assigning roles to each function. Much of the oversight, evaluation, monitoring, control and supervisory activity is face-to-face. Each of the district offices operates like the Branch of Financial Management, Insurance and Assessment.

Management communicates all procedural, policy, and operating goals to staff with regular staff meetings, a written procedure manual, e-mails, and frequent individual communications regarding changes, problems and issues.

Statutes provide the formal standards where these are applicable, such as privacy statutes, cash handling procedures and conflict of interest regulations. All codes, statutes, and regulations governing the conduct of Federal employees apply to all Longshore Division employees.

For cases paid by the Special Fund, a District Director or Administrative Law Judge issues a formal Compensation Order to identify the payee and set the amount. Five employees review each new case before making the payment to ensure accuracy.

With the exception of certain internal control deficiencies noted in the Independent Auditors' Report, monthly cash basis statements, monthly case management reports, quarterly review processes, biweekly payment summaries, the *Statement of Transactions* (SF-224) and the *Statement of Differences* (FMS-6652) all provide current, reliable, and accurate information.

Known Risks and Uncertainties

The Fund is the single largest payer of indemnity payments under the LWHCA. Although there are approximately 526 authorized insurance carriers and self-insured employers, benefit payments are concentrated among a relatively few. For example, the top ten

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Years ended September 30, 2012 and 2011

carriers and self-insurers alone pay 53% of the total industry payments excluding Special Fund payments. If a major carrier or self-insurer fails, the remainder would face substantially increased assessments.

The Fund is reviewed one year at a time for current expenses. There are no reserve funds for future Fund obligations. A series of high value single payment claims, for example a large number of hearing loss claims resolved in the private sector, could exceed the predictions used to quantify the assessment. A single, very large claim from an uninsured, bankrupt employer could have the same effect. Temporary collection issues could result, necessitating special, unscheduled assessments or other actions to ensure the Fund has sufficient liquid resources to fund claims liabilities as they come due.

There are currently no known examples of these risks and uncertainties.

Limitations of the Financial Statements

The following are limitations of the financial statements:

- The financial statements have been prepared to report the financial position and results of operations of the Fund, pursuant to the requirements of the Longshore and Harbor Workers' Compensation Act (33 U.S.C. 944(j)).
- While the statements have been prepared from the books and records of the Fund in accordance with U.S. Generally Accepted Accounting Principles for U.S. Government entities and the formats prescribed by the Office of Management and Budget, (OMB), the statements are different from the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.
- The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity, that liabilities cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the sovereign entity.



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Independent Auditors' Report

Acting Director
Office of Workers' Compensation Programs, U.S. Department of Labor

Deputy Inspector General
U.S. Department of Labor

We have audited the accompanying balance sheets of the U.S. Department of Labor's (DOL) Longshore and Harbor Workers' Compensation Act Special Fund (the Fund) as of September 30, 2012 and 2011, and the related statements of net cost, changes in net position, and budgetary resources (hereinafter referred to as "financial statements" or "basic financial statements") for the years then ended. The objective of our audits was to express an opinion on the fair presentation of these financial statements. In connection with our fiscal year (FY) 2012 audit, we also considered the Fund's internal control over financial reporting and tested the Fund's compliance with certain provisions of applicable laws, regulations, and contracts that could have a direct and material effect on these financial statements.

Summary

As stated in our opinion on the financial statements, we concluded that the Fund's financial statements as of and for the years ended September 30, 2012 and 2011, are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles.

As discussed in our opinion on the financial statements, management changed the Fund's presentation for reporting the Statement of Budgetary Resources in FY 2012.

Our consideration of internal control over financial reporting resulted in identifying certain deficiencies that we consider to be significant deficiencies, as defined in the Internal Control over Financial Reporting section of this report, as follows:

1. Controls over the Financial Reporting Process Need Improvement
2. Controls over the Assessments Subsidiary Ledger Need Improvement

We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses as defined in the Internal Control over Financial Reporting section of this report.



The results of our tests of compliance with certain provisions of laws, regulations, and contracts disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended.

The following sections discuss our opinion on the Fund's financial statements; our consideration of the Fund's internal control over financial reporting; our tests of the Fund's compliance with certain provisions of applicable laws, regulations, and contracts; and management's and our responsibilities.

Opinion on the Financial Statements

We have audited the accompanying balance sheets of the U.S. Department of Labor's Longshore and Harbor Workers' Compensation Act Special Fund as of September 30, 2012 and 2011, and the related statements of net cost, changes in net position, and budgetary resources for the years then ended.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the U.S. Department of Labor's Longshore and Harbor Workers' Compensation Act Special Fund as of September 30, 2012 and 2011, and its net costs, changes in net position, and budgetary resources for the years then ended, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1(j) to the financial statements, management changed the Fund's presentation for reporting the Statement of Budgetary Resources in FY 2012, based on new reporting guidance under OMB Circular No. A-136, *Financial Reporting Requirements*. As a result, the Fund's Statement of Budgetary Resources for FY 2011 has been adjusted to conform to the current year presentation.

U.S. generally accepted accounting principles require that the information in the Management's Discussion and Analysis 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.



Internal Control over Financial Reporting

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.

Our consideration of internal control over financial reporting was for the limited purpose described in the Responsibilities section of this report and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. In our FY 2012 audit, we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting described in Exhibit I that we consider to be significant deficiencies in internal control over financial reporting. 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.

Exhibit II presents the status of the prior year material weakness.

Compliance and Other Matters

The results of our tests of compliance, as described in the Responsibilities section of this report, disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 07-04.

* * * * *

Responsibilities

Management's Responsibilities. Management is responsible for the financial statements; establishing and maintaining effective internal control over financial reporting; and complying with laws, regulations, and contracts applicable to the Fund.

Auditors' Responsibilities. Our responsibility is to express an opinion on the FY 2012 and 2011 financial statements of the Fund based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Bulletin No. 07-04. Those standards and OMB Bulletin No. 07-04 require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion.



An audit also includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall financial statement presentation.

We believe that our audits provide a reasonable basis for our opinion.

In planning and performing our FY 2012 audit, we considered the Fund's internal control over financial reporting by obtaining an understanding of the Fund's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control over financial reporting. We did not test all controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*.

As part of obtaining reasonable assurance about whether the Fund's FY 2012 financial statements are free of material misstatement, we performed tests of the Fund's compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of the financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 07-04, as amended. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, and contracts applicable to the Fund. However, providing an opinion on compliance with laws, regulations, and contracts was not an objective of our audit and, accordingly, we do not express such an opinion.

Management's written response to the findings identified in our audit and presented in Exhibit I was not subject to the auditing procedures applied in the audit of the Fund's financial statements and, accordingly, we express no opinion on it.

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

KPMG LLP

March 29, 2013

1. Controls Over the Financial Reporting Process Need Improvement

In fiscal year (FY) 2012, the U.S. Department of Labor's (DOL) Office of Workers' Compensation Programs (OWCP) implemented corrective actions to address certain prior year recommendations related to the review of the draft financial statements. Specifically, the OWCP designed and implemented a checklist (referred to as the Reconciliation Checklist) that outlined the requirements for performing a review of the financial information in the draft financial statements. The checklist included procedures for agreeing comparative prior year financial data to the prior year audited statements; verifying financial data that was reported on multiple statements was consistent; reconciling the financial data between the general ledger and subsidiary ledgers; performing a budgetary to proprietary account relationship analysis; and analyzing significant variances between current period and prior period financial information. As a result, we noted certain improvements in financial reporting controls. However, we continued to note the following issues:

Financial Reporting Process. During our review of the Longshore and Harbor Workers' Compensation Act (LHWCA) Fund's FY 2012 draft financial statements, we noted that the Statement of Budgetary Resources (SBR) for FY 2012 and FY 2011 were not presented in conformity with the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*, new reporting guidance. For example, certain required financial statement captions, including "Budget Authority, net," were excluded from the SBR section "Budget Authority and Outlays." The OWCP informed us that they did not present the SBR in conformity with OMB Circular No. A-136 because they believed the excluded information was captured in other sections of the SBR. The OWCP subsequently corrected these presentation errors in the final year-end financial statements.

In addition, during our testing of the presentation of the Statement of Net Cost, we determined that certain benefit expenses reported for section 8(f) and section 18(b) were misclassified. This occurred because the benefit payment summary report used to record the expenses was not configured correctly. As a result, benefit expenses related to section 8(f) were initially understated by approximately \$1 million, while section 18(b) expenses were overstated by the same amount. The OWCP corrected these errors in the final year-end financial statements.

We also noted that certain key financial reporting controls were not performed in a timely manner. For example, the year-end budgetary to proprietary account relationship analysis was not prepared until December 11, 2012. In addition, the OWCP experienced delays in preparing the financial statements at year-end. The draft FY 2012 financial statements were initially due on November 22, 2012; however, the OWCP was not able to complete the initial draft financial statements until December 14, 2012.

During the FY 2012 audit, we also determined that management had not performed an analysis to assess whether certain administrative costs and rehabilitation services paid on behalf of the LHWCA Special Fund were properly accounted for in accordance with Statement of Federal Financial Accounting Standards (SFFAS) No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*. Although this matter was identified and presented to the OWCP management in November 2012, sufficient research to resolve these issues in a timely manner was not performed until February 2013. This occurred primarily because the OWCP did not have a formal process in place to ensure significant financial reporting issues were researched, properly resolved, and documented in a timely manner.

The issues noted above increased the risk that the Fund's financial statements could be misstated or not presented in conformity with U.S. generally accepted accounting principles.

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

- Internal control should generally be designed to assure that ongoing monitoring occurs in the course of normal operations. It is performed continually and is ingrained in the agency's operations. It includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties.
- Internal control should provide reasonable assurance that the objectives of the agency are being achieved relative to reliability of financial reporting, including reports on budget execution, financial statements, and other reports for internal and external use and compliance with applicable laws and regulations.
- 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.

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

Control deficiencies exist 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 design deficiency exists when a control necessary to meet the control objective is missing or an existing control is not properly designed,

so that even if the control operates as designed the control objective is not always met.

Journal Entries. During our FY 2012 audit, we identified certain deficiencies during our testing of a sample of fourteen journal entries recorded in the general ledger for the period October 1, 2011 through September 30, 2012. Specifically, we noted the following exceptions:

- Two journal entries did not accurately reflect the underlying events and transactions. The first journal entry resulted in an overstatement of Benefit Expenses, Other Revenue, and Obligations Incurred of \$132,661. As this error was uncorrected as of September 30, 2012, we included it in our summary of audit misstatements. The second journal entry resulted in an overstatement of Accounts Receivable, net, and Other Liabilities of \$288,720. The OWCP corrected this error as of September 30, 2012.
- Two journal entries related to assessment overpayments were incorrectly posted to Deferred Revenue instead of Other Liabilities and were not detected during the initial supervisory review. These errors were subsequently corrected by management.

The exceptions above were caused by insufficient review of journal entries by the OWCP supervisors to ensure that journal entries were properly prepared and supported before posting to the general ledger.

In addition, we identified two journal entries during our testing over benefit overpayments that were not posted in accordance with the U.S. Standard General Ledger (USSGL). These entries were to record the change in overpayments from claimants in the general ledger but were incorrectly posted to Benefit Expense instead of Other Expenses Not Requiring Budgetary Resources. As a result of these errors, we inspected the remaining ten journal entries used to record the change in overpayments from claimants and noted that they were also not in accordance with the USSGL. These exceptions occurred because management continued to use a general ledger posting model that was not in accordance with the USSGL. Although management acknowledges that changes were required, competing priorities prevented the completion of all necessary corrections of misclassified amounts in the general ledger for FY 2012. There was no impact on the presentation of amounts in the financial statements as a result of these exceptions.

The Standards state:

Internal control should generally be designed to assure that ongoing monitoring occurs in the course of normal operations. It is performed continually and is ingrained in the agency's operations. It includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties.

In addition, the USSGL contains the chart of accounts that provides the basic accounting structure for Federal agencies' general ledger systems. It incorporates both proprietary and budgetary accounts. It also provides the accounting transactions for events occurring throughout the Federal Government. These transactions illustrate the proper proprietary and budgetary entries for each accounting event.

To address the issues above, the OWCP Acting Director should:

- 1) Update the Reconciliation Checklist to include procedures for ensuring new financial reporting requirements are properly incorporated into the financial statements and notes.
- 2) Establish appropriate due dates to ensure key financial reporting controls, such as the budgetary to proprietary account relationship analysis, and the preparation of draft financial statements are completed in a timely manner.
- 3) Re-configure the benefit payment summary report so that the payment data is properly presented in the appropriate expense category, and implement procedures to correct any subsequent misclassification errors resulting from the incorrect configuration of the benefit payment summary report until the report is re-configured.
- 4) Develop and implement a formal process for promptly researching and resolving significant financial reporting issues that are identified. In addition, resolution of each issue should be formally documented and retained to support the financial statements' compliance with U.S. generally accepted accounting principles.
- 5) Provide training to applicable supervisors to ensure they are performing sufficient reviews of journal entries and related documentation before the entries are posted.
- 6) Develop and implement procedures to properly record transactions related to the change in overpayments from claimants in the future.

Management's Response

Management concurs with the recommendations. The Reconciliation Checklist will be updated to include deadlines for monthly, quarterly and year end reporting requirements. The checklist will also be updated to add requirements for verifying the format of the statements with OMB A-136, A-11 and the US SGL. The program office has agreed to reconfigure the summary report to properly reflect the payment data for each section of the LHCWA, by March 31, 2013.

OWCP has been making a concerted effort to recruit and hire new employees with extensive knowledge of the US SGL, as well as, expertise in reviewing journal entries and the associated supporting documentation. It is management's opinion that these efforts will improve our controls over journal entries. Additionally, a list of all journal entries will be compiled by month, quarter and year end to ensure that all entries are recorded timely.

Auditors' Response

We will conduct follow-up procedures in FY 2013 to determine whether corrective actions have been developed and implemented.

2. Controls over the Assessments Subsidiary Ledger Need Improvement

During the FY 2012 audit, we performed testing over the LHWCA Special Fund's assessments receivables. For one of the three assessment overpayment samples tested, the accounts receivable balance in the detailed subsidiary ledger exceeded the balance confirmed by the insurance carrier or self-insured employer. As a result, OWCP management reviewed the accounts receivable subsidiary ledger and determined that the assessment overpayment balances for 22 carriers and self-insured employers were overstated by \$92,660. OWCP subsequently corrected these errors for the year ended September 30, 2012.

These exceptions occurred because the OWCP did not record a final assessment amount in the accounts receivable subsidiary ledger for those carriers that did not receive a second assessment bill. This resulted in an error in the calculation of ending balances. Further, the OWCP did not have any policies or procedures that required someone other than the accountant who recorded the assessments activity to periodically review the accounts receivable subsidiary ledger to ensure amounts were correctly recorded.

Without adequate management review there is an increased risk that significant errors could occur and not be detected and corrected by management in a timely manner.

The Standards state:

Internal control should generally be designed to assure that ongoing monitoring occurs in the course of normal operations. It is performed continually and is ingrained in the agency's operations. It includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties.

To address the issues above, the OWCP Acting Director should develop and implement policies and procedures that require someone other than the preparer to periodically review the subsidiary ledger to ensure all required amounts, including the final assessment, are accurately recorded for the carriers.

Management's Response

Management concurs with the recommendations. Currently, assessments are billed in January and July of the program year. In accordance with this schedule, the Lead Accountant will review the subsidiary ledger subsequent to each billing cycle to ensure that the amounts are accurately recorded for the carriers. As part of this review, the Lead Accountant will select a sample of carriers from the final assessment and verify the balances with the program office to provide additional assurance that final assessments were correctly recorded even in situations where the carrier did not

receive a second assessment bill. Upon completion of each review, the Lead Accountant will provide the results to the Accounting Officer for final review and signature. Management agrees to amend the procedures to include this review and verification.

Throughout the year, it may be possible for an assessment bill to be amended. When this occurs, the program office has agreed to send a copy of the amended bill to the Accountant as an email attachment. This will serve as the supporting documentation for the change in the subsidiary ledger. The program office will amend their procedures to include this process.

Auditors' Response

We will conduct follow-up procedures in FY 2013 to determine whether corrective actions have been developed and implemented.

The following table provides the fiscal year 2012 status of all recommendations included in the Independent Auditors' Report on the U.S. Department of Labor's (DOL) Longshore and Harbor Workers' Compensation Act Special Fund's fiscal year 2011 Financial Statements, Report No. 22-12-004-04-432 (March 1, 2012).

Fiscal Year (FY) 2011 Finding	FY Finding Originated	FY 2011 Recommendations	FY 2012 Status
Internal Controls Over the Financial Reporting Process Need Improvement	2010 (as a Material Weakness)	Recommendation: Design and implement policies and procedures that require a comprehensive and detailed review of all financial information in the draft financial statements. The policies and procedures should include:	
		a. Specific procedures for agreeing comparative prior year financial data to the prior year audited statements;	Closed
		b. Comparing financial data reported on the different statements to ensure accuracy and consistency;	Closed
		c. Reconciling the financial data between the general ledger and subsidiary ledgers, including the case management system, to ensure existence, completeness, and accuracy of financial data reported;	Open (See Exhibit I, comment no. 1)
		d. Performing a budgetary to proprietary account relationship analysis and resolving identified variances; and	Closed
		e. Analyzing significant variances between current period and prior period financial information.	Closed
		Recommendation: Develop monitoring controls to ensure that sufficient supervisory review controls over journal entries and the related documentation are being performed before the journal entries are posted to the general ledger.	Open (See Exhibit I, comment no. 1)

**LONGSHORE AND HARBOR WORKERS'
COMPENSATION ACT SPECIAL FUND**

Balance Sheets

September 30, 2012 and 2011

Assets	2012	2011
Intra-governmental assets:		
Funds with U.S. Treasury (Note 1c and Note 2)	\$ 8,617	\$ 5,164
Investments, net (Note 1d and Note 3)	<u>55,656,000</u>	<u>58,170,000</u>
Total intra-governmental assets	55,664,617	58,175,164
Accounts receivable, net (Note 1e and Note 4)	<u>2,847,573</u>	<u>1,762,823</u>
Total assets	<u><u>\$ 58,512,190</u></u>	<u><u>\$ 59,937,987</u></u>
Liabilities and Net Position		
Liabilities:		
Accrued benefits payable (Note 1f)	\$ 1,314,535	\$ 655,439
Deferred revenue (Note 1h)	30,778,861	30,343,942
Other liabilities (Note 1g and Note 5)	<u>6,376,579</u>	<u>7,425,371</u>
Total liabilities	<u>38,469,975</u>	<u>38,424,752</u>
Net position:		
Cumulative results of operations -- Other	<u>20,042,215</u>	<u>21,513,235</u>
Total liabilities and net position	<u><u>\$ 58,512,190</u></u>	<u><u>\$ 59,937,987</u></u>

See accompanying notes to financial statements.

**LONGSHORE AND HARBOR WORKERS'
COMPENSATION ACT SPECIAL FUND**

Statements of Net Cost

Years ended September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Special fund net cost of operations:		
Second injury compensation, Section 8(f)	\$ 112,788,457	\$ 112,862,602
Wage increase compensation, Section 10(h)	1,340,972	1,388,781
Compensation payments for self-insured employer in default, Section 18(b)	7,056,558	6,303,804
Defaulted self-insured employer compensation payments backed by securities, Section 32(a)	800,829	967,854
Rehabilitation services, Section 39(c)	2,322,488	2,822,065
Medical services, Section 7(e)	3,975	—
Net cost of operations	<u>\$ 124,313,279</u>	<u>\$ 124,345,106</u>

See accompanying notes to financial statements.

**LONGSHORE AND HARBOR WORKERS'
COMPENSATION ACT SPECIAL FUND**

Statements of Changes in Net Position
Years ended September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Cumulative results of operations, beginning	\$ 21,513,235	\$ 21,119,180
Budgetary financing sources:		
Transfers in/out without reimbursement (Note 6)	(2,119,986)	(2,118,307)
Non-exchange revenues (Note 1i):		
Interest	18,628	24,791
Fines and penalties	456,980	472,110
Assessments	124,486,637	126,360,567
Total non-exchange revenues	<u>124,962,245</u>	<u>126,857,468</u>
Total financing sources	122,842,259	124,739,161
Net cost of operations	<u>(124,313,279)</u>	<u>(124,345,106)</u>
Cumulative results of operations and net position, end of period	<u>\$ 20,042,215</u>	<u>\$ 21,513,235</u>

See accompanying notes to financial statements.

**LONGSHORE AND HARBOR WORKERS'
 COMPENSATION ACT SPECIAL FUND**

Statements of Budgetary Resources
 Years ended September 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Budgetary Resources:		
Unobligated balance, brought forward, October 1	\$ 58,068,382	\$ 59,983,697
Budget Authority (mandatory)		
Appropriations (assessments, mandatory)	123,860,636	124,644,808
Spending authority from offsetting collections	21,751	29,609
Total budgetary resources	<u>\$ 181,950,769</u>	<u>\$ 184,658,114</u>
Status of Budgetary Resources:		
Obligations incurred (Note 7)	127,052,030	126,589,732
Unobligated balances, end of year:		
Exempt from apportionment	<u>54,898,739</u>	<u>58,068,382</u>
Total status of budgetary resources	<u>\$ 181,950,769</u>	<u>\$ 184,658,114</u>
Change in Obligated Balance:		
Unpaid obligations, brought forward, October 1	\$ 655,439	\$ 2,478,421
Obligations incurred	127,052,030	126,589,732
Less: Outlays (gross)	<u>(126,392,933)</u>	<u>(128,412,714)</u>
Obligated balance, end of year	<u>\$ 1,314,536</u>	<u>\$ 655,439</u>
Budget Authority and Outlays, Net:		
Budget authority, gross (mandatory)	\$ 123,882,387	\$ 124,674,417
Actual offsetting collections (mandatory)	<u>(21,751)</u>	<u>(29,609)</u>
Budget authority, net (mandatory)	<u>\$ 123,860,636</u>	<u>\$ 124,644,808</u>
Outlays, gross (mandatory)	126,392,933	128,412,714
Actual offsetting collections (mandatory)	<u>(21,751)</u>	<u>(29,609)</u>
Outlays, net (mandatory)	<u>\$ 126,371,182</u>	<u>\$ 128,383,105</u>

See accompanying notes to financial statements.

**LONGSHORE AND HARBOR WORKERS'
COMPENSATION ACT SPECIAL FUND**

Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(1) Summary Of Significant Accounting Policies

The principal accounting policies which have been followed in preparing the accompanying financial statements for the Fund are set forth below.

(a) Reporting Entity

The Longshore and Harbor Workers' Compensation Act (LHWCA) Special Fund (the Fund) is administered by the Department of Labor (DOL), Office of Workers' Compensation Programs (OWCP), Division of Longshore and Harbor Workers' Compensation program (DLHWC). The DLHWC has direct responsibility for administration of the Fund. The Fund offers compensation, and in certain cases, medical care payments to employees disabled from injuries which occurred on the navigable waters of the United States, or in adjoining areas used for loading, unloading, repairing, or building a vessel. The Fund also extends benefits to dependents if any injury resulted in the employee's death.

Additionally, the LHWCA [Section 10(h)] provides annual wage increase compensation (cost of living adjustments). Fifty percent of this annual wage increase for pre-1972 compensation cases is paid by the annual assessment. The remaining fifty percent is paid by the Federal Employees' Compensation Act's Special Benefit Fund through Federal Appropriations.

(b) Basis of Accounting and Presentation

These financial statements present the financial position, net cost of operations, changes in net position and budgetary resources of the Fund, in accordance with U.S. generally accepted accounting principles and the form and content requirements of Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*. These financial statements have been prepared from the books and records of the Fund. These financial statements are not intended to present, and do not present, the full cost of the

**LONGSHORE AND HARBOR WORKERS'
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Notes to the Financial Statements

Years ended September 30, 2012 and 2011

LHWCA Program (the Program). In addition to the Fund costs presented in these statements, the full cost of the Program would include certain direct costs of OWCP in the form of salaries and expenses for administration of the Program and allocated costs of OWCP and other DOL agencies incurred in support of the Program. The full cost of the Program is included in the DOL consolidated financial statements and related notes. The Fund is considered a fiduciary activity of DOL and is properly disclosed and reported in the consolidated financial statements of DOL as a fiduciary fund.

U.S. generally accepted accounting principles encompass both accrual and budgetary transactions. Under accrual accounting, revenues are recognized when earned, and expenses are recognized when a liability is incurred. Budgetary accounting facilitates compliance with legal constraints on, and controls over, the use of Federal funds. These financial statements are different from the financial reports, also prepared by management pursuant to OMB directives, used to monitor the Fund's use of budgetary resources.

(c) Funds with U.S. Treasury

The Fund's cash receipts and disbursements are processed by the U.S. Treasury. Funds with U.S. Treasury represent obligated balances available to pay current liabilities and finance authorized purchase commitments.

(d) Investments, Net

Investments in U.S. Government securities are reported at cost, net of unamortized premiums or discounts, which approximate market value. Premiums or discounts are amortized on a straight-line basis, which approximates the effective interest method. The Fund's intent is to hold investments to maturity, unless they are needed to finance claims or otherwise sustain the operations of the Fund. No provision is made for unrealized gains or losses on these securities because they are held to maturity. A portion of these investments is available for payment of compensation and medical benefits to covered employees of the defaulted companies.

**LONGSHORE AND HARBOR WORKERS'
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Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(e) *Accounts Receivable, Net*

The amounts due as receivables are stated net of an allowance for uncollectible accounts. The allowance is estimated based on past experience in the collection of the receivables and an analysis of the outstanding balances. Accounts receivable are comprised of assessments receivable and Fund benefit overpayments made to individuals primarily from amended compensation orders and corrections of payment computations.

(f) *Accrued Benefits Payable*

The Fund provides compensation and medical benefits for work related injuries to workers in certain maritime employment. The Fund recognizes a liability for disability benefits payable to the extent of unpaid benefits applicable to the current period. Ultimate responsibility for payment of such claims rests with the employer organizations.

(g) *Other Liabilities*

Other liabilities are comprised primarily of amounts received by the Fund from defaulted employers which are being held as security by authority of Section 32 of the LHWCA. These funds and investments are available for compensation and medical benefits to covered employees of the defaulted companies. Management estimates that these funds and investments held will be sufficient to cover the future benefits associated with the covered employees. Also included in other liabilities are assessment overpayments by insurance carriers or self-insured employers which are to be refunded at the insurance carrier or self-insured employers' request or applied to reduce future assessments.

(h) *Deferred Revenue*

Deferred revenue represents the portion of assessment revenue extending beyond September 30, the Fund's accounting year end. The annual assessments cover a calendar year and, accordingly, revenue extending beyond September 30 has been deferred. Deferred revenue reported on the balance sheets is considered "Other Liabilities" under OMB Circular A-136.

**LONGSHORE AND HARBOR WORKERS'
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Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(i) Financing Sources - Non-Exchange Revenue

Non-exchange revenues arise from the Federal government's power to demand payments from and receive donations from the public.

The Fund's primary source of revenue is annual assessments levied on insurance carriers and self-insured employers. Assessments are recognized as non-exchange revenue when due. Additional assessments may result from the application of audit procedures on reported carrier data. These assessments are recognized as revenues when final agreement is reached with the carriers. The Fund receives interest on Fund investments and on Federal funds in the possession of non-Federal entities. The Fund also receives revenue from fines and penalties assessed in accordance with various sections of the LHWCA.

(j) Reclassifications

The FY 2011 statements were reclassified to conform to the FY 2012 financial statement presentation requirements, including changes in the presentation of the Statement of Budgetary Resources and the reclassification of Audit Recoveries to Assessments on the Statement of Changes in Net Position and the related verbiage in Management's Discussion and Analysis.

**LONGSHORE AND HARBOR WORKERS'
 COMPENSATION ACT SPECIAL FUND**

Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(2) Funds with U.S. Treasury

Funds with U.S. Treasury at September 30, 2012 and 2011 consisted of cash deposits of \$8,617 and \$5,164, respectively. These cash deposits at September 30, 2012 and 2011 included \$419 and \$396, respectively, which are being held as security by authority of Section 32 of the LHWCA. These funds relate to the default of self-insured employers, and are available for payment of compensation and medical benefits to covered employees of the defaulted companies.

Funds with U.S. Treasury at September 30, 2012 consisted of the following:

<u>(In Dollars)</u>	Entity Assets			Total Entity Assets	Non-entity Assets	Total
	Unobligated Balance Available	Unobligated Balance Unavailable	Obligated Balance Not Yet Disbursed			
Trust Fund	\$ —	—	8,617	8,617	—	\$ 8,617

Funds with U.S. Treasury at September 30, 2011 consisted of the following:

<u>(In Dollars)</u>	Entity Assets			Total Entity Assets	Non-entity Assets	Total
	Unobligated Balance Available	Unobligated Balance Unavailable	Obligated Balance Not Yet Disbursed			
Trust Fund	\$ —	—	5,164	5,164	—	\$ 5,164

**LONGSHORE AND HARBOR WORKERS'
 COMPENSATION ACT SPECIAL FUND**

Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(3) Investments, Net

Investments at September 30, 2012 and 2011 consisted of the following:

		September 30, 2012			
<u>(In Dollars)</u>	<u>Face Value</u>	<u>Premium (Discount)</u>	<u>Net Value</u>	<u>Market Value</u>	
Intragovernmental securities:					
Non-marketable:					
Par value	\$ 55,656,000	—	55,656,000	55,656,000	
		September 30, 2011			
<u>(In Dollars)</u>	<u>Face Value</u>	<u>Premium (Discount)</u>	<u>Net Value</u>	<u>Market Value</u>	
Intragovernmental securities:					
Non-marketable:					
Par value	\$ 58,170,000	—	58,170,000	58,170,000	

Investments of \$6,180,100 and \$6,614,223 at September 30, 2012 and 2011, respectively, are restricted assets that are being held as security by authority of Section 32 of the LHWCA. Investments at September 30, 2012 and 2011 consist of overnight securities. Investments at September 30, 2012 bear an interest rate of 0.05% compared to an interest rate of 0.00% for September 30, 2011. Interest rates on securities bought and sold during FY 2012 ranged from 0.00% to 0.12% compared to 0.00% to 0.18% for FY 2011.

**LONGSHORE AND HARBOR WORKERS'
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Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(4) Accounts Receivable, Net

Accounts receivable at September 30, 2012 and 2011 consisted of the following:

<u>(In Dollars)</u>	<u>2012</u>	<u>2011</u>
Benefit overpayments	\$ 1,688,118	\$ 1,695,591
Assessments receivable	1,637,123	499,129
Less: allowance for doubtful accounts	<u>(477,668)</u>	<u>(431,897)</u>
Total accounts receivable from the public, net	<u>\$ 2,847,573</u>	<u>\$ 1,762,823</u>

Assessments receivable represent the unpaid annual assessments. Accounts receivable from benefit overpayments to claimants arise primarily from amended compensation orders and corrections of payment computations. These receivables are primarily recovered by partial and total withholding of benefit payments.

Changes in the allowance for doubtful accounts during FY 2012 and FY 2011 consisted of the following:

<u>(In Dollars)</u>	<u>2012</u>			
	<u>Allowance October 1, 2011</u>	<u>Write Offs</u>	<u>Bad Debt</u>	<u>Allowance September 30, 2012</u>
Entity assets:				
Benefit overpayments	\$ (429,402)	-	(41,524)	\$ (470,926)
Assessment receivable	<u>(2,495)</u>	<u>-</u>	<u>(4,247)</u>	<u>(6,742)</u>
	<u>\$ (431,897)</u>	<u>-</u>	<u>(45,771)</u>	<u>\$ (477,668)</u>
<u>(In Dollars)</u>	<u>2011</u>			
	<u>Allowance October 1, 2010</u>	<u>Write Offs</u>	<u>Bad Debt</u>	<u>Allowance September 30, 2011</u>
Entity assets:				
Benefit overpayments	\$ (504,212)	-	74,810	\$ (429,402)
Assessment receivable	<u>(45,002)</u>	<u>-</u>	<u>42,507</u>	<u>(2,495)</u>
	<u>\$ (549,214)</u>	<u>-</u>	<u>117,317</u>	<u>\$ (431,897)</u>

**LONGSHORE AND HARBOR WORKERS'
COMPENSATION ACT SPECIAL FUND**

Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(5) Other Liabilities

Other liabilities at September 30, 2012 and 2011 consisted of the following liabilities:

<u>(In Dollars)</u>	<u>2012</u>	<u>2011</u>
Other liabilities:		
Assessment overpayments by carriers	\$ 196,060	\$ 810,752
Defaulted employer liability:		
Held in investments	6,180,100	6,614,223
Held in cash	419	396
	<u>6,180,519</u>	<u>6,614,619</u>
Total other liabilities	<u>\$ 6,376,579</u>	<u>\$ 7,425,371</u>

Assessment overpayments by carriers are to be refunded upon request or applied to reduce future assessments.

Defaulted employer liability relates to cash and investments held by the Fund which are being held as security by authority of Section 32 of the LHWCA. These funds are available for compensation and medical benefits to covered employees of the defaulted companies.

(6) Transfers to OWCP

The Fund is required to reimburse OWCP (a related entity within the Department of Labor) for rehabilitation services provided to eligible claimants and certain direct expenses associated with administrative support of the Fund. Approved transfers out to the OWCP were \$2,119,986 in FY 2012 and \$2,118,307 in FY 2011. Transfers are made from the Special Fund in accordance with sections 39(c), 44(d), and 44(j) of the LHWCA.

**LONGSHORE AND HARBOR WORKERS'
 COMPENSATION ACT SPECIAL FUND**

Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(7) Status of Budgetary Resources

(a) Apportionment Categories of Obligations Incurred

<u>(In Dollars)</u>	<u>2012</u>	<u>2011</u>
Direct obligations:		
Exempt from apportionment	\$ 127,052,030	\$ 126,589,732

(b) Explanation of Differences Between the Statement of Budgetary Resources and the Budget of the United States Government

A reconciliation of budgetary resources, obligations incurred and outlays, as presented in the Statement of Budgetary Resources to amounts included in the Budget of the United States Government for the year ended September 30, 2011 is shown below:

<u>(Dollars in Millions)</u>	<u>2011</u>		
	<u>Budgetary Resources</u>	<u>Obligations Incurred</u>	<u>Outlays</u>
Statement of Budgetary Resources - LHWCA	\$ 185	\$ 127	\$ 128
Statement of Budgetary Resources - DCCA, reported separately	14	10	10
Adjustments included in the Statement of Budgetary Resources	2	2	1
Total Statement of Budgetary Resources	<u>201</u>	<u>139</u>	<u>139</u>
Budget of the United States Government	\$ <u>201</u>	\$ <u>139</u>	\$ <u>139</u>

**LONGSHORE AND HARBOR WORKERS'
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Notes to the Financial Statements

Years ended September 30, 2012 and 2011

(8) Reconciliation of Budgetary Resources Obligated to Net Cost of Operations

	2012	2011
Resources used to finance activities		
Budgetary resources obligated		
Obligations incurred	\$127,052,030	\$126,589,732
Total resources used to finance activities	127,052,030	126,589,732
 Resources used to finance items not part of the net cost of operations		
Resources that funded expenditure transfers	(2,119,986)	(2,118,307)
Total resources used to finance items not part of the net cost of operations	(2,119,986)	(2,118,307)
Total resources used to finance the net cost of operations	124,932,044	124,471,425
 Components of net cost of operations that will not require or generate resources in current period		
Components not requiring or generating resources		
Revaluation of assets and liabilities	41,524	(74,810)
Other	(660,289)	(51,509)
Total components of net cost of operations that will not require or generate resources in current period	(618,765)	(126,319)
Net cost of operations	\$124,313,279	\$124,345,106

(9) Concentration of Risk

The Fund makes assessments to authorized insurers and self-insurers one year at a time for current expenses; there is no reserve for future Fund obligations. In keeping with the requirement of Section 44 of the LWHCA, obligations are paid as they are incurred. Assessments are based on compensation and medical benefits paid in the prior calendar year.

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