



Employee Benefits Security Administration

Performance Audit of the Thrift Savings Plan Loans Process

May 9, 2017

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EXECUTIVE SUMMARY

Members of the Federal Retirement Thrift Investment Board
Washington, D.C.

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As a part of the U.S. Department of Labor Employee Benefits Security Administration (EBSA) Fiduciary Oversight Program, we conducted a performance audit of the Thrift Savings Plan (TSP) loans process. We performed our fieldwork from August 16, 2016 through February 10, 2017, primarily at the Federal Retirement Thrift Investment Board's Staff's (Agency) headquarters in Washington, DC. Our scope period for testing was October 1, 2015 through September 30, 2016.

We conducted this performance audit in accordance with the performance audit standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and the American Institute of Certified Public Accountants' *Standards for Consulting Services*. *Government Auditing Standards* require that we plan and perform the audit to obtain sufficient, appropriate audit evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Criteria used for this engagement are defined in EBSA's *Thrift Saving Plan Fiduciary Oversight Program*, which includes United States Code (USC) Title 5, Chapter 84, and Code of Federal Regulations (CFR) Title 5, Chapter VI.

The objectives of our audit over the TSP loans process were to:

- a Determine whether the Agency implemented certain procedures to (1) process TSP loan transactions promptly and accurately in individual participant accounts and in the appropriate investment fund(s); (2) disburse TSP loans in accordance with regulations and participant authorizations; (3) limit participation in the TSP loan program to participants who meet eligibility criteria; and (4) accurately record loan activity in the TSP accounting records.

- Test compliance of the TSP loans process with 5 USC 8433(g) and 8439 and 5 CFR 1655.2, 1655.2(a), 1655.4, 1655.6, 1655.9 (a -d), 1655.13, 1655.14, 1655.14(f), 1655.15, 1655.16, 1655.18b, and 1655.21.

We present three new recommendations, all of which address other controls. Fundamental control recommendations address significant¹ procedures or processes that have been designed and operate to reduce the risk that material intentional or unintentional processing errors could occur without timely detection or that assets are inadequately safeguarded against loss. Other control recommendations address procedures or processes that are less significant than fundamental controls. All recommendations are intended to strengthen the TSP loans process. The Agency should review and consider these recommendations for timely implementation. Section III.C presents the details that support the current year findings and recommendations.

Based upon the performance audit procedures conducted and the results obtained, we have met our audit objectives. We determined that for the period October 1, 2015 through September 30, 2016, the Agency implemented certain procedures to (1) process TSP loan transactions promptly and accurately in individual participant accounts and in the appropriate investment fund(s); (2) disburse TSP loans in accordance with regulations and participant authorizations; (3) limit participation in the TSP loan program to participants who meet eligibility criteria; and (4) accurately record loan activity in the TSP accounting records. As a result of our compliance testing, we did not identify any instances of noncompliance with 5 USC 8433(g) or 8439; or 5 CFR 1655.2, 1655.2(a), 1655.4, 1655.6, 1655.9(a-d), 1655.13, 1655.14, 1655.14(f), 1655.15, 1655.16, 1655.18b, or 1655.21. However, as indicated above, we noted internal control weaknesses in certain areas of the TSP loans process.

We noted no prior recommendations requiring follow-up during our performance audit.

The Agency's response to the recommendations, including the Executive Director's formal reply, is included as an appendix within the report (Appendix A). The Agency concurred with the recommendations.

This performance audit did not constitute an audit of the TSP's financial statements in accordance with *Government Auditing Standards*. KPMG was not engaged to, and did not render an opinion

¹ *Government Auditing Standards* section 6.04 defines significance in the context of a performance audit.

on the Agency's internal controls over financial reporting or over financial management systems. KPMG cautions that projecting the results of this audit to future periods is subject to the risks that controls may become inadequate because of changes in conditions or because compliance with controls may deteriorate.

While we understand that this report may be used to make the results of our performance audit available to the public in accordance with *Government Auditing Standards*, this report is intended for the information and use of the U.S. Department of Labor Employee Benefits Security Administration, Members of the Federal Retirement Thrift Investment Board, and Agency management. The report is not intended to be, and should not be, used by anyone other than these specified parties.

KPMG LLP

May 9, 2017

I. BACKGROUND OF THE TSP AND THE LOANS PROCESS

A. The Thrift Savings Plan

Public Law 99-335, the Federal Employees' Retirement System Act of 1986 (FERSA), as amended, established the Thrift Saving Plan (TSP). The TSP is the basic component of the Federal Employees' Retirement System (FERS) and provides a Federal (and, in certain cases, state) income tax deferral on employee contributions and related earnings. The TSP is available to Federal and Postal employees, members of Congress and certain Congressional employees, and members of the uniformed services. The TSP began accepting contributions on April 1, 1987, and as of September 30, 2016, had approximately \$485 billion in assets and approximately 5.0 million participants².

The FERSA established the Federal Retirement Thrift Investment Board (the Board) and the position of Executive Director. The Executive Director manages the TSP for its participants and beneficiaries. The Board's Staff (Agency) is responsible for administering TSP operations.

B. Overview of the TSP Loans Process³

1. Loan Requirements – Borrowing Rules

Actively employed TSP participants may borrow a part of the amount that they have contributed along with related earnings. Retired, separated, or employees in non-pay status at the time of the loan are not eligible to borrow funds from their contributions. Agency automatic amounts, first conversion amounts, matching amounts, and related earnings on agency-matched amounts cannot be borrowed.

TSP loans can be obtained for the purchase of a primary residence or for general purposes. Documentation of the need for a general purpose loan is not required, but certain documentation is required for a residential loan such as copies of the purchase contract, settlement sheet, or other documentation to prove the cost and address of the residence. Prior to the distribution of a loan, documentation is reviewed to determine if all information applicable to the loan is appropriate and complete.

² Source: Minutes of October 31, 2016, Federal Retirement Thrift Investment Board meeting, posted on www.fitib.gov.

³ Sources: TSP Loan Booklet – *Loans*, February 2013; TSP Bulletin 05-16, *Processing Thrift Savings Plan Loan Payments in the TSP Record Keeping System*; *Agency Loans Policy*; and *Agency Loans Procedures*.

Loan applicants specify the amount of time they want to repay the loan in years and months, but not more than 5 years or 60 months for a general purpose loan or 15 years or 180 months for a residential loan. Both the EX AG Image system (AG) (for paper loan applications received) and the web interface (for loan applications completed on-line) perform edit checks to ensure that the following key requirements are met:

- The participant must be an active Federal employee or uniformed service member;
- The participant must have at least \$1,000 of his/her own contributions, including related earnings, in his/her account as the smallest amount a participant can borrow is \$1,000;
- The loan must comply with Internal Revenue Code (IRC)⁴ requirements such that the borrowed amount cannot exceed the lesser of the following: (1) 50 percent of a participant's total vested account balance (including any outstanding loan balance) or \$10,000, whichever is greater, minus any outstanding loan balance; or (2) \$50,000 less the participant's highest outstanding loan balance, if any, during the last 12 months. Therefore, a participant's total outstanding loan principal balance may not exceed \$50,000 at any given time. In addition, Code of Federal Regulations Title 5, Part 1655.6(b) requires that the borrowed amount cannot exceed contributions and earnings in the participant's account, not including any outstanding loan balance.
- If the participant has a civilian account and a uniformed service account, the combined account balances and loan balances will be used when meeting IRC requirements 2 and 3.
- Participants cannot have two loans of the same type outstanding at the same time in the same account type (i.e., civilian account vs. uniformed services account) but are allowed to have one general purpose loan and one residential loan outstanding simultaneously.
- Participants who pay off their TSP loans are not eligible to apply for another loan of the same type for 60 calendar days after full repayment.

2. Loan Application Process

Participants complete Form TSP-20, *Loan Application*, to apply for a TSP Loan. The loan application can be requested through the TSP website, the ThriftLine (TSP's automated telephone service), the participant's Federal agency/service personnel office, or a Participant Support Representative (PSR) at the TSP call center. Participants may also apply for a loan on-line, via

⁴ IRC Title 26 Chapter 72(p)(2)(A).

the TSP website, and depending on their retirement system coverage, marital status, the type of loan, and method selected for receipt of funds, may complete the loan process on-line.

Paper Loan Requests

The completed paper loan applications (Form TSP-20) are mailed or faxed directly to the TSP Service Bureau for scanning and data entry. The TSP Service Bureau is responsible for providing efficient, accurate, and timely processing of these loans. The TSP Service Bureau is charged with reviewing and approving loan agreement packages for all applications that are not or cannot be submitted via the TSP website. Once the TSP Service Bureau receives the completed loan package from the participant, if it is a residential loan, the TSP Service Bureau reviews the supporting documentation supplied in the loan package to verify that all required documentation has been received. The following explains the specific requirements for the two types of loans:

- General purpose loan - Documentation of the reason requested is not required.
- Residential loan - A primary residence can be a house, condominium, a share in a cooperative housing corporation, a mobile home, townhouse, a boat, or a recreational vehicle, but it must be used as the participant's primary residence. The participant must be either purchasing an existing residence (whole or in part) or constructing a new residence. A loan may not be used for refinancing an existing mortgage or for renovations.

Upon receipt of the loan application and supporting documentation by the TSP Service Bureau, a TSP operator scans the received forms and documents into AG. AG handles the workflow and document storage requirements for the TSP system by facilitating the processing (including manual data entry) of TSP forms and correspondence. The Automatic Data Correction (ADC) tool within AG scans all paper loan applications received for completeness and accuracy of data and obvious errors. The ADC tool performs various edit checks on the applications received to determine whether any suspected errors or discrepancies exist. This process includes verification of the participant's identity as the ADC tool matches the applicant information to information on record for the applicant's TSP account number. If suspected errors or discrepancies exist, they are highlighted for the data entry operator to determine whether any errors occurred. If the data imaged matches the data on the forms, the data entry operator forwards the forms to quality control (QC). If data imaged does not match the form, or is missing or invalid, and the data entry operator is unable to correct, identify, or determine what information was entered on the loan application

form, the form is rejected or sent to quality control (QC) review for a more experienced operator to review the information. If a QC reviewer cannot determine the information on the participant's form, the form is subsequently rejected and sent back to the participant for correction and resubmission. AG rejects forms that contain errors and processes a reject notice that is mailed to the participant. Resubmitted applications are reprocessed in the same manner as initial applications going through the initial data entry checks along with a final QC review.

If the applications are determined to be free of errors, the loan transaction information from the loan applications is transmitted from AG into OMNI during the nightly unified processing cycle. Also during the unified nightly processing cycle, OMNI, the host record keeping processor in the TSP system, performs additional edit checks on the transaction information from the loan application and generates a Form TSP-21-G or Form TSP-21-R, *Loan Agreement*, if the system edit checks are passed. Some edit checks which the OMNI system performs include verifying that the participant is currently active (or in pay status), determining if sufficient funds exist within the participant's account (minimum of \$1,000) to process the loan, ensuring a loan was not closed within 60 days if paid normally or within 365 days of a taxable distribution, and ensuring that the participant does not currently have outstanding loans of the same type (general purpose/residential). A Form TSP-21-G is generated from OMNI for a general purpose loan and a Form TSP-21-R is generated from OMNI for a residential loan. Each agreement is preprinted with pertinent loan data, including the loan number and participant information, and is mailed to the participant for completion.

Both types of loan agreements denote the loan amount requested, the interest rate⁵, loan payment period requested, the number of loan payments, the amount of each loan payment, the total interest charge, and the total payment amount. The participant must complete the loan agreement by signing and returning the Form TSP-21-R or Form TSP-21-G, provide any other required documentation (such as residential documentation), and return the forms and completed documentation to the TSP Service Bureau before the expiration date located at the top of the agreement. The participant's signature on the loan agreement must be notarized. A loan request not completed by its expiration date expires, and the participant is required to submit a new application for loan (Form TSP-20).

⁵ Interest over the life of the loan is calculated using the latest available TSP Government Securities Investment Fund (G Fund) rate at the time the participant's application is processed.

If the participant has requested a residential loan, in addition to signing the Form TSP-21-R as stated above, the participant also must provide copies of the purchase contract, settlement sheet, or other documents to show the cost and address of the residence, or additional documentation needed depending on the type of residence being purchased.

If the participant is a married FERS employee or a married uniformed services member, spousal consent to the loan by signing the loan agreement is required; for married Civil Service Retirement System (CSRS) participants, the TSP is required to notify the spouse when the participant applies for a loan. In certain instances, a FERS or CSRS participant may receive a spousal waiver if he/she can show that the spouse's whereabouts is unknown; additionally, a FERS or uniformed service participant may receive a spousal waiver if exceptional circumstances make it inappropriate to secure the spouse's consent.

All loan agreements sent to the TSP Service Bureau are scanned into AG and sent through the same process as noted for a loan application. Additional edit checks are performed on the loan agreements to verify their accuracy and completeness. The system or a QC reviewer then determines whether a loan should be approved. In addition, the documentation for a residential loan is reviewed by a QC reviewer to ensure sufficiency before the loan agreement can be processed.

Loan agreements for CSRS participants are sent to OMNI marked with a two-day hold, to allow time for spousal notification, if required. All successful transactions are sent to OMNI for verification and nightly processing where additional edit checks are performed to ensure the participant is still eligible to receive a general purpose or residential loan based on eligibility criteria.

Electronic Loan Requests

Participants can complete loan applications via the TSP web interface to the OMNI system. The TSP web interface performs various edits on the data that the participants enter. Participants are alerted to any detected errors on-line and cannot submit the application without correcting the errors. Successful submission of the on-line loan application results in the immediate generation of a loan agreement provided it passes the additional OMNI edit checks previously discussed. In these cases, once the loan applications are approved, the loan agreements are displayed on the participants' computer screen. If the participant qualifies for a general purpose loan, is not married, and elects to have the loan payment sent via check to the address on record, the participant is able

to submit the loan request completely on-line. Participants whose loans were approved on-line can print out their forms from the TSP website. Participants who are not eligible to complete their loan agreements on-line must print, complete, and mail or fax them to the TSP Service Bureau for processing.

3. Loan Disbursement and Payment

Once the loan has been approved, the loan is scheduled for disbursement at the lesser of the amount in the loan agreement or what is available upon disbursement based on the market value of the participant's investments. OMNI is configured to automatically decrease the loan amount if a change in market value has caused the loan amount to exceed the available balance in the participant's account. The TSP disburses loans either through an electronic funds transfer (EFT) or by check to the participant's address on record, as indicated by the participant. The loan principal is disbursed from that portion of the account represented by employee contributions and attributable earnings, pro rata from each TSP Fund in which the account is invested and pro rata from tax-deferred and tax-exempt balances. The OMNI system generates a confirmation notice that is mailed to the participant the same day or within one business day of the loan disbursement. If the loan is disbursed for a lesser amount than in the loan agreement, the confirmation notice informs the participant of the change.

Prior to and after disbursement of a loan, participants can access the terms of their loans via the TSP web interface. Participants may reamortize their loans at any time in order to lower their loan payments or to change their term of repayment. However, any loan reamortized must still comply with TSP requirements for a maximum 5 year loan term for general purpose loans and a 15 year loan term for residential loans.

A \$50 fee is charged for each new loan. The fee is automatically deducted from the proceeds of the loan at disbursement and is posted to the TSP's general ledger on a daily basis from the TSP 3405, *Investment True-Up of Trade Report: OmniPay Loan Disbursements (Actuals)*.

The Agency maintains an overall general ledger system, Sage, and a separate general ledger system for the TSP, Savantage. OMNI interfaces with Savantage to transfer loan disbursement data. Manual entries are recorded daily in Sage to transfer loan activity on a summary level from OMNI. The Office of the Chief Financial Officer performs various daily reconciliations between Sage, Savantage, OMNI, the U.S. Department of the Treasury (Treasury), and the Federal Reserve Bank to ensure completeness, existence, and accuracy of the disbursed funds.

Upon completion of the loan disbursement, a TSP 19401, *Loan Status Report*, which contains pertinent participant information, is sent electronically to the participant's Federal agency or uniformed service payroll office to initiate payroll deductions from the participant's pay. TSP 19401s are sent to agencies daily. These reports are only sent to payroll agencies regarding a participant if (1) a loan has been disbursed and payments are required to be withheld from the participant's paycheck, (2) the loan has been paid off or been declared a taxable distribution and payments should cease, or (3) the loan has been changed or reamortized and the payment previously withheld has changed. Federal agency and the uniformed services payroll offices use either the (1) discretionary allotment method, or (2) the journal voucher method to submit loan payments to the TSP.

As previously mentioned, TSP loan payments are received via the payroll deductions and submitted via the Agency Payroll Interface (API), which is a key application that supports and processes submissions by Federal agencies and the uniformed services. Scheduled loan payments must be made through payroll deductions, and participants are responsible for ensuring that loan payments are being properly withheld from their paychecks. Additional payments can be made directly to the TSP via personal checks submitted to the TSP lockbox at the discretion of the participant. Upon posting to the participant's account, loan payments are credited to the appropriate TSP Fund(s) in accordance with the participant's most recent contribution allocation and credited to the participant's tax-deferred and tax-exempt balances in the same proportion that the loan was distributed from the participant's account.

Payroll offices and the uniformed services primarily provide payment services with respect to loan operations. They withhold participant deductions for loan payments and deposit payments to the TSP's Treasury account.

4. Treatment of Loan Prepayments, Refunds, and Delinquencies

Loan Prepayments

Participants can prepay their loans in full or with partial payments without a prepayment penalty. A full prepayment is the payment of the entire outstanding loan balance prior to the scheduled loan maturity.

Participants may either call the ThriftLine or a PSR or visit the TSP website (www.tsp.gov) to determine their exact outstanding loan amounts. The prepayment amount will include all unpaid principal and accrued interest at the time of the request plus 30 days of upcoming interest. The participant sends the payment along with a loan payment coupon to the TSP for processing. All checks must be made payable to the Thrift Saving Plan, include the loan number and TSP account number, and be sent by the participant to the TSP lockbox. Personnel at the lockbox review the loan payment coupon and/or check to ensure all required information is submitted and valid. If all information is present, the check is processed. If information is missing, the check is returned to the participant. Items submitted to the lockbox must be processed by the next business day after receipt. Funds are usually posted to the participant's account the day after they have been processed by the lockbox. Loan prepayments are invested according to the participant's percentage share of contributions at the time the loan was received. The TSP sends the participant a confirmation whenever a partial or full payment has been made on a loan. Images of the check, payment coupon, and other correspondence are scanned into AG and stored. Once the loan is closed, the applicable payroll office or uniformed service is notified via the TSP 19401.

Loan Refunds

A participant is entitled to a refund when his/her loan account has been overpaid by \$10 or more because the payment is greater than the amount due and/or a loan allotment is received from the employing office when that loan has already been paid in full. Such overpayments are automatically identified by OMNI, and refunds are issued to participants daily.

Loan Delinquencies

On a quarterly basis, a loan sweep is performed in OMNI to identify participants who are at least two and a half payments behind on their loan. When a participant is behind two and a half payments or more at the end of a quarter, the loan is considered delinquent. A delinquent notice is sent informing the participant of the delinquency and instructing the participant to make the required principal and interest payments by the end of the current quarter. A subsequent delinquent notice is sent to the participant in the middle of the quarter reminding the participant of the pending taxable distribution if a sufficient payment is not made.

If the appropriate amount is not posted to the loan account by the end of the current quarter, a taxable distribution is declared. Participants are notified that their loans have been closed and taxable distributions have been declared at the time of the taxable distributions. Subsequently,

taxable distributions are documented on the Internal Revenue Service Form 1099-R and sent to the participant no later than the end of January of the following year. Taxable distributions are based on the unpaid outstanding loan amount, including interest owed, and determined by the taxable and non-taxable basis of the loan disbursement.

When participants with outstanding loans separate from Federal service, they receive a notice stating that they have been separated from their previous agency and must repay the loan in full within 90 days of the notice or receive a taxable distribution. Participants may then repay the loan balance, receive a taxable distribution, or submit documentation stating they are employed with another eligible agency or military branch. A participant may accelerate a taxable distribution by signing an Intent Not to Repay Statement, which will prompt the immediate declaration of the taxable distribution. Generally, no inactive loan balances are older than 90 days other than for participants on approved non-pay status.

If a participant is on approved non-pay status for one year or more (unless related to military service), he/she must make loan payments from his/her personal funds to avoid being in default. When a participant returns from non-pay status, his/her loan is reamortized, and the participant is required to begin making payments based on the new amortization schedule. If the participant fails to make the required payments on the reamortized loan, he/she is subject to the delinquency process discussed above. Participants that enter non-pay status to perform military service are permitted to suspend payments on their loans until they return to pay status. Interest continues to accrue during this period. The maximum time limits for repayment are extended by the length of military service.

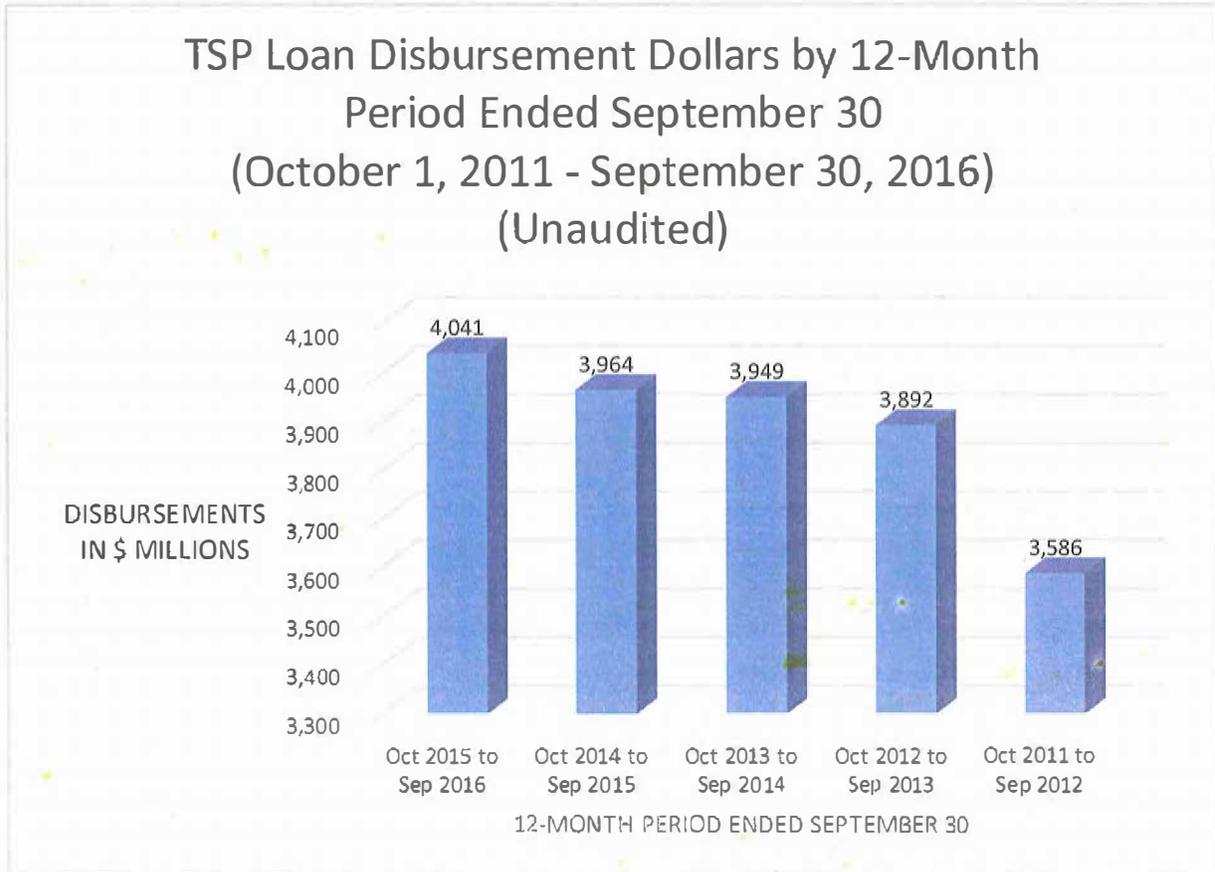
The primary method to document non-pay status is the submission of Form TSP-41, *Notification to TSP of Nonpay Status*, by the employing agency; the Form TSP-41 should include the intended start date of the non-pay status and the type of non-pay status (Military or Non-Military). If the agency does not submit the Form TSP-41, a SF-50, *Notification of Personnel Action*; military orders; or letter from the agency with all the required information is also accepted. When received, these forms are scanned into AG and processed by the TSP Service Bureau. Upon return from non-pay status, the aforementioned forms should be submitted by the participant's agency to indicate a return from non-pay status. Military participants are excluded from the quarterly default loan sweeps performed during approved non-pay status, and non-military participants are excluded from the sweeps during the first year of approved non-pay status.

Participants who transfer to another Federal agency or uniformed service are responsible for ensuring that correct loan payments continue upon transfer. Participants are instructed to notify the TSP if they transfer or change payroll offices or services.

5. TSP Loan Statistics

TSP loans have been disbursed since the inception of the loan program on January 1, 1988. Exhibit I-1 below illustrates total loan dollars disbursed⁶ during the last five 12-month periods beginning October 1 and ending September 30. TSP loan disbursements increased \$77 million or 2 percent, from the 12-month period ended September 30, 2015 to the 12-month period ended September 30, 2016.

Exhibit I-1



⁶ Source: TSP 600 I, *Cumulative Disbursement Reports* (October 2011 through September 2016)

Exhibit I-2 below presents the number of loans disbursed during the last five 12-month periods beginning October 1 and ending September 30⁶. The number of loans processed increased by 4,604, or 2 percent, from the 12-month period ended September 30, 2015 to the 12-month period ended September 30, 2016.

Exhibit I-2

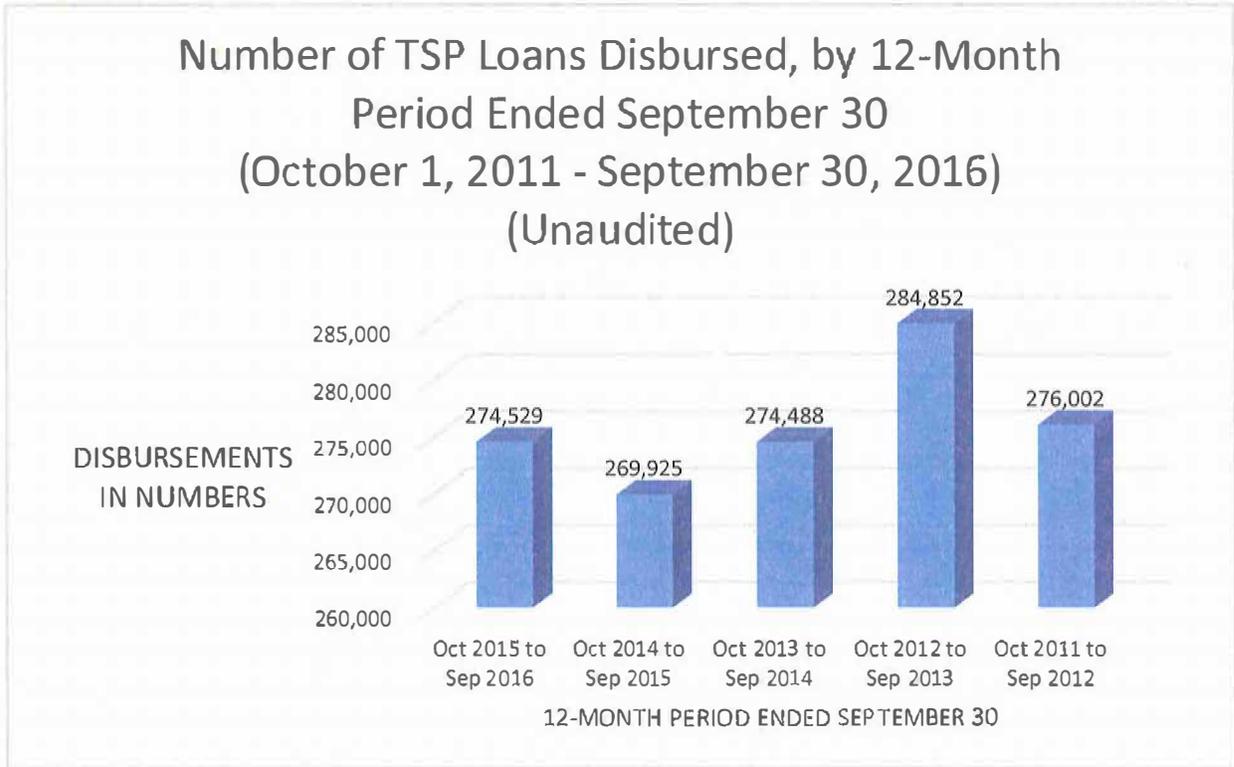
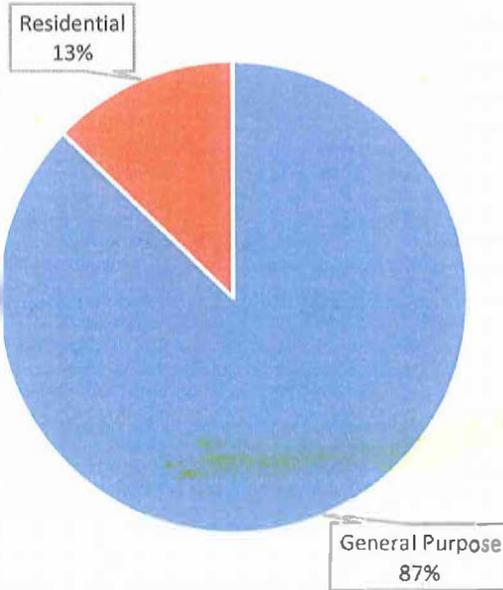


Exhibit I-3 on the next page illustrates the percentage of loan dollars disbursed by loan type for the 12-month period ended September 30, 2016⁶. The higher percentage of the two loan types, in terms of both dollars and number, is for general purpose loans. In the 12-month period ended September 30, 2016, approximately \$3.52 billion in general purpose loans were disbursed, which represented 87 percent of total loan disbursements. This percentage is consistent with the loan disbursements for the 12-month period ended September 30, 2015.

TSP Loan Dollars Disbursed by Type
during the Period October 1, 2015 - September 30, 2016
(Unaudited)



II. OBJECTIVE, SCOPE, AND METHODOLOGY

A. Objective

The U.S. Department of Labor Employee Benefits Security Administration (EBSA) engaged KPMG LLP (KPMG) to conduct a performance audit of Thrift Saving Plan (TSP) loans process.

The objectives of our performance audit were to:

- Determine whether the Federal Retirement Thrift Investment Board's Staff (Agency) implemented certain procedures to (1) process TSP loan transactions promptly and accurately in individual participant accounts and in the appropriate investment fund(s); (2) disburse TSP loans in accordance with regulations and participant authorizations; (3) limit participation in the TSP loan program to participants who meet eligibility criteria; and (4) accurately record loan activity in the TSP accounting records.
- Test compliance of the TSP loans process with United States Code (USC) Chapter 5, Sections 8433(g) and 8439 (hereinafter referred to as FERSA) and Code of Federal Regulations (CFR) Title 5, Parts 1655.2, 1655.2(a), 1655.4, 1655.6, 1655.9(a -d), 1655.13, 1655.14, 1655.14(f), 1655.15, 1655.16, 1655.18b, and 1655.21 (hereinafter referred to as Agency Regulations).

B. Scope and Methodology

We conducted this performance audit in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States and the American Institute of Certified Public Accountants' *Standards for Consulting Services*, using EBSA's *Thrift Savings Plan Fiduciary Oversight Program*. Our scope period for testing was October 1, 2015 through September 30, 2016. We performed the audit in four phases: (1) planning, (2) arranging for engagement with the Agency, (3) testing and interviewing, and (4) report writing.

The planning phase was designed to assist team members to develop a collective understanding of the activities and controls associated with the applications, processes, and personnel involved with the TSP loans process. Arranging the engagement included contacting the Agency and agreeing on the timing of detailed testing procedures.

During the testing and interviewing phase, we conducted interviews, collected and inspected auditee-provided documentation and evidence, participated in process walk-throughs, and designed and performed tests of controls and compliance⁷. We conducted these test procedures primarily at the Agency's headquarters in Washington, DC. In Appendix B, we identify the key documentation provided by Agency personnel that we reviewed during our performance audit.

Our performance audit procedures included using random attribute sampling to select specific samples related to TSP loans, which we used to determine if the Agency processed, disbursed, and managed loans in a manner that complied with FERSA and Agency Regulations. We selected the following samples in this manner:

- Loans disbursed during the period of October 1, 2015 through September 30, 2016
- Loan payments made during the period of October 1, 2015 through September 30, 2016
- Participants to whom a second loan was disbursed while another loan was outstanding during the period of October 1, 2015 through September 30, 2016
- Loans paid in full during the period of October 1, 2015 through September 30, 2016
- Loans with participant-initiated payments during the period of October 1, 2015 through September 30, 2016
- Participants for whom a taxable distribution was declared during the period of October 1, 2015 through September 30, 2016
- Participants with loans who entered non-pay status during the period of October 1, 2015 through September 30, 2016
- Participants with loans who entered non-pay status during the period of October 1, 2014 through September 30, 2015
- Loans re-amortizations during the period of October 1, 2015 through September 30, 2016
- Loan fees received during the period of October 1, 2015 through September 30, 2016
- Participants with loans which were approaching default (i.e., those with missed loan payments) during the period of October 1, 2015 through September 30, 2016

Additionally, our performance audit procedures included testing non-statistical samples of the following information obtained from the Agency for the period of October 1, 2015 through September 30, 2016:

⁷ We tested certain information technology edit checks performed over the loan application process subsequent to the scope period and in a test environment. The Agency represented that such edit checks were functionally and technically the same as those designed and operating in the production environment from October 1, 2015 through September 30, 2016. In addition, we tested the requirements underlying the edit checks in our 2016 compliance procedures.

- Daily Federal Reserve Board reconciliations to determine if payments disbursed by the Federal Reserve Bank were accurately recorded in the TSP's general ledger.
- Daily lockbox (SF-215) reconciliations to determine if participant-submitted payments to the lockbox were accurately recorded in the TSP's general ledger.
- Daily SF-1166 Omni Pay to Omni Plus reconciliations to determine if loan information between the two TSP systems agree.
- Daily reconciliation of outstanding loans to determine if the TSP's general ledger accurately included disbursed loan activity.
- Daily Loan Reports to determine if loan activity was accurately recorded in the TSP's general ledger.

Because we used non-statistically determined sample sizes in these instances, our results are applicable to the sample items we tested and were not extrapolated to the population.

Criteria used for this engagement are defined in the EBSA's *Thrift Saving Plan Fiduciary Oversight Program*, which includes 5 USC Chapter 84 and 5 CFR Chapter VI.

The report writing phase entailed drafting a preliminary report, conducting an exit conference, providing a formal draft report to the Agency for comment, and preparing and issuing the final report.

III. FINDINGS AND RECOMMENDATIONS

A. Introduction

We performed procedures related to the Thrift Savings Plan (TSP) loans process while conducting a performance audit at the Federal Retirement Thrift Investment Board's (the Board) Staff (Agency) headquarters. Our scope period for testing was October 1, 2015 through September 30, 2016. This performance audit consisted of reviewing applicable policies and procedures and testing manual and automated processes and controls, which included interviewing key personnel, reviewing key reports and documentation (Appendix B), and observing selected procedures.

Based upon the performance audit procedures conducted and the results obtained, we have met our audit objectives. We conclude that for the period October 1, 2015 through September 30, 2016, the Agency implemented certain procedures to (1) process TSP loan transactions promptly and accurately in individual participant accounts and in the appropriate investment fund(s); (2) disburse TSP loans in accordance with regulations and participant authorizations; (3) limit participation in the TSP loan program to participants who meet eligibility criteria; and (4) accurately record loan activity in the TSP accounting records. As a result of our compliance testing, we did not identify any instances of noncompliance with United States Code Chapter 5, Sections 8433(g) or 8439; or Code of Federal Regulations (CFR) Title 5, Parts 1655.2, 1655.2(a), 1655.4, 1655.6, 1655.9(a -d), 1655.13, 1655.14, 1655.14(f), 1655.15, 1655.16, 1655.18b, or 1655.21. However, we noted internal control weaknesses in certain areas of the TSP loans process.

We present three new recommendations, presented in Section III.B, related to the TSP loans process, all of which address other controls. Fundamental control recommendations address significant¹ procedures or processes that have been designed and operate to reduce the risk that material intentional or unintentional processing errors could occur without timely detection or that assets are inadequately safeguarded against loss. Other control recommendations address procedures or processes that are less significant than fundamental controls. These recommendations are intended to strengthen the TSP loans process. The Agency should review and consider these recommendations for timely implementation. The Agency's responses to these recommendations are included as an appendix within this report (Appendix A).

We noted no prior recommendations requiring follow-up during our performance audit.

Section III.B presents the findings and recommendations from this performance audit. Section III.C summarizes the open recommendations.

B. 2016 Findings and Recommendations

While conducting our performance audit over the TSP loans process, we identified three new findings and developed related recommendations. The U.S. Department of Labor Employee Benefits Security Administration requests appropriate and timely action for each recommendation.

RECOMMENDATIONS TO ADDRESS OTHER CONTROLS

2016-1: TSP Service Bureau Performance Monitoring Weaknesses

During our scope period, the Agency had formal procedures in place requiring the monthly review of performance measures at the TSP Service Bureau based on the contractor's monthly performance report submitted to the Agency. The procedures required that the report be reviewed by the designated Contracting Officer Representative (COR) and that issues be raised to the TSP Service Bureau contractor as necessary. However, these procedures did not define the documentation requirements for the COR's review of the monthly performance reports, and the Agency was unable to provide evidence that the COR consistently reviewed the monthly performance reports during the scope period.

Further, the Agency's contract with the TSP Service Bureau contractor requires that incoming documents are processed within two business days of receipt, and Agency management monitors processing times as part of the COR's review of the TSP Service Bureau monthly performance reports. In the *FY2016 FRTIB Performance Measurement Plan*, the Agency defined an internal benchmark of the acceptable percentage of forms processed within five business days in order to assess the contractor's form processing time metrics in the monthly performance reports; however, the Agency had not modified the terms of the contract to be consistent with the internal benchmark.

As a result of our testing, we noted that the taxable distributions for five of the 29 participants tested who had a taxable distribution declared during the scope period that was processed through a paper form submitted to the TSP Service Bureau were not processed within the contractually-required two business days of receipt. All five of these taxable distributions were declared through the participants' submission of an Int Not to Repay Statement. In addition, we noted that for one of these five participants, the taxable distribution was processed six business days after receipt

of the Intent Not to Repay Statement, one day in excess of the internal benchmark and the timeframe identified in Notice LC4048⁸.

Management determined that it was not necessary to formally document the COR's review of the monthly performance reports. In addition, management indicated that the two business day processing time requirement in the contract with the TSP Service Bureau was determined based on a previous system, and a modification to the contract terms was in progress to reflect current requirements.

The Government Accountability Office's *Standards for Internal Control in the Federal Government*, page 48, states the following:

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.

Transactions are promptly recorded to maintain their relevance and value to management in controlling operations and making decisions. This applies to the entire process or life cycle of a transaction or event from its initiation and authorization through its final classification in summary records. In addition, management designs control activities so that all transactions are completely and accurately recorded.

Section 5.c of the Agency's contract with the TSP Service Bureau contractor, dated March 23, 2007, states the following:

The Contractor shall complete all data entry no later than two (2) business days of receipt (including mail receipt, handling, scanning, and indexing). Turnaround time does not include weekends and Federal holidays.

⁸ Notice LC4048, *Notice to Separated Participant with Outstanding Loan*, provides the following processing time expectation to the participants: "The TSP will process your signed Intent Not to Repay Statement within approximately five business days of receipt."

1. **The Agency should:**
 - a. **Enhance its formal procedures to specify the documentation requirements for the COR's review of the TSP Service Bureau monthly performance reports, and maintain documentation of the reviews in accordance with such procedures; and**
 - b. **Modify the contract with the TSP Service Bureau contractor to reflect a form processing time requirement consistent with the current internal benchmark (i.e., five business days).**

By not formally documenting the Agency's monitoring of the TSP Service Bureau's performance, a risk exists that the Agency's procedures are inconsistently applied. Additionally, inconsistencies between contract requirements and the Agency's internal benchmarks increase the risk of misunderstandings of performance requirements between the contractor and the Agency.

2016-2: Lack of Formal Policy for the Timing of Certain Taxable Distributions

5 CFR 1655.15 identifies six situations in which unpaid loan principal, plus unpaid interest, is considered a taxable distribution. However, the CFR does not specifically address the order of precedence in which the six requirements should be applied if more than one is applicable, and the Agency did not formally define the order of precedence in its policies.

During our testing, we selected a random attribute sample of [REDACTED] participants who missed loan payments during our scope period to determine if a taxable distribution was declared in accordance with 5 CFR 1655.15, and we identified situations where more than one of the six requirements applied. Specifically, for three participants tested, the Agency sent the participant a notice that a taxable distribution would be declared by the end of the following calendar quarter if the required loan payments were not made, in accordance with 5 CFR 1655.15(a)(3). Subsequent to this initial notice, the participant separated from Federal service and received a second notice that the entire balance of the loan must be repaid by a new due date, which was later than the taxable distribution date initially communicated to the participant, in accordance with 5 CFR 1655.15(a)(2). For these three participants, no repayments were made by the taxable distribution date communicated on the initial pending default notice sent prior to their separation, and a taxable distribution was not declared on this date in accordance with 5 CFR 1655.15(a)(3) because of the participant's subsequent separation.

Management determined that documenting its policy and procedures with respect to the timing of taxable distributions when more than one situation in 5 CFR 1655.15 applies was not necessary.

5 CFR 1655.15 states:

- (a) The Board may declare any unpaid loan principal, plus unpaid interest, to be a taxable distribution from the Plan if [...]:
 - (2) A participant separates from Government service and does not repay the outstanding loan principal and interest in full within the period specified by the notice to the participant from the TSP record keeper explaining the participant's repayment options;
 - (3) The TSP record keeper advises the participant that there are missing payments and the participant fails to make (by personal check or guaranteed funds) a direct payment of the entire missing amount or repayment in full by the deadline established in accordance with § 1655.14(e).

The Government Accountability Office's *Standards for Internal Control in the Federal Government* states the following:

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. (page 48)

Management documents in policies for each unit its responsibility for an operational process's objectives and related risks, and control activity design, implementation, and operating effectiveness. Each unit, with guidance from management, determines the policies necessary to operate the process based on the objectives and related risks for the operational process. Each unit also documents policies in the appropriate level of detail to allow management to effectively monitor the control activity. (page 56)

2. **The Agency should formally document its policy with respect to the timing of taxable distributions when more than one situation in 5 CFR 1655.15 applies.**

By not formally documenting policies with respect to the timing of taxable distributions when more than one situation in 5 CFR 1655.15 applies, an increased risk exists that the Agency's policies are not consistently applied to all participants.

2016-3: Weakness in the Processing of Participants Returning from Military Non-Pay Status

During our testing to determine if taxable distributions were declared for participants who were delinquent on their loans during the scope period, we identified a control weakness, unrelated to the objective of this test, over participants returning from military non-pay status. We selected a random attribute sample of 58 participants to assess if they were accurately included in the Quarterly Default Sweep Reports used in our testing. As a result of this accuracy test, we identified one participant who should not have been included in these reports and ultimately had a taxable distribution declared in error based on 5 CFR 1620.45(a)(1). For this participant, the Agency received a Form TSP-41 in April 2016 indicating that the participant had returned from military non-pay status in October 2014, from which point the participant was current on loan payments. However, the participant's loan was not properly reamortized or extended when the Form TSP-41 was received by the Agency. As a result, the Agency incorrectly identified the participant as delinquent in the June 30, 2016 Quarterly Default Sweep Report, and subsequently declared a taxable distribution in error on September 30, 2016. The taxable distribution was reversed after the participant alerted the Agency to the error.

Agency management has not identified the specific cause of this participant's loan not being properly reamortized or extended upon receipt of the Form TSP-41. However, Agency management noted that the error was likely caused by the abnormal length of this participant's non-pay status of approximately six years.

The Government Accountability Office's *Standards for Internal Control in the Federal Government*, pages 13 and 14, state the following:

In the government sector, objectives related to compliance with applicable laws and regulations are very significant...Management considers objectives in the category of compliance comprehensively for the entity and determines what controls are necessary to design, implement, and operate for the entity to achieve these objectives effectively.

3. **The Agency should research the cause of the participant’s loan not being properly reamortized or extended upon notification of return from non-pay status and develop and implement appropriate corrective action to remediate the issue.**

By not implementing appropriate controls to prevent participants’ loans from not being properly reamortized upon notification of a participant’s return from non-pay status, other taxable distributions could be incorrectly declared.

C. Summary of Open Recommendations

2016 RECOMMENDATIONS

RECOMMENDATIONS TO ADDRESS OTHER CONTROLS

TSP Service Bureau Performance Monitoring Weaknesses

1. The Agency should:
 - a. Enhance its formal procedures to specify the documentation requirements for the COR’s review of the TSP Service Bureau monthly performance reports, and maintain documentation of the reviews in accordance with such procedures; and
 - b. Modify the contract with the TSP Service Bureau contractor to reflect a form processing time requirement consistent with the current internal benchmark (i.e., five business days).

Lack of Formal Policy for the Timing of Certain Taxable Distributions

2. The Agency should formally document its policy with respect to the timing of taxable distributions when more than one situation in 5 CFR 1655.15 applies.

Weakness in the Processing of Participants Returning from Military Non-Pay Status

3. The Agency should research the cause of the participant’s loan not being properly reamortized or extended upon notification of return from non-pay status and develop and implement appropriate corrective action to remediate the issue.

AGENCY'S RESPONSE



FEDERAL RETIREMENT THRIFT INVESTMENT BOARD
77K Street, NE Washington, DC 20002

May 9, 2017

Mr. Michael Auerbach
Acting Chief Accountant
Employee Benefits
Security Administration
United States Department of Labor
Suite 400
122 C Street, N.W.
Washington, D.C. 20001-2109

Dear Michael:

This is in response to KPMG's email on April 28, 2017, transmitting the KPMG LLP report entitled Employee Benefits Security Administration Performance Audit of the Thrift Savings Plan Loans Process, dated May 2017. My comments with respect to this report are enclosed.

Thank you once again for the constructive approach that the Department of Labor and its contractors are taking in conducting the various audits of the TSP. The information and recommendations that are developed as a result of your reviews are useful to the continued improvement of the Thrift Savings Plan.

Very truly yours,

A handwritten signature in blue ink that reads "Ravindra Deo". The signature is written in a cursive style.

Ravindra Deo
Acting Executive Director

Enclosure

AGENCY'S RESPONSE, CONTINUED

Executive Director's Staff Formal Comments on the
Employee Benefits Security Administration Performance Audit of the Thrift Savings Plan
Loans Process**2016 RECOMMENDATIONS TO ADDRESS FUNDAMENTAL CONTROLS****2016-1 TSP Service Bureau Performance Monitoring Weaknesses**

The Agency should:

- a. Enhance its formal procedures to specify the documentation requirements for the COR's review of the TSP Service Bureau monthly performance reports, and maintain documentation of the reviews in accordance with such procedures; and
- b. Modify the contract with the TSP Service Bureau contractor to reflect a form processing time requirement consistent with the current internal benchmark (i.e., five business days).

Agency Response:

- a) The agency concurs with this recommendation, and will consider this finding to be closed and complete when modifications to the "OPOP.171 – OPOP Service Provider Performance Oversight Procedures" are updated to reflect the maintenance, and documentation of requirements defining the COR's review of the TSP Service Bureau monthly performance reports. The Agency expects to complete this procedure modification by July 31, 2017.
- b) The agency concurs with this recommendation, and will consider this finding to be closed when modifications to the Service Bureau contract are completed to reflect a form processing time requirement consistent with the current internal benchmark (i.e., five business days). The Agency expects to complete this contract modification by January 31, 2018.

2016-2 Lack of Policies and Procedures over Timeliness of Taxable Distribution Processing

The Agency should formally document its policy with respect to the timing of taxable distributions when more than one situation in 5 CFR 1655.15 applies.

Agency Response:

The agency concurs with this recommendation, and will consider this finding to be closed and complete when modifications to the "OPOP.130 Loans Procedures" are updated to reflect the administrative steps involved in the timing of a taxable distribution when a participant transitions from one status code to a different status code (applicable

AGENCY'S RESPONSE, CONTINUED

to 5 CFR 1655.15). The Agency expects to complete this procedure modification by July 31, 2017.

2016-3 Weakness in the Processing of Participants Returning from Military Non-Pay Status

The Agency should research the cause of the participant's loan not being properly reamortized or extended upon notification of return from non-pay status and develop and implement appropriate corrective action to remediate the issue.

Agency Response:

The agency concurs with this recommendation. The Agency will develop a Corrective Action Plan by August 31, 2017.

KEY DOCUMENTATION AND REPORTS REVIEWED

Federal Retirement Thrift Investment Board Documents

- TSP Fact Sheet, *Effect of NonPay Status on TSP Participation*, dated February 2013
- TSP website, from August 2016 – March 2017
- TSP Report 3000, *Participant Balances Subsidiary*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 3040, *Loans Receivable & Earned Interest*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 3402, *Investment True-Up of Trades Report*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 3404, *Investment True-Up Report: Withdrawal*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 3405, *Investment True-Up Report: Loan Disbursements*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 3070, *Miscellaneous Receipts and Loan Refunds*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 9001, *SF 224 Board Summary Report*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 9030, *Unapplied Deposits Report*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 9110, *Cash Reconciliation*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 3302 P1, *Investment Pre-Note of Trades Report: Loan Payments*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 3302 P2, *Investment Pre-Note of Trades Report: Loan Payments*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP Report 6001, *Cumulative Disbursements Report*, for October 1, 2011 through September 30, 2016
- TSP Report 19401, *Loan Status Report*, for selected dates during the period October 1, 2015 through September 30, 2016
- TSP-20 (TSP-U-20), *Loan Application*
- TSP 21-G and TSP 21-R, *Loan Agreement*
- TSP 41, *Notification of TSP Non-pay Status*

KEY DOCUMENTATION AND REPORTS REVIEWED, CONTINUED

- Form 1099-R, *Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*
- LC/LU 201, *Loan Re-amortization Confirmation Notice*
- LC/LU 401, *Pending Taxable Distribution Notice*
- LC/LU 402, *5118 Term Limit Notice*
- LC/LU 403, *Loan Taxable Distribution Notice*
- LC/LU 406, *Loan Taxable Distribution Reminder*
- LC/LU 502, *Loan Paid in Full Notice*
- LC/LU 601, *Nonpay Confirmation Notice*
- Loans receivable general ledger account detail as of September 30, 2016
- Loans payable general ledger account detail as of September 30, 2016
- Taxable Distributions general ledger account detail for the period October 1, 2015 through September 30, 2016
- G Fund Contributions- Employee general ledger account detail for the period October 1, 2015 through September 30, 2016
- Loan fees received general ledger account detail for the period October 1, 2015 through September 30, 2016
- All active loans (general purpose and residential) during the period October 1, 2015 through September 30, 2016
- All loans disbursed during the period of October 1, 2015 through September 30, 2016
- Participants to whom a second loan was disbursed while another loan was outstanding during the period of October 1, 2015 through September 30, 2016
- All loans paid in full during the period of October 1, 2015 through September 30, 2016
- Participants for whom a taxable distribution was declared during the period of October 1, 2015 through September 30, 2016
 - All loan re-amortizations during the period of October 1, 2015 through September 30, 2016
 - All loans with participant-initiated payments during the period October 1, 2015 through September 30, 2016
 - Participants who entered non-pay status while having an outstanding loan during the period October 1, 2015 through September 30, 2016
 - Participants who entered non-pay status while having an outstanding loan during the period October 1, 2014 through September 30, 2015

KEY DOCUMENTATION AND REPORTS REVIEWED, CONTINUED

- Participants who missed more than two and a half loan payments or whose loan payments were insufficient and not repaid in full by the following calendar quarter during the period October 1, 2015 through September 30, 2016
- Daily Federal Reserve Board (FRB) Reconciliation Reports for selected dates during the period October 1, 2015 through September 30, 2016
- Daily 215 Lockbox reconciliation for selected dates during the period October 1, 2015 through September 30, 2016
- Daily TSP-3040 Outstanding Loans to FRTIB General Ledger Reconciliation for selected dates during the period October 1, 2015 through September 30, 2016
- Daily SF1166 Omni Pay to Omni Plus reconciliations for selected dates during the period October 1, 2015 through September 30, 2016
- Quarterly Loan Default Sweep Reconciliations during the period October 1, 2015 through September 30, 2016
- U.S. Treasury *EFT Payment Voucher Report* for selected dates during the period October 1, 2015 through September 30, 2016
- U.S. Treasury *Deposit Information Voucher Report* for selected dates during the period October 1, 2015 through September 30, 2016
- *TSP Service Bureau Monthly Performance Review* reports for selected months during the period October 1, 2015 through September 30, 2016
- *Standards of Conduct* – New Hire Ethics Training 2016

Other Documents and Reports

- U.S. Treasury Office of Debt Management *End-of-Month Average Market Yields for Trust Funds and Other Government Programs* from September 2015 through September 2016