



*Office of Inspector General*

**MEMORANDUM**

**FOR:** Dr. Rajiv Shah, Administrator

**FROM:** Michael Carroll, Acting Inspector General

**SUBJECT:** Report on United States Agency for International Development's (USAID) Compliance With the Improper Payments Elimination and Recovery Act

The Office of Inspector General (OIG) is transmitting its report on our evaluation of USAID's compliance with the requirements of the Improper Payments Elimination and Recovery Act of 2010 (IPERA) as of September 30, 2011. USAID's management is responsible for compliance with those requirements. Our responsibility is to review USAID's reporting on improper payments in the Annual Financial Report (AFR) and accompanying materials, to determine whether the agency complied with IPERA.

OIG found that as of September 30, 2011, and in its November 15, 2011, Agency Financial Report, USAID complied with IPERA requirements. Our tests disclosed one area in internal controls over improper payments that should be improved. Specifically, we determined that USAID did not ensure that audits of costs incurred by contractors are completed in a timely manner to identify, prevent and recover improper payments.

This report contains one recommendation to improve USAID's internal controls over improper payments.

We have considered USAID's management comments on the draft report and the recommendation therein and have reached management decision on the recommendation. Please forward all information to your Office of Audit, Planning and Coordination for final action.

OIG appreciates the cooperation and courtesies extended to us during the evaluation. OIG is looking forward to working with your staff during the fiscal year 2012 evaluation of USAID's compliance with IPERA.

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## Background

Congress passed the Improper Payments Information Act of 2002 (IPIA), requiring federal agencies to provide estimates and reports of improper payments. Specifically, IPIA required agencies to review all programs and activities annually and identify those that may be susceptible to improper payments.<sup>1</sup> Despite IPIA, improper payments continued to increase throughout government agencies, and federal agencies reported approximately \$100 billion in improper payments for fiscal year (FY) 2009.<sup>2</sup> In response, the President signed Executive Order 13520 of November 20, 2009—Reducing Improper Payments and Eliminating Waste in Federal Programs. The purpose of the Executive order was to increase transparency and hold federal agencies accountable for reducing improper payments. On March 22, 2010, the Office of Management and Budget (OMB) issued government-wide guidance for the implementation of the Executive order in OMB Circular A-123, Appendix C, Part III. The guidance included specific responsibilities for each agency's accountable officials: to determine high-priority programs, define targets for high-priority programs, and establish procedures to identify agencies with outstanding improper payments.

On July 22, 2010, Congress passed the Improper Payments Elimination and Recovery Act of 2010 (IPERA). It amended IPIA, repealed the Recovery Auditing Act, and significantly increased agency recapture efforts by expanding the types of payments that can be reviewed and lowering the threshold of annual outlays that requires agencies to conduct payment recapture audit programs. OMB Memorandum M-11-16 provides agencies guidance on implementing IPERA and requires all agencies to submit to OMB a plan for payment recapture audits that describes their current payment recapture efforts. The new requirements of IPERA<sup>3</sup> are summarized below.

- IPERA lowers the threshold for conducting payment recapture audits from \$500 million in annual outlays to \$1 million in annual outlays if conducting such audits would be cost-effective. IPERA also expands the scope of the audits from reviewing just contract payments to reviewing all programs and activities.
- IPERA requires the Director of OMB to develop specific criteria as to when an agency should be required to obtain a separate, annual audit opinion on internal control over improper payments, and criteria for establishing a multiyear cycle for obtaining an audit for internal control over improper payments.
- IPERA establishes that the Director of OMB has 1 year to develop the criteria for obtaining opinions on internal control over improper payments. Payment recapture audits are an effective tool to identify improper payments and their root causes. An agency not having a robust audit program for payment recapture would likely trigger a separate opinion on internal control over improper payments under the forthcoming guidance on internal control over improper payments.

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<sup>1</sup> IPIA, Public Law 107-300, Section 2(a).

<sup>2</sup> OMB Memorandum M-10-13, March 22, 2010.

<sup>3</sup> OMB Memorandum M-11-04, November 16, 2010.

According to OMB's guidance, compliance with IPERA means that the agency has:

- Published a Performance and Accountability Report (PAR) or an Agency Financial Report (AFR) for the most recent fiscal year and posted that report and any accompanying materials required by OMB on the agency Web site.
- Conducted a specific risk assessment of each program or activity that conforms with Section 3321 of Title 31 U.S.C. (if required).
- Published estimates of improper payments for all programs and activities identified as susceptible to significant improper payments under its risk assessment (if required).
- Published programmatic corrective action plans in the PAR or AFR (if required).
- Published, and met, annual reduction targets for each program assessed to be at risk and measured for improper payments.
- Reported a gross improper payment rate of less than 10 percent for each program and activity for which an estimate of improper payments was obtained and published in the PAR or AFR.
- Reported information on its effort to recapture improper payments.<sup>4</sup>

The guidance further specifies that if the agency did not meet one or more of these requirements, it was not compliant with IPERA. The agency's inspector general should also evaluate the accuracy and completeness of the agency's reporting and performance in reducing and recapturing improper payments.

## **Evaluation Objective**

The Office of Inspector General (OIG) performed this examination to determine whether the U.S. Agency for International Development (USAID) complied with IPERA for the fiscal year ended September 30, 2011, and as reported in the AFR dated November 15, 2011.

## **Evaluation of USAID's Efforts**

USAID complied with the requirements of IPERA in its assessment of improper payments in the AFR dated November 15, 2011. The efforts described therein to identify, prevent, and recover improper payments appear to be reasonable. However, those efforts could be augmented by expediting audits of costs incurred by contractors who perform various services for the Agency around the world.

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<sup>4</sup> OMB Circular A-123, Management's Responsibility for Internal Control, Appendix C, Part II, "Compliance with the Improper Payment Requirements," April 2011. As previously noted in this report, IPIA has been amended by IPERA.

## **Independent Auditor's Report on USAID's Compliance with the Improper Payments Elimination and Recovery Act of 2010**

We have evaluated the United States Agency for International Development's (USAID) compliance with the requirements of the Improper Payments Elimination and Recovery Act of 2010 (IPERA) as of September 30, 2011. USAID's management is responsible for compliance with those requirements. Our responsibility is to review USAID's improper payments reporting in the AFR and accompanying materials to determine whether the agency complied with IPERA. Compliance with IPERA means that the agency has:

- Published a PAR or AFR for the most recent fiscal year and posted that report and any accompanying materials required by OMB on the agency Web site.
- Conducted a specific risk assessment for each program or activity that conforms with Section 3321 of Title 31 U.S.C. (if required).
- Published estimates of improper payments for all programs and activities identified as susceptible to significant improper payments under its risk assessment (if required).
- Published programmatic corrective action plans in the PAR or AFR (if required).
- Published, and met, annual reduction targets for each program assessed to be at risk and measured for improper payments.
- Reported a gross improper payment rate of less than 10 percent for each program and activity for which an estimate of improper payment was obtained and published in the PAR or AFR.
- Reported information on its effort to recapture improper payments.<sup>5</sup>

We conducted the evaluation in accordance with attestation standards established by the American Institute of Certified Public Accountants and with generally accepted government auditing standards issued by the Comptroller General of the United States. Accordingly, our work included examining, on a test basis, evidence about USAID's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our evaluation provides a reasonable basis for determining USAID's compliance. Our evaluation does not provide a legal determination on USAID's compliance with the specified requirements.

Based on the results of our evaluation, we determined that USAID complied, in all material respects, with the aforementioned requirements as of September 30, 2011, and as reported on November 15, 2011, in its AFR.

Our tests disclosed one area of USAID's internal controls over improper payments that needs improvement. Specifically, we determined that USAID did not ensure that audits of costs

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<sup>5</sup> OMB Circular A-123, "Management's Responsibility for Internal Control," Appendix C, Part II, "Compliance with the Improper Payment Requirements," April 2011. As previously noted in this report, IPIA has been amended by IPERA.

incurred by contractors are completed in a timely manner to identify, prevent, and recover improper payments.

USAID, Office of Inspector General  
March 15, 2012

## Notification of Finding and Recommendation

### 2011-IPP-1

#### **Audits of Costs Incurred by Contractors Are Not Completed in a Timely Manner to Identify, Prevent, and Recover Improper Payments**

USAID contracts with for-profit organizations to perform various types of services around the world. USAID requires all costs incurred by these contractors to be audited and, to conduct these audits, contracts with the Defense Contract Audit Agency (DCAA). During our review, we noted that DCAA is not conducting the audits and reporting the results in a timely manner. As of September 30, 2011, 168 audits were still outstanding.

It is essential that these audits be performed and completed because they have the potential to identify and lead to the recovery of improper payments made by the Agency as illustrated in the table below.

Table 1: Analysis of Audits Completed by DCAA

Fiscal Year	Audits Completed	Questioned Costs
2007	91	\$12 million
2008	54	\$11 million
2009	43	\$ 5 million
2010	7	\$ 0

As of October 1, 2010, 176 audits requested by USAID had not been completed and after meeting with OIG, DCAA agreed to complete 62 of these audits in FY 2011. However, it completed only eight of the audits and 168 audits were still outstanding as of September 30, 2011. USAID should try to expedite these audits to improve its performance in identifying, preventing, and recovering improper payments. One way to expedite the audits would be to contract with public accounting firms.

***Recommendation:*** We recommend that the USAID Administrator direct the Office of Acquisition and Assistance to explore all options available, including the use of public accounting firms, to expedite the audits of costs incurred by contractors.

## **Evaluation of Management Comments**

We have reviewed and evaluated USAID's management comments on the finding and recommendation included in the draft report. The following is a summary of USAID's management's comments and our evaluation of them.

USAID management agreed to implement the recommendation and commented that the Chief Financial Officer office accepted the finding and stated that audits are an effective tool for bringing such payments to light, affecting corrective action and strengthening internal controls. USAID management also commented that the Defense Contract Auditing Agency (DCAA) has not been meeting acceptable time and quality standards in recent years and the Office of Acquisitions and Assistance has already coordinated with the Office of Inspector General to meet with DCAA to continue to address these concerns. USAID's management has already begun the process of seeking such services from non-federal auditing firms. The target completion date is December 31, 2012. We have reached a management decision on the recommendation and will review USAID's implementation of the recommendation during FY 2012.



## Scope and Methodology

USAID management is responsible for (1) complying with IPERA requirements, (2) reporting improper payments in accordance with OMB Circular A-136, Section II.5.8, IPIA (as amended by IPERA), and (3) complying with other applicable laws and regulations.

OIG is responsible for obtaining reasonable assurance about whether USAID complied with IPERA requirements as of September 30, 2011. OIG is also responsible for (1) obtaining a sufficient understanding of the internal controls over improper payments and compliance to plan the evaluation, (2) testing whether USAID complied with the reporting requirements of OMB Circular A-136 Section II.5.8, IPIA (as amended by IPERA), and (3) testing compliance with selected provisions of IPERA.

To fulfill these responsibilities, OIG:

- Obtained an understanding of USAID's internal control over improper payments and compliance with IPIA and IPERA.
- Reviewed the Management's Discussion and Analysis and Improper Payments Reporting Details in USAID's FY 2011 AFR to ensure compliance with the requirements of IPERA.
- Examined, on a test basis, evidence supporting the amounts disclosed in the quarterly report on high-dollar overpayments.
- Evaluated the overall presentation of the improper payments and risk assessment in the AFR.
- Tested relevant internal controls over improper payments, and evaluated the design and operating effectiveness of the internal controls.
- Tested USAID compliance with specific IPERA requirements.

Because of inherent limitations in internal control, noncompliance may occur and not be detected, and such testing may not be sufficient for other purposes.

This report is intended solely for the information and use of the USAID Administrator and the Chief Financial Officer and others within USAID, as well as of OMB and Congress, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record, and its distribution is not limited.

Office of Inspector General  
March 15, 2012

**Management Comments**