Office of Inspector General

January 14, 2011

MEMORANDUM

TO: David D. Ostermeyer, Chief Financial Officer

FROM: Joseph Farinella, AIG/A [redacted] /s/

SUBJECT: Control Deficiencies Identified during the Office of Inspector General's Audit of USAID's Fiscal Years 2010 and 2009 Financial Statements

We have audited the balance sheet as of September 30, 2010 and the related statements of net cost, changes in net position, and budgetary resources for the year then ended, hereinafter referred to as financial statements, of the United States Agency for International Development (USAID), and have issued an unqualified opinion thereon dated November 12, 2010. In planning and performing our audit of the financial statements of USAID, we considered its internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control. We have not considered the internal control since the date of our report.

During our audit we noted certain matters involving USAID's internal controls that are presented in this letter for your consideration. The comments and suggestions, all of which have been discussed with the appropriate members of USAID's management, are intended to improve USAID's internal controls or result in other operating efficiencies.

We appreciate the cooperation and courtesies that your staff extended to the Office of Inspector General during the audit. If you have questions concerning this letter or would like to discuss its contents, please contact Rohit Chowbay at (202) 712-1317.

Attachment (a/s)

Control Deficiencies for Management

Accrued Expenses and Accounts Payable

USAID's methodology for estimating and recording accounts payable and accrued expenses using Cognizant Technical Officer (CTO) reviews of the information contained in the Accrual Reporting System is not operating effectively. Specifically, we found that CTOs were not consistently reviewing and revising as necessary, the quarterly estimates for accounts payable and accrued expenses before those amounts were recorded in its general ledger. USAID estimates its accounts payable and accrued expenses using its Accrual Reporting System but several CTOs recorded the estimated pipeline amounts, which are significantly higher, as accrued expenses instead of the estimated accrual amounts calculated by the Accrual Reporting System. From a sample of 60 estimated accrued expenses reviewed, management did not provide supporting documentation for 16 of the sampled items while 6 were incorrectly recorded in the general ledger resulting in an overstatement of approximately $6 million dollars. As a result, management recorded an adjustment to accurately reflect USAID's accounts payable and accrued expenses in the general ledger. Automated Directive System 631, Accrued Expenditures, Section 631.5 Integrated Accruals System Procedures Guide, states that the Obligation Manager or CTO must: (a) review system-generated accrual amounts and/or allocations to determine if the amount can be validated and to validate the accrual amount as indicated in the Accruals Query. We suggest that the Chief Financial Officer coordinate with the Director, Office of Acquisition and Assistance, to ensure that: (1) supporting documentation for accruals is easily retrievable and available for review and (2) accruals are accurately recorded and reported in the financial statements.

Unliquidated Obligations

USAID has not completed its analysis of unliquidated obligations to determine whether those without activity for 12 months are still required or should be deobligated. Although the agency has made progress in reviewing and deobligating inactive obligations, as of September 30, 2010 it had approximately $57 million in unliquidated obligations that had no activity for more than two years and should be evaluated for deobligation. This occurred because, as of September 30, 2010, USAID had not implemented a process to consistently review, analyze, and deobligate unneeded obligations. USAID's Automated Directive System (ADS) No. 621 states that as part of the annual budget process, Assistant Administrators, independent Office Directors, and Mission Directors must certify whether unexpended balances are necessary for on-going programs. The directive further requires that in conducting reviews of obligations to identify funds that must be deobligated, obligation managers and others involved in the review process should consider circumstances that could result in excessive or unneeded obligation balances. We suggest that the Chief Financial Officer conduct an analysis of the unliquidated obligations and determine whether the $57 million should be deobligated.

Loans Receivable Confirmations

Confirmation of USAID's outstanding loans receivable continues to be problematic. During the fiscal year 2010 audit, we were unable to confirm 38 percent of the sample of loans receivable that we selected. The amount of these loans was $13 billion, including $12.8 billion that was a loan guarantee to Israel. This occurred because the Government of Israel (GOI) did not respond in a timely manner to the loan confirmation requests in which we requested them to provide their loan balances. Instead, GOI requested USAID to provide them with the outstanding principal and interest balances per USAID general ledger which they confirmed. We suggest that the Chief Financial Officer direct its Washington Financial Services to coordinate with Mission controllers and officials of the Department of State to ensure that loan confirmation requests are submitted to appropriate personnel of the host governments and that they are completed and returned to the OIG in a timely manner.

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Credit Authority Financing Accounts

During our review of the USAID's credit programs, we determined that USAID's Central Accounting and Reporting Division (CAR) does not reconcile available funds (unobligated authority) between the budget module and the general ledger for its Development Credit Authority (DCA) and Micro and Small Enterprise Development (MSED) financing accounts. We found that MSED account 72X4343 had a difference of $5,006,773 and the DCA account 72X4266 had differences of $700,241. This occurred because USAID has not completed a reconciliation of the budget transfers and obligations for these accounts. As a result, CAR recorded a large number of adjustments to bring the budget module account into agreement with the general ledger account. We suggest that the Chief Financial Officer direct CAR to complete the reconciliation of its credit program financing accounts to the budget module.

Required Historical Data to Calculate the Annual Re-estimates

During our review of loan guarantee programs, we determined that USAID lacks the historical data that is required to accurately calculate the annual year end re-estimates that are submitted to the Office of Management and Budget (OMB). OMB Circular A-11 requires that all agencies use the Credit Subsidy Calculator 2 to compute the re-estimates by using the traditional and balances approaches and reconciling the results. USAID cannot do this because it does not have the necessary data, such as Financing Account Interest, re-estimates fees, subsidy transfers, and borrower cash flow information. Instead, USAID uses the balances approach only to compute re-estimates because that approach does not require the missing historical data. We suggest that the Chief Financial Officer obtain the missing historical data, which is available at the U.S. Treasury and OMB, and calculate the re-estimates in accordance with the requirements of OMB Circular A-11, section 185.6 (C).

Accounts Receivable

During our testing of accounts receivable write-offs, we found that USAID used the wrong posting model to write off its accounts receivable. This occurred because USAID's Phoenix financial management system provided a choice of several posting model options when initiating accounts receivable write-off transactions and the Financial Management Division chose the wrong posting model to process the write-offs. As a result, USAID understated its FY 2010 advances account by approximately $7.84 million. We suggest that the Chief Financial Officer develop and implement procedures to ensure that the correct posting model is used to write off accounts receivable. We also suggest that the Chief Financial Officer adjust the advances accounts that were erroneously charged with accounts receivable written off during FY 2010.

Advances

USAID's process to account for pooled advances needs improvement. Our tests of advances found that, as of June 30, 2010, 98 obligations recorded on the Department of Health and Human Services Payment Management System (PMS) Synchronization Report, valued at approximately $4.8 million were deobligated twice by USAID. The obligations were deobligated once by USAID when the funds were manually removed from the PMS after the Cash Management and Payment Division (CMP) received notification that those grants were completed and that the grantees would no longer be incurring expenses against those obligations. The same obligations were deobligated from the PMS a second time because the USAID Office of Acquisition and Assistance recorded a deobligation in the Phoenix Accounting System after receiving notification that the period of performance had expired. When the daily Phoenix Outbound Interface with PMS occurred, the obligations that were manually removed from the PMS were reduced a second time and the closed grants were re-established on the PMS. As a result, the obligations recorded for those grants in PMS were lower than the expenses that the grantees were supposed to report on their quarterly

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reports. The grantees were therefore, forced to report expenses to the extent of the obligations available and not all the expenses that were incurred. As a result, the outstanding advances on the balance sheet were overstated by $4.8 million. Statements on Federal Financial Accounting Standards (SFFAS) #1 paragraph 59 states that Advances should be recorded as assets and subsequently reduced when services are received or expenses are actually incurred. Because of the duplicate de-obligation mentioned above USAID did not comply with the related requirements of SFFAS #1. CMP is coordinating with CGI to develop a solution for this problem and therefore, we are not making any suggestions to the Chief Financial Officer.

Sensitive Payments
USAID's process to monitor activities related to sensitive payments should be improved to avoid abuses and violations. During our review of sensitive payments, we found that USAID is not adequately monitoring entertainment funds, gifts received, speaking honoraria, and executive travel. Specifically, we determined that USAID did not have procedures in place to review the use of the entertainment fund purchase card. We further determined that procedures outlined in ADS 628.3.2 for accepting and recording gifts were not consistently followed by all USAID's overseas missions. Our review also revealed that USAID has not implemented adequate procedures to determine if speaking honoraria was received by senior level officials. Furthermore, we determined that four overseas missions were not using the required E2 travel system to prepare executive Travel Authorizations (TA's) and process the related vouchers. As a result, USAID obligated travel funds although the TA's were not prepared in accordance with ADS 522 Interim Update 09-10. The deficiencies occurred because USAID does not have specific procedures for all areas of sensitive payments outlined in the GAO guidance. Therefore, we suggest that the Chief Financial Officer augment its policies and procedures to ensure that sensitive payment activities are effectively monitored and reported.

USAID Treasury Report on Receivables
During our audit of USAID's loan activities, we found that its quarterly Treasury Report on Receivables Due from the Public (TROR) does not accurately reflect its loans receivable balances reported by Midland Loan Services (MLS) during the first quarter of FY 2010. Our audit identified instances, throughout the fiscal year, where adjustments were made on the TROR by Washington Financial Services (WFS), of the CFO's office, that were not reviewed and validated by supervisory personnel before this report was submitted to Treasury. For example, we determined that Midland Loan Services reported a beginning balance adjustment of $33,187,875 in one portfolio but USAID reported $334,434,848 to Treasury on the TROR. This required an adjustment of $301,246,972 by USAID. Our audit further found that, in some instances, USAID adjusted the beginning balance of the TROR because of errors identified in the calculation of interest and late fees by MLS. As a result, USAID made a year end adjustment in the amount of $89,000,000 to bring the TROR into agreement with Treasury. In addition, we noted that WFS did not reconcile the TROR to the general ledger as is required by ADS 625.3.8.1(b) for the first and second quarters of FY 2010. We suggest that USAID's Chief Financial Officer direct WFS to perform a supervisory review of the TROR before it is submitted to Treasury and to ensure that the information on the TROR is reconciled to the general ledger.

FY 2010 Mission Reviews
During our FY 2010 GMRA at the 10 selected missions, we identified the following internal control deficiencies:

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Estimating and Recording Accrued Expenses
USAID Missions' procedures to estimate and record accrued expenses are not effective. During our audit we found that Contracting Technical Officer Representatives (COTRs) were not accurately calculating and recording the estimated amounts for the quarterly accrued expenses recorded in the general ledger. Specifically, we found that estimated accrual transactions of approximately $31 million were incorrectly recorded in the Phoenix accounting system and that it was not discovered by the responsible COTRs. This occurred because the COTRs were not consistently reviewing and/or analyzing the estimated accruals that were generated by the Accrual Reporting System and comparing the estimated amounts to the documentation used to support the accruals. We suggest that USAID's Chief Financial Officer direct the mission COTRs to review and if necessary, modify the quarterly accrued expenses generated by the Accrual Reporting System before this information is recorded in the general ledger.

Process to Review Outstanding Advances
USAID Mission's process to review outstanding advances is not effective. During our review of outstanding advances as of June 30, 2010 at the selected missions, we identified approximately $7.2 million in advances on the Advance Aging reports that were outstanding for more than 90 days and should have been liquidated. Automated Directives System 636.3.4, Program Funded Advances, requires Mission Controllers to ensure that outstanding advances to contractors and other recipients are periodically reviewed, at least quarterly, so that funds advanced are not in excess of immediate disbursement needs. We suggest that Chief Financial Office implement a process to identify and liquidate outstanding advances within 90 days in accordance with agency guidelines.

Process to Review Unliquidated Obligations
Our review found that the process to review unliquidated obligations needs improvement. During our review of unliquidated obligations at the selected missions, we identified obligations totaling approximately $47.2 million that were inactive for over one year as of June 30, 2010. Although Mission management has shown improvement in the de-obligation process, we determined that missions were not de-obligating funds in a timely manner. Automated Directives System (ADS) 621.3.17, Review of Unexpended Obligated Balances, states that unexpended obligated balances must be monitored to ensure that the level of funding is consistent with Agency forward funding guidelines and that balances are deobligated when they are no longer needed for the purposes for which they were initially obligated. Therefore, we suggest that the Chief Financial Office direct its mission Controllers to conduct timely review and evaluation of all unliquidated obligations and deobligate excess funds as necessary.

Administrative Approval of Project Disbursements
Our review found that the process for administrative approval of project disbursements needs improvement. During our review of project disbursements, we noted that in some instances, Contracting Officer Technical Representatives (COTR) could not provide evidence of administrative approval for project disbursements. In other instances, the COTR's checklist was not completed or was missing from the related files. USAID's Office of Procurement Guidebook for Managers and COTRs on Acquisition and Assistance states that COTRs should maintain contract work file for their projects. The contract work file should contain all relevant documentation such as notes of conversations with the contractor, written instructions given to contractor, and similar items that were provided to the COTR. Therefore, we suggest that the Chief Financial Officer coordinate with the Office of Acquisition and Assistance to implement procedures that require mission COTRs to maintain documentation of site visits and/or other oversight activities of projects for which they are responsible.