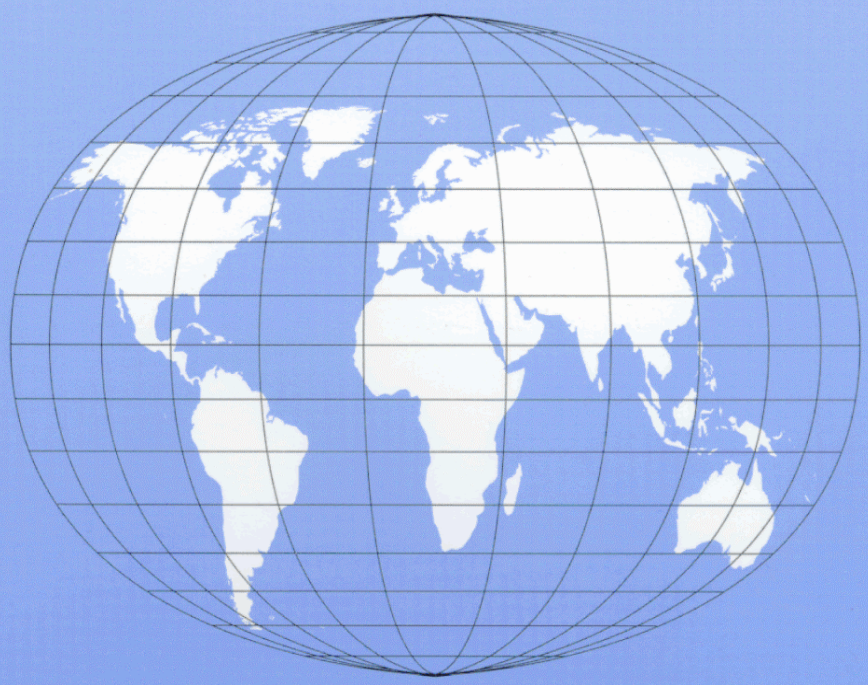
Report of Audit

Audit of the Accuracy of USAID/South Africa's Recipient Audit Universe

Report No. 4-674-01-004-P
July 23, 2001



PRETORIA, SOUTH AFRICA

OFFICE OF INSPECTOR GENERAL
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

RIG/Pretoria

July 23, 2001

MEMORANDUM

FOR: Mission Director, USAID/South Africa, William Stacy Rhodes

FROM: Regional Inspector General/Pretoria, Joseph Farinella /s/

SUBJECT: Audit of the Accuracy of USAID/South Africa's Recipient Audit Universe, Report Number 4-674-01-004-P

This memorandum is our final report on the subject audit. In finalizing the report, we considered your comments on the draft report. These comments are summarized on page 6 of the report and presented in their entirety in Appendix II.

Based on your comments, we consider that management decisions have been reached to address both Recommendation Nos. 1 and 2 of the report. In accordance with USAID guidance, please notify the Bureau for Management, Office of Management Planning and Innovation (M/MPI) when final action has been completed on the recommendations.

Thank you for the assistance and courtesies extended to my staff during the audit.

Summary of Results

Our audit of the Accuracy of USAID/South Africa's Recipient Audit Universe focused on determining whether the Mission's audit universe was complete and accurate, and if the required audits were done in a timely manner.

Our results showed that USAID/South Africa's recipient audit universe was complete and accurate. However, 13, or 45 percent, of the 29 required audits were not done in a timely manner. Periodic monitoring by the Management Control Review Committee could help alleviate this problem.

This issue is discussed in more detail in the *Audit Findings* section of this report.

Background

Financial audits of contracts and grants are a primary basis for effective management and control of USAID's program expenditures. These audits are designed to provide USAID management reasonable assurance that transactions are properly recorded and accounted for; laws and regulations, and provisions of contract or grant agreements are complied with; and USAID-financed funds, property and other assets are safeguarded against unauthorized use or disposition.

In response to Congressional concerns, USAID has taken an active role in recent years, using audits as a management tool, to improve financial accountability of its programs. In 1991, USAID revised its standard provisions for its contracts, cooperative agreements and grants, requiring annual audits of non-U.S. organizations *receiving* USAID funds of $25,000 or more a year. The threshold was increased to $100,000 in May 1994. In July 1998, USAID again revised the standard provisions for its grants, cooperative agreements and contracts, but this time requiring annual audits when the recipient *expends* $300,000 or more in USAID awards in its fiscal year.

Furthermore, in April 1992, USAID issued a General Notice, defining the role of USAID missions in obtaining audits of their contracts, grants and cooperative agreements with non-U.S. organizations. In May 1996, these requirements were incorporated into Chapter 591 of USAID's Automated Directives System (ADS), which, among other things, requires USAID missions to (i) establish an audit management program; (ii) maintain an audit inventory database; and (iii) have audits done for non-U.S. grants, contracts and cooperative agreements that meet the audit threshold.

These initiatives are far reaching in preventing misuse of USAID development funds and facilitating timely corrective actions. Lack of adequate audit coverage constitutes an unacceptable risk because, without such a control mechanism, financial accountability of program expenditures cannot be reasonably assured.

In March 1995, the Office of Inspector General (OIG) issued Audit Report No. 3-000-95-009 on USAID's implementation of a 1992 initiative to improve the financial management of its programs. The report concluded that most missions had implemented the general requirements of the financial audit management program and established audit inventory databases. However, complete coverage was impaired as a result of obstacles arising from host government restrictions and local audit firm capabilities.

In March 1998, the OIG issued Audit Report No. 9-000-98-002-F on USAID missions' roles in obtaining audits of their contracts, grants and cooperative agreements. The report concluded that 11 of the 14 USAID missions selected worldwide generally obtained audits of their contracts, grants, and cooperative agreements as required by ADS Chapter 591, but that a significant number of required audits were not completed.

In May 1999, OIG management decided to verify the accuracy of USAID missions' recipient audit universe worldwide over a period of three years because lack of audit coverage was perceived as a high-risk area. Accordingly, RIG/Pretoria included this audit in our fiscal year 2001 audit plan.

Audit Objective

RIG/Pretoria performed this audit to answer the following question:

> **Is USAID/South Africa's audit universe complete and accurate, and are required audits done in a timely manner?**

The audit scope and methodology are described in Appendix I.

Audit Findings

> **Is USAID/South Africa's audit universe complete and accurate, and are required audits done in a timely manner?**

The audit showed that USAID/South Africa (Mission) maintained a complete and accurate recipient audit universe; however 13, or 45 percent, of the 29 required audits were not done in a timely manner. (The Scope and Methodology section describes our sampling methodology.)

For those agreements that met the audit threshold during our defined audit period covering three fiscal years (October 1, 1997 through December 31, 2000), USAID/South Africa disbursed approximately $173 million to U.S. organizations and $23 million to non-U.S. organizations. The table below

provides a breakdown of these disbursements by recipient and type of agreement:

	U.S. RECIPIENTS[1]		NON-U.S. RECIPIENTS		TOTAL	
TYPE OF AGREEMENT	**CUMULATIVE DISBURSEMENTS & NUMBER OF RECIPIENT AGREEMENTS**					
Project Implementation Letter	$0	0	$5,215,004	4	$5,215,004	4
Contract	124,810,544	32	0	0	124,810,544	32
Grant	13,109,936	6	7,085,193	11	20,195,129	17
Cooperative Agreement	35,247,758	13	11,026,476	8	46,274,234	21
TOTAL	$173,168,238	51	$23,326,673	23	$196,494,911	74

We ascertained that the Mission's recipient audit universe was complete, and included the U.S. and non-U.S. recipients' agreements that we reviewed. In addition, we verified that the agreements contained the required audit clauses.

Further, the Mission implemented an audit management program in accordance with the requirements of ADS Chapter 591, which included:

- establishing a Management Control Review Committee (MCRC) to monitor the status of the Mission's audit program and to assure that its audit responsibilities were carried out;

- designating an audit management officer to coordinate and monitor the Mission's financial audit program, and follow up on the implementation of recipient-contracted audit recommendations;

- stipulating required audit clauses in its grants, cooperative agreements and contracts, and budgeting funds for audits; and

[1] USAID/Washington is responsible for the audit coverage of the 51 U.S. recipient agreements that met the audit threshold.

- maintaining an automated inventory of contracts, grants, and cooperative agreements for use in determining audit requirements.

However, not all the required audits were submitted in a timely manner, as discussed below.

Emphasis Needed to Ensure Required Audit Reports Are Received

With regard to timeliness, for the sampled 23 non-U.S. recipients' agreements identified in the foregoing table, 29 audits were required during the period October 1, 1997 through December 31, 2000. However, at the time of our review, only 16 reports had been submitted to USAID/South Africa. And, four of the 16 reports were submitted from one to seven months late. The remaining 13 audit reports, covering approximately $11.4 million in disbursements, had not been submitted and were one to two years overdue. This occurred because the MCRC did not regularly monitor the status of outstanding reports.

To comply with ADS 591.3, the Mission Order established the MCRC through which Mission management takes the leadership role and assures that its audit monitoring responsibilities are fully carried out. The Mission Order requires the audit management officer to advise and report to the MCRC on the status of the Mission's audit management and resolution system.

In reviewing ADS 591.3 and the Mission Order, we considered the roles of the audit management officer, team leaders, and project officers in assuring smooth implementation of the Mission's audit management and resolution program. In our opinion, it is the MCRC's responsibility, which is chaired by the Deputy Director and includes the audit management officer and other responsible officials, to assure that the Mission's audit monitoring responsibilities are fully carried out.

Mission officials stated that the MCRC meetings addressed topics pertaining to its yearly Federal Managers' Financial Integrity Act submission; it never discussed whether its audit monitoring responsibilities were being carried out. The audit management officer stated that the MCRC's last meeting was in September 2000, and prior to that in September 1999. But, minutes were not kept to document what was covered at these meetings.

In our opinion, the Mission Order needs to specify, at a minimum, that periodic meetings should be held to discuss audit requirements, and address any problems needing attention to ensure that audit monitoring responsibilities are being carried out. This should include conducting follow-up on any outstanding audit reports. In addition, the results of these meetings should be documented. This would provide the management oversight needed to ensure

timely action and resolution of any outstanding issues or problems. Mission officials agreed and further stated that periodic Project Implementation Review meetings would be the best forum to address the timeliness of submitting audit reports and any problems to ensure that audit monitoring responsibilities are being carried out.

Furthermore, we noted that Mission Order 813 needed revisions that could improve controls. For example, Mission Order 813, dated March 23, 1998, requires audits be submitted 13 months after the end of the recipient's fiscal year. This requirement has been changed to nine months for grants, cooperative agreements and contracts signed beginning July 1998, as per ADS E591.5.4.e. However, the Mission Order does not reflect this change.

Therefore, we are making the following recommendations:

Recommendation No. 1: We recommend that USAID/South Africa establish a plan of action to review its entire audit universe and obtain all past due audit reports from recipients.

Recommendation No. 2: We recommend that USAID/South Africa revise Mission Order 813 to be consistent with ADS Chapter E591 and include, at a minimum, that periodic documented meetings be held to ensure that audit monitoring responsibilities are being carried out, and all required reports are submitted.

Management Comments and Our Evaluation

USAID/South Africa concurred with our audit findings and recommendations contained in the report, and advised RIG/Pretoria of the actions planned and/or taken to address the recommendations.

Recommendation No. 1 states that USAID/South Africa establish a plan of action to review its entire audit universe and obtain all past due audit reports. Mission management implemented a plan immediately, which is scheduled for completion in early October 2001. Therefore, a management decision has been reached on Recommendation No. 1.

Recommendation No. 2 states that USAID/South Africa revise its Mission Order to ensure that audit monitoring responsibilities are carried out. The Mission has revised Mission Order 813, which is in the clearance process, to address the recommendation. Therefore, a management decision has been reached on Recommendation No. 2.

The complete text of the Mission's comments is included in Appendix II.

Scope and Methodology

Scope

The audit was performed in accordance with generally accepted government auditing standards, and ascertained whether (1) USAID/South Africa's audit universe was complete and accurate, and (2) required audits were done in a timely manner.

The OIG conducted a "Worldwide Audit of Selected Missions' Role in Obtaining Audits of Their Contracts, Grants and Cooperative Agreements" (Report No. 9-000-98-002-F, March 20, 1998). That report considered recipient financial audits which had been completed as of October 31, 1996. For the purposes of this audit, we obtained information on audits due and/or completed from October 1, 1997 through December 31, 2000, covering three fiscal years – 1998, 1999, and 2000. (USAID/South Africa's recipient audit inventory file was maintained as of December 31, 2000; therefore, our scope was extended from September 30, 2000 to December 31, 2000.) Further, upon the advice of the RIG/Pretoria management, we limited our review to those agreements that were statistically selected from the Mission's audit universe. This decision was made due to the magnitude of the Mission's audit universe as well as constraints in time and resources.

Fieldwork was performed at USAID/South Africa in Pretoria, South Africa from February 7 – May 14, 2001, and covered approximately $23 million of USAID disbursements for non-U.S. recipients' agreements subject to audit. The audit scope included:

(1) reviewing the Mission's audit management program and related documents,

(2) interviewing cognizant Mission officials, and

(3) reviewing information from the Mission's automated database universe on contracts, grants, and cooperative agreements, and identifying those that require audits.

In addition, we obtained information on (1) total disbursement for all grants, contracts, project implementation letters and cooperative agreements (U.S. and non-U.S.) for USAID for the three-year period ended December 31, 2000, and (2) the number and amount of grants, project implementation letters, contracts, and cooperative agreements meeting the audit threshold of $100,000 or more a year in Federal awards received prior to July 1998 and $300,000 or more a year in disbursements on or after July 1998 to form a complete picture of the Mission's portfolio.

The relevant audit criteria included Chapter 591 of USAID's Automated Directives System (ADS), USAID/South Africa's Mission Order 813, *Audit Management and Resolution Program*, dated March 1998, and the OIG's "Guidelines for Financial Audits Contracted by Foreign Recipients" (Guidelines), revised in July 1998.

Methodology

The methodology included (1) reviewing the Mission's audit inventory database system to determine if it contains the information needed to monitor and track required audits, (2) examining contracts, grants, project implementation letters, and cooperative agreements, and amounts committed and disbursed, (3) validating the disbursements as shown in the Mission's audit inventory database against the disbursements recorded in the MACS, and, (4) conducting interviews with cognizant officials to determine whether the Mission met its responsibilities established by ADS Chapter 591 and the Guidelines.

To answer our audit objective, we obtained the universe of USAID/South Africa's grants, contracts, project implementation letters and cooperative agreements, and determined the number and dollar amounts of all instruments for non-U.S. recipients subject to audit coverage as of December 31, 2000. As of December 31, 2000, USAID/South Africa's recipient audit universe contained a total of 277 non-U.S. agreements. To ensure the accuracy of USAID/South Africa's audit recipient inventory, we classified the agreements into three strata.

We randomly selected samples based on a stratified statistical sampling methodology. We utilized the services of the statistician located at OIG Headquarters Liaison and Coordination's Office. The sample was selected at a 95 percent confidence level and an error rate of 5 percent to give us a good and reliable sample. We considered error rates in excess of 5 percent significant. We sampled 121 of the 277 non-U.S. recipients' agreements for accuracy. The table below provides the selection criteria, total number of agreements and the number sampled.

Stratum	Selection Criteria of Non-U.S. Recipient Agreements	Total	Sampled
1	Did not meet either the defined audit period or set disbursement threshold	69	30
2	Met the defined audit period but not the set disbursement threshold	131	57
3	Met both the defined audit period and the set disbursement threshold	77	34
	Total	**277**	**121**

Of the 121 sampled agreements, 87 agreements tested under the first two selection criteria were generally accurate and complete. However, these agreements were not subject to audit coverage. Thirty of the 87 agreements did not meet either the defined audit period or the set disbursement threshold. The remaining 57 agreements met the defined audit period but not the disbursement threshold.

For the 34 remaining agreements tested under the third selection criteria, we found that 11 were not subject to audit because:

- 8 did not meet the set disbursement threshold;
- 2 were U.S. recipients that were erroneously classified as non-U.S. recipients by the financial analyst; and
- 1 was a fixed amount reimbursement agreement.

In regard to the agreements for the 23 non-U.S. recipients that were subject to audit coverage, we then determined whether: (1) required audits were completed in a timely manner; and (2) audit reports were prepared in accordance with USAID's guidelines and sent to RIG/Pretoria for desk review.

Management Comments

USAID

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

Memorandum

DATE: July 11, 2001

TO: Nancy Lawton, A/RIG

FROM: Eilene Oldwine, A/DIR /s/

SUBJECT: Audit of the Accuracy of USAID/South Africa's Recipient Audit Universe

We concur with the two audit recommendations discussed at the de-briefing held June 8, 2001 in the draft audit report.

The following actions have been planned or addressed:

Recommendation No 1: We recommend that USAID/South Africa establish a plan of action to review its entire audit universe and obtain all past due audit reports from recipients.

Action:

a. A plan of action to review the audit universe has been discussed with the Financial Analysts and is being implemented immediately and is scheduled to be completed within three months (October 10, 2001). This includes MACS Intelligence Query (IQ) reports being developed and run and matched against the current database to verify agreements and end dates on the tracking report. Additionally copies of the tracking report will be sent to Strategic Objective Team Leaders and the Director's Office quarterly with a memo requesting them to action as appropriate and to notify the financial analyst if there are any missing agreement or inaccurate data on the report.

Recommendation No 2: We recommend that USAID/South Africa revise Mission Order 813 to specify at a minimum, that periodic meetings be held and documented to ensure that audit monitoring responsibilities are being carried out, including submission of all required reports.

Action:

a. Mission order 813 has been revised as recommended and is in the clearance process. The Project Implementation Reviews (PIR) take place twice a year and the status of recipient contracted audits is covered as part of the review. The entire Management Control Review Committee (MCRC) attends these meetings and it is more efficient to cover this along with other implementation issues rather than having a separate meeting. The revision to the mission order will include the requirement for submission of the audit within 9 months after the end of the recipients fiscal year.

b. Provisions have been made to include clearance of the Financial Analysts on all MAARDs. If there are outstanding audits then incremental funding will not be added, estimated completion dates will not be extended and new agreements will not be issued to an organization.

c. A clearance procedure for processing of program vouchers now includes checking a list provided to the Voucher Examiners on a weekly basis by the Financial Analyst of over due audits.

Management decisions have been reached on the two recommendations and the action necessary to address the are in process.

Cleared:
Eric Schaeffer, D/CONT /s/

Drafter:
Barbara Krell, CONT /s/