OFFICE OF INSPECTOR GENERAL

AUDIT OF USAID/ETHIOPIA'S COMPLIANCE WITH FINANCIAL AUDIT REQUIREMENTS REGARDING FOREIGN RECIPIENTS

AUDIT REPORT NO. 4-663-06-009-P

May 31, 2006

PRETORIA, SOUTH AFRICA

Office of Inspector General

May 31, 2006

MEMORANDUM

TO: USAID/Ethiopia Mission Director, William Hammink

FROM: RIG/Pretoria, Jay Rollins /s/

SUBJECT: Audit of USAID/Ethiopia's Compliance with Financial Audit Requirements Regarding Foreign Recipients (Report No. 4-663-06-009-P)

This memorandum transmits our draft report on the subject audit. In finalizing this report, we considered management comments on the draft report and have included those comments, in their entirety, as Appendix II.

The report has seven recommendations to help USAID/Ethiopia improve its financial audit program with regard to foreign recipients. For Recommendation Nos. 4, 6, and 7, the Mission provided evidence that corrective actions have been implemented. Therefore, we consider Recommendation Nos. 4, 6, and 7 to have received final action upon issuance of this report. For Recommendation Nos. 1, 2, 3, and 5, the Mission provided agreement, corrective action plans, and target completion dates. Therefore, we consider that a management decision has been reached for Recommendation Nos. 1, 2, 3, and 5. Please provide the Audit, Performance and Compliance Division (M/CFO/APC) with evidence of final action in order to close these recommendations.

I appreciate the cooperation and courtesy extended to my staff throughout the audit.

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CONTENTS

SUMMARY OF RESULTS

The Regional Inspector General/Pretoria performed this audit to determine whether USAID/Ethiopia effectively managed its financial audit program in accordance with USAID policies and procedures for fiscal years 2003, 2004, and 2005. (See page 2.)

USAID/Ethiopia did not effectively manage its financial audit program regarding foreign recipients during the period covered by the audit. Specifically, USAID/Ethiopia did not ensure that planned audits of foreign recipients were performed in a timely manner, delinquent audits were followed up on and completed, or standard statements of work were used. To help correct and strengthen these problem areas, we recommended that USAID/Ethiopia 1) develop and implement an audit tracking system to better monitor and ensure timely submission of planned audits, 2) complete all identified delinquent audits, and 3) develop a system to ensure that standard statements of work are included in future audit agreements. (See pages 5 – 9.)

In addition, although USAID/Ethiopia prepared annual audit plans for fiscal years 2003-2005, those plans were incomplete. Specifically, the plans omitted required closeout audits for 23 expired awards with amounts totaling $109.6 million. Also, two of the Mission's host country contracts were not included in its award inventories. We recommended that USAID/Ethiopia 1) amend its Mission Order dealing with recipient audits to ensure that expiring awards requiring closeout audits are included in future audit plans, 2) obtain and submit audit reports for all expired awards requiring closeout audits, 3) include identified host country contracts in the current award inventory, and 4) amend Mission Order 504 to ensure that host country contracts are included in future award inventories and audit plans. (See pages 9 - 13.)

For Recommendation Nos. 4, 6, and 7, the Mission provided evidence that corrective actions have been implemented. Therefore, we consider Recommendation Nos. 4, 6, and 7 to have received final action upon issuance of this report. For Recommendation Nos. 1, 2, 3, and 5, the Mission provided agreement, corrective action plans, and target completion dates. Therefore, we consider that a management decision has been reached for Recommendation Nos. 1, 2, 3, and 5. (See page 14.)

BACKGROUND

USAID administers most of its foreign assistance programs by awarding contracts, grants and cooperative agreements to U.S.-based and foreign organizations. In order to help ensure accountability over funds given to such organizations, USAID and the Office of Inspector General (OIG) have jointly developed a financial audit program as outlined in Automated Directive System (ADS) 591. This section of the ADS requires that USAID missions, in consultation with the cognizant Regional Inspector General (RIG), ensure that required financial audits are conducted for foreign for-profit and nonprofit organizations and host government entities (including any mission-funded activities in nonpresence countries), and local currency special accounts.

All foreign nonprofit organizations expending more than $300,000 of USAID funds during their fiscal year are required to have an annual financial audit performed. A closeout audit is required for recipients expending more than $500,000 throughout the life of an award. Incurred cost audits must be performed annually of all foreign for-profit organizations performing under direct awards or cost reimbursable host country contracts and subcontracts.[1] To ensure that such audits are performed in a timely and acceptable manner, missions are required to develop annual audit plans which are populated from inventories maintained by the missions of all contracts, grants and cooperative agreements, including cash transfer and nonproject assistance grants, awards financed with host country owned local currency and activities in nonpresence countries for use in determining audit requirements.

The audits are normally performed by independent auditors acceptable to the cognizant RIG office. The audit agreements between recipients and independent auditors contain a standard statement of work. On occasion, USAID missions may contract directly with an audit firm to conduct financial audits of foreign recipients or locally-incurred costs of U.S.-based recipients. Audits of USAID recipients are required to be performed in accordance with U.S. Government Auditing Standards as well as the OIG's Guidelines for Financial Audits Contracted by Foreign Recipients. Missions must ensure that such audit reports are submitted to the cognizant RIG office for review and issuance no later than nine months following the end of the audited period.

USAID/Ethiopia is one of the USAID missions in the Eastern and Southern Africa region with a large number of recipients. In fiscal year 2005, the Mission had 64 non-U.S.-based recipients. During fiscal years 2003-2005, the Mission reported budget authorizations totaling $537.6 million for programs in:

- Food Security
- Essential Services for Health
- Basic Education
- Democracy and Governance
- Mitigate the Effects of Disaster

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[1] In terms of a 2005 revision to ADS 591, there is no automatic requirement for annual incurred cost audits for foreign for-profit organizations. Instead, Missions are required to annually assess risks to determine whether financial audits are warranted and the results of these risk assessments must be shared with the cognizant RIG office.

- Anticipate and Manage Shocks
- Human Capacity
- Governance Capacity
- Economic Growth
- Knowledge Management

For fiscal year 2003, alone, the actual amount for Public Law 480, Title II program, as reported in the Congressional Budget Justification, was over $352.2 million.

AUDIT OBJECTIVES

An audit of the Mission's compliance with financial audit requirements regarding foreign recipients was performed because Regional Inspector General/Pretoria's (RIG/Pretoria) experience is that USAID missions in eastern and southern Africa have generally not been complying with Automated Directives System (ADS) 591 in terms of ensuring that required financial audits of foreign recipients are conducted in a timely and acceptable manner. To determine USAID/Ethiopia's compliance with USAID rules and regulations regarding financial audits of its foreign recipients, the audit was performed to answer the following questions:

Objective No. 1: Did USAID/Ethiopia ensure that planned financial audits of foreign recipients were performed and submitted in accordance with USAID rules and regulations?

Objective No. 2: Did USAID/Ethiopia ensure that annual audit plans included all recipients from their award inventory that required a financial audit?

AUDIT FINDINGS

Did USAID/Ethiopia ensure that planned financial audits of foreign recipients were performed and submitted in accordance with USAID rules and regulations?

USAID/Ethiopia did not ensure that all planned financial audits of foreign recipients[2] were performed and submitted in accordance with USAID rules and regulations.

During the last three years, USAID/Ethiopia has made a great deal of progress towards improving its recipient financial audit program. USAID/Ethiopia has planned for and submitted its audit inventories and plans to RIG/Pretoria for 2003 - 2005. Since April 30, 2003, RIG/Pretoria has issued 14 financial audit reports of USAID/Ethiopia recipients covering $13.5 million in expenditures of USAID funds. Those audit reports included recommendations that addressed $2 million in questioned costs, 20 internal control weaknesses, and 22 instances of material noncompliance with applicable laws and regulations.

While the above financial audit work has undoubtedly had a positive effect on USAID/Ethiopia's accountability over USAID funds expended by foreign recipients, there were several areas in which USAID/Ethiopia could improve its recipient financial audit program including timeliness, follow-up on delinquent audits, and use of a standard statement of work.

Audit Reports Not Submitted Within Required Timeframe

Summary: According to Agency regulations, USAID missions must submit audit reports of foreign recipients to the cognizant Regional Inspector General (RIG) no later than nine months after the end of the audited period. USAID/Ethiopia submitted 19 of the 37 audits planned for fiscal years 2003 to 2005. All 19 were submitted to RIG/Pretoria after the required timeframe. This occurred because USAID/Ethiopia had not developed a system to track and follow up on planned audits. Also, many audit reports had to be corrected and resubmitted due to noncompliance with applicable standards and guidelines. Audits that are not completed in a timely manner reduce USAID's accountability over funds awarded to recipients.

Automated Directive System (ADS) 591.3.2.1 requires that foreign nonprofit organizations and host governments that expend $300,000 or more of USAID funds during their fiscal year must have an annual audit conducted in accordance with the Office of Inspector General's *Guidelines for Financial Audits Contracted by Foreign Recipients* (Guidelines). Paragraphs 1.16 and 2.3 of the Guidelines spell out the timeframe within which recipients must submit final audit reports to the cognizant USAID

[2] For the purpose of this audit, foreign recipients include non-U.S.-based grantees and contractors who were awarded grants, contracts, cooperative agreements and implementation letters.

mission, which, in turn, will forward them to the RIG for review and issuance. According to the Guidelines, the cognizant RIG must receive the audit report no later than nine months after the end of the audited period.

USAID/Ethiopia's annual audit plans prepared for fiscal years 2003, 2004, and 2005 included 37 distinct planned financial audits of 18 different recipients. The breakdown of the 37 audits is presented in Table 1 below.

Table 1
Recipient Audits in Annual Plans for Fiscal Years 2003-2005

Number of recipients	# of annual audits in plans	Totals
1	5	5
3	4	12
6	2	12
8	1	8
18		37

Only 19 (51 percent) of the 37 audits included in the Mission's audit plans for fiscal years 2003, 2004, and 2005 had been submitted to RIG/Pretoria as of December 31, 2005. On average, those audit reports were submitted 237 days (approximately 8 months) after they were due.

The lack of timeliness was caused by several factors. One of the principal factors was that the Mission had not developed or implemented an effective tracking system to ensure that the planned audits were performed and submitted within the required timeframe. As a result, not only were the majority of planned audits not submitted in a timely manner, but a number were not submitted at all. For example, only 19 of the 37 audits included in the Mission's audit plans for fiscal years 2003, 2004, and 2005 had been submitted to RIG/Pretoria as of December 31, 2005. Twelve audits (listed in Appendix III) had either not been performed, or, if performed, had not been submitted to RIG/Pretoria. The remaining six audits were not yet due as of December 31, 2005.

Further evidence that USAID/Ethiopia lacked an effective follow-up system was reflected by the fact that the Mission's audit plans for fiscal year 2005 included 9 delinquent audits[3], more than the number of planned audits for fiscal year 2003, as shown in the following table.

[3] Audit reports that are not received by the cognizant RIG within the timeframe set forth under paragraph 1.16 of the Guidelines for Financial Audits Contracted by Foreign Recipients are considered delinquent audits.

Table 2
Delinquent Audits from USAID/Ethiopia's Annual Audit Plans

	FY 2003	FY 2004	FY 2005	Totals
# of current audits in plan	7	9	16	32
# of delinquent audits in plan	0	0	9	9
Total # of audits in plan	7	9	25	41[4]

In several situations, "catch up" audits were performed that covered multiple years of expenditures by those recipients. For example, USAID/Ethiopia's audit plan for fiscal year 2003 included an audit of fiscal year 2002 expenditures by a recipient under a 5-year, $1.4 million USAID grant. This recipient was also included in the fiscal year 2004 audit plan. The audits were eventually completed in fiscal year 2004 covering the period July 1, 1999 to June 30, 2001, amounting to $749,331 in expenditures of USAID funds. The audit report questioned $21,708 in expenditures and identified three internal control weaknesses and two instances of material noncompliance with applicable laws and regulations.

As of December 31, 2005, USAID/Ethiopia had 12 planned audits from fiscal years 2003-2005 that were still delinquent. A list of the awards with delinquent audits is included as Appendix III in this report.

Another contributing factor was that the audit work did not comply with applicable standards and regulations. This resulted in audit reports received by RIG/Pretoria that often had to be sent back to the audit firms for correction or additional work. Although these reports were eventually corrected and resubmitted to RIG/Pretoria, the additional work required added to their lack of timeliness. (The cause of substandard audit work will be addressed in the following section of this report.)

Delayed performance and submission of audit reports reduces USAID's accountability over funds awarded to recipients. This also increases the risk that recipients' financial records are no longer available for audit, or that their offices may have ceased operations, making the determination and recovery of potential questioned costs difficult or impossible. Even when records do exist, or the recipient is still in operation, untimely audit reports lose their usefulness because management (USAID or recipient) cannot, based on the reports, implement corrective actions in a timely manner to help prevent potential fraud, waste and abuse. Total estimated expenditures that have not been audited as of December 31, 2005 amounted to over $10.4 million.

For the Mission to be able to submit timely audit reports to RIG/Pretoria, it must have a system to monitor the status of planned audits and dedicated personnel to provide interventions when targeted milestones are not being met. Therefore, we are making the following recommendations:

> *Recommendation No. 1: We recommend that USAID/Ethiopia develop and implement an audit tracking system to monitor the recipient financial audit*

[4] Although there was a total of 37 distinct audits in the Mission's audit plans for fiscal years 2003-2005, the annual audits of four other recipients were carried forward from one annual plan to the next without being accomplished bringing the total number of audits listed in all three plans to 41.

process to ensure timely submission of reports to RIG/Pretoria. This system should, at a minimum, include controls to ensure that:

- *appropriate timing targets and milestones are set for each audit in the Mission's current audit plan;*
- *audit instructions are sent to recipients prior to the recipient's fiscal year end requesting them to initiate the procurement for the audit;*
- *periodic follow-up is performed to determine the implementation status of all planned audits; and*
- *corrective actions are taken and documented for audits that are not progressing as planned.*

Recommendation No. 2: We recommend that USAID/Ethiopia obtain and submit all delinquent audit reports.

Standard Statement of Work Not Used in Every Audit

Summary: Agency policy requires that audit agreements between recipients and independent auditors contain a standard statement of work (SOW) that incorporates all the requirements of the OIG Guidelines. Not all of the agreements for financial audits of USAID/Ethiopia's recipients contained a standard SOW that was reviewed and approved by the Mission. This occurred because USAID/Ethiopia did not have a system to ensure that all audit agreements incorporated standard SOWs. The lack of a standard SOW has resulted in many audits being rejected by RIG/Pretoria due to lack of compliance with applicable auditing standards and guidelines.

According to the OIG's Guidelines for Financial Audits Contracted by Foreign Recipients (Guidelines), a mandatory reference in ADS 591, USAID missions must ensure that audit agreements between USAID recipients and independent auditors include a standard statement of work (SOW) containing all of the requirements of the Guidelines. To ensure that this requirement is complied with, recipients must send all prospective audit agreements to the cognizant USAID mission for approval prior to finalization, as stated in paragraph 1.14 of the Guidelines.

On January 10, 2006, RIG/Pretoria requested USAID/Ethiopia to provide evidence that, for the last 17 audit reports submitted, the Mission had reviewed and approved audit agreements between recipients and auditors, and that those agreements contained USAID's standard SOW. From the 17 sampled audits, only 4 (24 percent) had a standard SOW. The other 13 audits did not meet this requirement.

Although the Mission reported ensuring that the audit firms and the auditees received a copy of the OIG Guidelines, providing auditors and recipients with the Guidelines did not constitute the required review and approval of the audit agreement. Nor did it ensure that the standard SOW has been included as part of the audit agreement. In addition, since some audits were performed for the same recipient in different fiscal years, it should not be assumed that the standard SOW would still be effective for the following year. A new SOW should have been approved for each fiscal year audit.

The majority of recipient audits were not performed under agreements which included the standard SOW because USAID/Ethiopia did not have a system in place to ensure that all audit agreements were reviewed and approved by the Mission prior to the commencement of the audits. Therefore, the Mission could not ensure that the standard SOW was incorporated into those audit agreements.

Experience has shown that independent audit firms conducting USAID recipient audits without a standard SOW typically perform “statutory” audit work in accordance with local standards. Such audits do not address the unique fieldwork and reporting requirements of USAID audits relating to such areas as testing expenditures for eligibility, allocability, and compliance with U.S. laws and regulations. Financial audit requirements for USAID recipients differ substantially from statutory audit requirements within Ethiopia. Consequently, audits that are conducted without a Mission-approved agreement containing the standard SOW, which refers to the audit requirements in the OIG Guidelines, are less likely to be performed in accordance with U.S. Government Auditing Standards and/or the OIG Guidelines. This was reflected in the large percentage of recipient audit reports that RIG/Pretoria rejected due to lack of conformity with those standards and guidelines. Of the 19 reports submitted to RIG/Pretoria, 9 (47 percent) were initially rejected due to lack of compliance with applicable standards and guidelines.

The review and approval of prospective audit agreements, and the inclusion of a standard SOW in those agreements which references specific USAID audit requirements, will help prevent audits from being performed that do not comply with U.S. Government Auditing Standards and/or the OIG Guidelines. Once incorporated into the audit agreement, the standard SOW becomes binding and should compel the audit firms to comply with necessary USAID audit requirements. Therefore, we are making the following recommendation:

> *Recommendation No. 3: We recommend that USAID/Ethiopia develop and implement a system to ensure that the Mission reviews, approves and maintains a copy of an audit agreement containing a standard statement of work that incorporates USAID’s audit requirements for every recipient audit covering each individual fiscal year .*

Did USAID/Ethiopia ensure that annual audit plans included all recipients from their award inventory that required a financial audit?

USAID Ethiopia did not ensure that annual audit plans included all recipients from their award inventories that required a financial audit.

As required by ADS 591.3.4.2, USAID/Ethiopia developed award inventories for fiscal years 2003, 2004, and 2005 which included the required information for each award, such as contractor/grantee name, type of organization, award number, amount in U.S. dollars, start/completion dates, prior audits and period covered, receipt date for required audits, dates for planned audits, and reason(s) for not including an award in the annual audit plan. The Mission also developed an annual plan for each of those fiscal years which included 37 distinct audits of foreign recipients receiving awards listed in those inventories.

Although USAID/Ethiopia prepared the award inventories and related audit plans as required, not all awards that required audits were included in the audit plans. The Mission's audit inventory had several awards that required closeout audits but were not included in the audit plan. The details of this finding are discussed below.

Awards Requiring Closeout Audits Need To Be Included In Audit Plans

Summary: Agency policy requires that all awards in excess of $500,000 be subject to a final closeout audit. USAID/Ethiopia's annual audit plans omitted 23 expired direct awards that required closeout audits. This occurred because Mission officials were unaware that closeout audits were required. As a result, USAID-funded awards totaling $109.6 million that should have received closeout audits have not.

Automated Directives System (ADS) 591.3.3.2 states that "Contract Information Bulletin (CIB) 90-12 requires that all awards in excess of $500,000 be subject to a final close-out audit." This section of the ADS also states that annual audits, performed in accordance with the "Guidelines for Financial Audits Contracted by Foreign Recipients" must be accepted as fulfilling the close-out audit requirements for foreign nonprofit organizations.

The intent of CIB 90-12 was to ensure that awards[5] that did not exceed the $300,000 threshold for requiring an annual audit, but that amounted to significant amounts of expenditures on a cumulative basis, were audited to ensure proper closeout of the award. The Mission's award inventories included columns such as "Prior Audits & Dates Covered" and "Reason not in Audit Plan." The data from these columns provided information as to the most recent annual audit prior to the recipient's award completion date. This information was used to determine whether a close-out audit was required for a given recipient.

USAID/Ethiopia's award inventories for fiscal years 2003, 2004, and 2005 included 8 recipients with 23 expired direct awards over the $500,000 threshold which were not included in the Mission's respective annual audit plans. According to the Mission's award inventory for fiscal years 2003 – 2005, these expired awards had no recent annual audits that might have served as closeout audits per ADS 591.3.3.2 Consequently, required closeout audits were not conducted for those awards. A list of the 23 awards requiring closeout audits is included as Appendix IV in this report. The following table presents the aging of the unaudited expired awards as of December 31, 2005. As shown in the table, the majority of these awards expired more than five years ago, indicating that this has been a long-standing problem.

[5] For the purpose of this audit, awards include grants, contracts, cooperative agreements, and implementation letters.

Table 3
Aging of Expired Awards Requiring Closeout Audits
(years since expiration of award)

0-1 yr.	2-3 yrs.	4-5 yrs.	Over 5 yrs.	Total
0	5	2	16	23

Mission officials did not include these expired awards in annual audit plans because they were unaware of the policy regarding closeout audits. The reasons listed in the Mission's award inventories for not including such awards in the annual audit plans included statements such as "Expired Award," "Directly paid for debt settlement," and "Estimated Expenditure less than $300,000." Also, USAID/Ethiopia's Mission Order No. 504, *Audit and Management Control Review Committee,* did not include any procedures regarding the planning or performance of closeout audits of awards exceeding $500,000.

As a result, 23 expired direct awards that should have received closeout audits remain unaudited. The amount of USAID funding included in those awards totaled $109.6 million.

Closeout audits are important tools in the control and accountability of USAID funds. Such audits may be used, among other things, to finalize indirect cost rates and to determine whether the disposition of USAID-funded assets was properly performed at the end of a project or activity. A closeout audit of expenditures of USAID funds would be especially important when a recipient may have expended less than $300,000 in any single year, but the total award was over $500,000. Such recipients may never have been subjected to a USAID audit as required. Further, according to ADS 591.3.3.2, Contract/Grant Officers cannot proceed with the closeout process until final action has been taken on all audit recommendations. Finally, because they were not included in the Mission's audit plans during the period they were due, such audits would not likely be performed within the required timeframe. We are, therefore, making the following recommendations:

> *Recommendation No. 4: We recommend that USAID/Ethiopia amend its Mission Order 504 to ensure that closeout audits of expiring awards in excess of $500,000 are included in future audit plans and performed as required.*

> *Recommendation No. 5: We recommend that USAID/Ethiopia obtain and submit audit reports in accordance with Guidelines requirements for all expired awards requiring closeout audits.*

Host Country Contracts Need To Be Included in Award Inventories

Summary: Agency policy requires missions to maintain an inventory of all awards from which annual audit plans may be developed. Agency policy also dictates that host country contracts[6] are subject to the same USAID audit requirements as direct contracts. Two host country contracts, active during fiscal year 2005, were not included in the Mission's award inventory. This occurred because Mission officials were not aware that host country contracts needed to be included in award inventories, or that host country contracts were subject to USAID audit requirements. Although the two host country contracts totaling $394,282 were below the audit thresholds, these contracts must still be included in the Mission's award inventory.

ADS 591.3.4.2 requires missions to "maintain an inventory of all contracts, grants and cooperative agreements, including cash transfer and nonproject assistance grants, awards financed with host country-owned local currency, and activities in nonpresence countries for use in determining audit requirements." Country Contracting Handbook section 3.8 states that an audit of non-U.S.-based firms shall be a cost-incurred, financial audit performed by the principal audit agency to the host country or an independent audit agency acceptable to USAID Inspector General and as set forth in the Strategic Objective Agreement (SOAG) or a SOAG Implementation Letter. It further adds that the Guidelines should be followed in the selection of auditors and that the auditors should observe the Guidelines in planning, conducting, and reporting the results of the audit. Moreover, section 3.9 of the Country Contracting Handbook specifically states that "Final payment to the contractor is withheld until the contractor provides evidence that it has met all of its obligations under the contract and all required certifications (including acceptance of the work by the Contracting Agency) have been executed and the contract has been **audited**, as provided above. The USAID Activity Manager will be notified of contract closeout and contract files will be maintained in storage at least three years from the final disbursement under the SOAG." (emphasis added)

RIG/Pretoria obtained a list of USAID-funded host country contracts from USAID/Ethiopia that were active during the fiscal years 2003-2005. A comparison of this list to the Mission's award inventories revealed that two of the host country contracts, with amounts totaling $394,282, were not included in the award inventory as shown in the following table:

Table 4
Host Country Contracts Not Included in Award Inventory

Award Number	Recipient's Fiscal Year End	Award Amount (In US $)
IL-663-04-01	9/30/2005	285,063
IL-663-0080-20	2/1/2006	109,219
Total		394,282

[6] ADS Glossary defines Host Country Contracting as "A means of program implementation in which USAID finances, but is not a party to, contractual arrangements between the host country and the supplier of goods and/or services." ADS 301.5.1a states that when USAID decides to use host country contracting procedures – it acts as financier and not a contracting party, reserving certain rights of approval and activity monitoring.

This occurred because Mission officials were unaware that host country contracts should have been included in the Mission's award inventories and considered for potential financial audits. Consequently, two host country contracts, with amounts totaling $394,282 were not included in the Mission's award inventory and were not considered for inclusion in the Mission's annual audit plan for receiving potential financial audits.

To prevent the omission of host country contracts from the Mission's award inventories, and possibly the annual audit plans, in the future, we are making the following recommendations:

Recommendation No. 6: We recommend that USAID/Ethiopia include all host country contracts in its award inventory for fiscal year 2006.

Recommendation No. 7: We recommend that USAID/Ethiopia amend Mission Order 504 to include procedures for including host country contracts in award inventories and annual audit plans, as appropriate.

EVALUATION OF MANAGEMENT COMMENTS

In response to our draft report, USAID/Ethiopia agreed with all seven recommendations. For Recommendation Nos. 4, 6, and 7, the Mission provided evidence that corrective actions have been implemented. Therefore, we consider Recommendation Nos. 4, 6, and 7 to have received final action upon issuance of this report.

For Recommendation Nos. 1, 2, 3, and 5, the Mission provided agreement, corrective action plans, and target completion dates. Therefore, we consider that a management decision has been reached for Recommendation Nos. 1, 2, 3, and 5.

SCOPE AND METHODOLOGY

Scope

The Regional Inspector General/Pretoria performed this audit in accordance with generally accepted government auditing standards. The audit was performed at the office of the Regional Inspector General in Pretoria, South Africa during the period December 14, 2005 though March 10, 2006.

The audit covered financial audit requirements for USAID/Ethiopia's awards to non-U.S.-based recipients during fiscal years 2003, 2004, and 2005.

The type of evidence examined during the audit included, but was not limited to, award inventories and audit plans submitted by the Mission for fiscal years 2003-2005, RIG/Pretoria's Audit Management Database and archives, and correspondence from the Mission.

For the most part, we relied on the accuracy and completeness of the award inventories that were submitted by the Mission to RIG/Pretoria because we believe that the responsibility for preparing award inventories rests with the Mission's Audit Management Officer, who should have the technical capacity to prepare reliable award inventories. The primary focus of our audit was the development and execution of the annual audit plans from those award inventories. Thus, with few exceptions, we limited our procedures to determine whether data in the award inventories were properly used to develop the audit plans and whether those audit plans were executed in an acceptable and timely manner. We recognize the limitations of our reliance on the accuracy and completeness of the award inventories, and hereby disclose this in the audit report--the primary limitation being that all awards requiring a financial audit may not have been included in the Mission's award inventories. Further, expiration dates and total amounts of awards in inventories may not have been accurate.

With regard to internal controls, we assessed:

- award inventories;
- audit plans; and
- mission orders regarding financial audits.

Methodology

To accomplish the audit objectives, we reviewed and analyzed the annual audit plans and award inventories submitted to RIG/Pretoria for fiscal years 2003, 2004 and 2005 for USAID/Ethiopia. We compared audit reports actually submitted to RIG/Pretoria to planned audits listed in the Mission's audit plans in order to determine the timeliness of the submission. We compared the audit plans to the award inventories to determine the accuracy of the audit plans. To determine recipients requiring closeout audits, we reviewed the Mission's award inventories and selected awards above $500,000 that were not subject to an annual audit in the eleven-month period prior to the program completion date. The audit also included a review of correspondence between RIG/Pretoria and the Mission regarding award inventories and annual audit plans. We also requested additional information from the Mission when required.

For materiality thresholds, we considered the following to be material:

- timeliness of submission of audit reports - if the number of acceptable audit reports submitted after the 9-month due date was > 10 percent of the number of planned audits, we considered the lack of timeliness to be material;

- delinquent audit reports – any number of delinquent planned audit reports was considered to be material; and

- completeness and accuracy of audit plans – any number of required audits not included in the audit plans was considered to be material.

This was one of a total of nine similar audits that we are performing of USAID missions within the eastern and southern Africa region. As RIG/Pretoria already possesses most of the information needed to conduct the audits, we did not consider travel to the locations of the respective missions to be necessary. Any questions regarding audit procedures or preliminary results were handled via email or telephone.

MANAGEMENT COMMENTS

Date: May 15, 2006

To: Jay Rollins, Regional Inspector General

From: William Hammink, USAID/Ethiopia Director /s/

Subject: Mission Comments on Report No. 4-663-06-XXX-P (Audit of USAID/Ethiopia's Compliance with Financial Audit Requirements Regarding Foreign Recipients)

This memorandum contains USAID/Ethiopia's comments on the subject audit report transmitted on March 30, 2006. We appreciate the auditors' assessment and assistance in strengthening the Mission's financial audit systems during the past three years. Per review of the subject audit report, the following is USAID/Ethiopia's management response and plan of action.

Recommendation No. 1: We recommend that USAID/Ethiopia develop and implement an audit tracking system to monitor the recipient financial audit process to ensure timely submission of reports to RIG/Pretoria. This system should, at a minimum, include controls to ensure that:

- **appropriate timing targets and milestones are set for each audit in the Mission's current audit plan;**
- **audit instructions are sent to recipients prior to the recipient's fiscal year end requesting them to initiate the procurement for the audit;**
- **periodic follow-up is performed to determine the implementation status of all planned audits; and**
- **corrective actions are taken and documented for audits that are not progressing as planned.**

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Management Response:
The Mission already has an audit/assessment management plan that addresses most of the points made in the above recommendation, and agrees with the above recommendation to strengthen the Mission's existing audit/assessment management plan. An additional column has been added to the plan to facilitate the monitoring of transmission of audit instructions to the auditees prior to the recipient's fiscal year end. USAID/Ethiopia will request closure of this recommendation from M/APC once the audit/assessment management plan has been updated for the FY 2006 audits. The Mission plans on completing final action by August 31, 2006.

Recommendation No. 2: We recommend that USAID/Ethiopia obtain and submit all delinquent audit reports.

Management Response:
The Mission agrees to complete the submission of the delinquent audit reports identified in Appendix III, or to provide the necessary documentation to M/APC as to why specific audit reports are not required. Four of the twelve audit reports listed in Appendix III have been submitted to RIG/Pretoria and the Mission anticipates that final action on the remaining reports will be completed by November 30, 2006.

Recommendation No. 3: We recommend that USAID/Ethiopia develop and implement a system to ensure that the Mission reviews, approves and maintains a copy of an audit agreement containing a standard statement of work that incorporates USAID's audit requirements for every recipient audit covering each individual fiscal year.

Management Response:
The Mission agrees with this audit recommendation, and believes that the necessary actions have been initiated. A column has been added to the Mission's existing audit/assessment management plan to assist in verifying that a copy of each audit agreement containing the USAID approved standard statement of work is on file. (Please see attached.) The Mission will request closure of this recommendation from M/APC once this information has been completed for the FY 2005/2006 audits. The Mission plans on completing final action by August 31, 2006.

Recommendation No. 4: We recommend that USAID/Ethiopia amend its Mission Order No. 504 to ensure that closeout audits of expiring awards in excess of $500,000 are included in future audit plans and performed as required.

Management Response:
In compliance with the above audit recommendation, Mission Order No. 504 has been amended to include specific reference to the requirement for closeout audits (please see attached Mission Order). USAID/Ethiopia believes the necessary action has been taken to resolve this recommendation, and requests closure of this audit recommendation upon issuance of the final audit report.

Recommendation No. 5: We recommend that USAID/Ethiopia obtain and submit audit reports in accordance with Guidelines requirements for all expired awards requiring closeout audits.

Management Response:
The Mission agrees with the need to obtain and submit audit reports in accordance with the Guidelines' requirements for expired awards requiring closeout audits. Of the 23 awards listed as requiring closeout audits in Appendix IV, 16 are from the time period 1993 – 1998. Therefore, the Mission has focused on the seven awards in Appendix IV that date from 2001 to 2004. Upon researching these seven awards, it appears that none of the seven required closeout audits. To facilitate RIG/P's future reviews, USAID/Ethiopia will do a better job in the future of documenting the audit inventory when closeout audits are not required. To close this recommendation, the Mission will either provide the audit reports or provide the supporting documentation as to why closeout audits are not required to M/APC for the seven awards in Appendix IV that date from 2001 to 2004. The Mission anticipates that final action will be completed by June 30, 2006.

Recommendation No. 6: We recommend that USAID/Ethiopia include all host country contracts in its award inventory for fiscal year 2006.

Management Response:
USAID/Ethiopia concurs, and is in compliance, with this recommendation. The Mission does not differentiate between host country and non-host country contracts when preparing audit inventories. A review of the two host country contracts that are listed as having been improperly excluded in the FY 2005 award inventory indicates that these two host country contracts were not funded agreements at the time of submission of the fiscal year 2005 award inventory. IL-663-04-01 was finalized in August, 2005 and IL-663-0080-20 was not signed by the Government of Ethiopia until February, 2005. (Please see attachments.) Both these awards were included in the Mission's FY 2006 audit inventory which was submitted to RIG/P. USAID/Ethiopia believes the necessary action has been taken to resolve this recommendation, and requests closure of this audit recommendation upon issuance of the final audit report.

Recommendation No. 7: We recommend that USAID/Ethiopia amend Mission Order 504 to include procedures for including host country contracts in award inventories and annual audit plans, as appropriate.

Management Response:
As documented under Recommendation No. 6, the statement that "Mission officials were unaware that host country contracts should have been included in the Mission's award inventories and considered for potential financial audits" is inaccurate. However, in order to facilitate inclusion of host country contracts in Mission award inventories, Mission Order No. 504 has been amended to include specific reference to the requirement for including host country contracts in award inventories and annual audit plans, as appropriate (please see attached Mission Order). USAID/Ethiopia believes the necessary action has been taken to resolve this recommendation, and requests closure of this audit recommendation upon issuance of the final audit report.

The Mission appreciates the opportunity to respond to this audit report and to share with you the actions USAID/Ethiopia is taking to address the above audit recommendations.

LIST OF DELINQUENT AUDITS AS OF DECEMBER 31, 2005

	Award Number[7]	Recipient's Fiscal Year End	Total Amount of Award (in US $)	Estimated Annual Expenditures (in US $)[8]	# of Days Between Audit Report Due Date and 12/31/05
1	IL-663-0019-09; IL-663-0070-16	7/7/2004	488,108	138,252	268
2	IL-663-0019-11; IL-663-0070-16	7/7/2004	371,480	245,371	268
3	IL-663-0110-04, 7 & 8	6/30/2004	750,087	439,035	275
4	FSP-A-00-98-00032-05	12/31/2004	1,054,930	354,666	92
5	LSGA-663-03-02	7/7/2004	4,000,000	4,000,000	268
6	IL-663-0110-02 IL-663-0110-1	7/7/2004	316,527	151,364	268
7	LSGA-663-03-03	7/7/2004	400,000	400,000	268
8	IL-663-0080-17; IL-663-0080-18; IL-663-0017-09 & IL-663-0080-06	7/7/2004	665,234	325,539	268
9	PIL663-0015-28; IL-663-0015-39 & IL-663-0090-4	7/7/2003	1,307,343	1,307,343	633
10	PIL663-0015-26; IL-663-0090-3 & PIL663-0015-28	12/31/2003	808,037	808,037	457
11	663-A-00-03-00352; 663-A-00-02-00366; FFP-A-00-03-00-49-05; 663-A-00-03-00354; FFP-A-00-03-00004-07& DFD-G-00-04-0162	12/31/2004	10,695,679	2,048,142	92
12	663-A-00-02-00321 & 663-0015-A-00-5010-00	6/30/2004	4,692,927	2,918,844	275
	Totals		25,550,352	13,136,593	3,432

[7] ADS 591.3.2.1 requires a foreign recipient to have a single audit performed when it has expended over $300,000 of USAID funds. This audit should include all awards from which those funds were disbursed during the period audited. USAID/Ethiopia had recipients with several awards.

[8] The Mission's audit plans for fiscal years 2003-2005 provided the estimated annual expenditures.

LIST OF EXPIRED AWARDS REQUIRING CLOSEOUT AUDITS

	Award Number	Award Completion Date*	Total Amount of Award (in US $)	# of Days Between Audit Report Due Date and 12/31/05
1	PIL-663-0007-93-05	6/30/1993	500,000	4,293
2	GR-6630003.00-92-01	9/27/1993	1,000,000	4,204
3	GR-6630003-92-02	8/7/1995	2,000,000	3,525
4	GR-663-T-601E	8/7/1995	8,395,000	3,525
5	PIL9681007.63-20	6/8/1996	973,680	4,293
6	PIL9681007.63-22	6/30/1996	1,038,675	3,197
7	PIL-663-0014-07	3/14/1998	8,000,000	2,575
8	PIL-663-0016-06	9/30/1998	5,000,000	2,375
9	623-0002-A-00-2108-00	9/30/1993	526,446	4,201
10	663-C-00-01-00374	9/21/2001	930,053	1,288
11	663-C-00-01-00368	9/30/2001	652,261	1,279
12	663-0015-A00-5010-00	6/30/2002	2,884,820	1,006
13	IL-663-0080-05	6/30/2003	2,500,000	641
14	PIL-663-0014-15	6/30/2003	8,000,000	641
15	663-A-00-02-00381	March 31	636,981	789
16	663-A-00-02-00321	2/3/2004	1,025,142	423
17	DRA-663-T-601B	8/31/1993	15,003,000	4,231
18	DRA-663-T-601C	8/31/1993	4,051,000	4,231
19	DRA-663-T-601D	8/31/1993	4,051,000	4,231
20	DRA-663+T-0601	9/30/1993	5,000,000	4,201
21	DRA-663-T-0601	9/30/1993	1,339,000	4,201
22	DRA-663-T-0601A[9]	9/30/1993	28,637,828	4,201
23	DRA-663-T-604	8/10/1996	7,500,000	3,156
	Total		109,644,886	70,908

* This information was obtained from the Mission's award inventory for fiscal years 2003-2005.

[9] This award was presented in the Mission's award inventory with two different award amounts, which were combined in this appendix.

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