

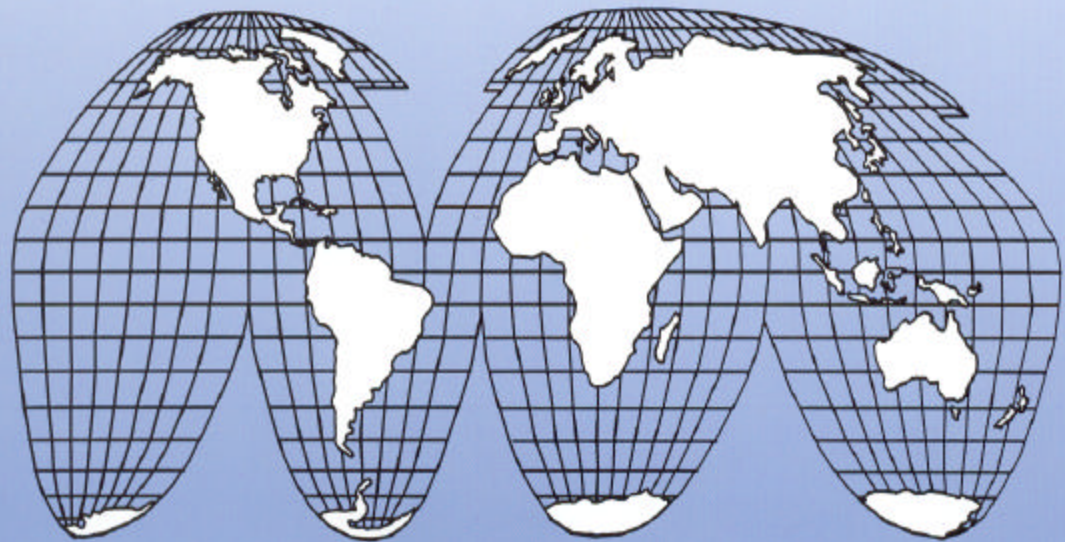
USAID

OFFICE OF INSPECTOR GENERAL

**Audit of USAID's Accrued Expenditures,
Accounts Payable, and Related Internal Controls
for Fiscal Year 2000**

Report No. 0-000-01-004-F

February 15, 2001



**OFFICE OF THE INSEPECTOR GENERAL
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT**



U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

MEMORANDUM FOR CFO, Michael T. Smokovich

FROM: IG/A/FA, Alvin A. Brown

SUBJECT: Independent Auditor's Report on USAID's Accrued Expenditures, Accounts Payable, and Related Internal Controls for Fiscal Year 2000.
Report No. 0-000-01-004-F

This memorandum audit report is our report on the U.S. Agency for International Development's (USAID) accrued expenditures, accounts payable, and related internal controls. The report is part of our audit of USAID's consolidated financial statements which is required by the Government Management and Reform Act of 1994. This report is one in a series of reports that communicate the results of our audits conducted on the selected line items reported in USAID's Fiscal Year 2000 Balance Sheet.

This report provides the results of our audit work performed to determine whether USAID properly calculated and reported its accrued expenditures and accounts payable to permit the preparation of reliable financial statements as of September 30, 2000. We were unable to determine whether USAID properly calculated and reported accrued expenditures and accounts payable to permit the preparation of reliable financial statements as of September 30, 2000. USAID changed its methodology for calculating and reporting accrued expenditures and related accounts payable and took action to improve its policies and procedures and the quality of the financial data recorded in the system. As result of the new methodology, USAID made material year-end adjustments to reverse the incorrect accrual calculations performed by the NMS and to record the accrual estimates derived from the application of the new accrual methodology. Due to time constraints, we were unable to evaluate the new methodology and determine the reliability of the balances reported.

Accordingly, the OIG is not expressing an opinion nor making any recommendations in this report. Instead, we will review USAID's new methodology and the implementation of its revised policies and procedures during our audit of USAID's fiscal year 2001 consolidated financial statements. See **Appendix II** for USAID Management's comments.

I would like to express my sincerest appreciation for the courtesies extended by your staff to the auditors over the past year.

BACKGROUND

USAID was created in 1961 to advance the United States' foreign policy interests by promoting broad-based sustainable development and providing humanitarian assistance. USAID has an overseas presence in 70 countries; 42 of which have fully operational and formal USAID missions.

Accounts payable systems for USAID consist of transactions and procedures associated with identifying, assembling, classifying, and recording transactions to report grants, contracts, and program and operating expenditures. The accounts payable line item on a balance sheet is established to record an entity's liability for goods and services received or work completed by a contractor for which payment has not been made.

In prior years we reported:

- In fiscal year 1997, USAID did not provide the OIG with USAID/Washington's accrued expenditure methodology until after the completion of our fieldwork. Therefore, the OIG did not have an adequate opportunity to review and test the methodology used.
- In our fiscal year 1998 audit report, the OIG reported that USAID/Washington's accrued expenditure methodology did not comply with the standards established by the Federal Accounting Standards Advisory Board (FASAB). USAID did not properly calculate and report its accrued expenditures and related accounts payable. USAID's methodology for calculating accounts payable at USAID/Washington was based on the scheduled completion date and the unliquidated obligation balance. In accordance with USAID's Office of Financial Management policy, these accounts payable were not accurately calculated at fiscal yearend. Accounts payable were recorded against dormant obligations with no activity during the prior 365 days or more. This material weakness impacted USAID's ability to prepare auditable financial statements.
- In fiscal year 1999, the OIG reported that the Office of Financial Management, did not make any changes in its methodology for calculating accrued expenditures USAID/Washington. Therefore, USAID's accrued expenditures and accounts payable were not properly calculated and reported to permit the preparation of reliable financial statements as of September 30, 1999. The OIG provided USAID with adjustments totaling about \$1.7 billion.¹

¹ Adjustments were noted in Report No. 0-000-00-004-F, issued February 9, 2000.

- As explained above, in previous years the OIG could not express an opinion on USAID's financial statements because our audit was impaired. Our audits of those years indicated that USAID's poorly functioning financial, accounting systems and other previously reported material internal control weaknesses caused this impairment. For those years, the OIG concluded that these deficiencies in USAID's accounting and financial management systems² created consequential risks that the financial statements could contain material misstatements. The amount of substantive testing required to express an opinion on the fairness of the presentation of USAID's financial statements would have been prohibitive and unattainable by the statutory deadline of March 1, for submitting the audited financial statements to the Office of Management and Budget (OMB) for those years. Accordingly, the OIG did not express an opinion on the fairness of the financial statements.

As a result of problems noted in prior year audits, the OIG, in agreement with USAID, decided to focus our fiscal year 2000 audit efforts on the material line items on its balance sheet.

AUDIT OBJECTIVE

This audit was performed to support the fiscal year 2000 Government Management and Reform Act (GMRA) audit of USAID's consolidated financial statements. For fiscal year 2000, the OIG agreed with USAID management to concentrate our audit efforts on selected major balance sheet items. Accordingly, the following is the objective of this audit:

Were USAID's Accrued Expenditures and Accounts Payable Properly Calculated And Reported to Permit the Preparation of Reliable Financial Statements as of September 30, 2000?

See Appendix I for a discussion of the scope and methodology for the audit.

The following section presents our findings for those matters that we consider reportable conditions and material weaknesses.

² According to OMB Circular A-127 and the Chief Financial Officers' Act, a financial management system includes supporting systems that contain the information needed to carry out financial management functions, manage financial operations, and report financial status information. The systems provide the information managers need to (1) carry out their fiduciary responsibilities; (2) deter fraud, waste, and abuse; and (3) relate financial consequences to agency program performance. Thus, in addition to basic accounting functions, USAID's financial management system includes supporting systems that perform performance measurement, budget, and procurement functions.

AUDIT FINDINGS

Were USAID's Accrued Expenditures and Accounts Payable Properly Calculated And Reported to Permit the Preparation of Reliable Financial Statements as of September 30, 2000?

We were unable to determine whether USAID properly calculated and reported accrued expenditures and accounts payable to permit the preparation of reliable financial statements as of September 30, 2000. Initially, USAID's plan was to use a statistical model to calculate accrued expenditures and related accounts payable for its Washington activities based on obligations recorded in the New Management System (NMS). However, USAID officials abandoned the planned process because of uncertainties about the accuracy of the scheduled completion dates for the contracts recorded in NMS. On December 12, 2000, USAID officials informed us that a new methodology was used to calculate accrued expenditures and related accounts payable, which resulted in an adjustment in excess of \$1.9 billion to this line item. Subsequently, on December 20, 2000, USAID officials informed us that this methodology was modified and an additional adjustment of \$300 million was recorded, for a total adjustment of about \$2.3 billion. The adjustments were necessary to reverse the incorrect accrual calculations performed by the NMS and to record the accrual estimates derived from the application of the new accrual methodology. The amount of substantive testing needed to evaluate the new methodology and determine the reasonableness of the adjustments would have been prohibitive and unattainable by the statutory deadline for submitting the audited financial statements to the Office of Management and Budget. Accordingly, we were unable to determine the reliability of the balances reported for accrued expenditures and related accounts payable.

We Could Not Determine Whether USAID's Methodology for Calculating Accrued Expenditures And Accounts Payable Met FASAB Standards

The basic accounting principle for calculating accrued expenditures and recording accounts payable at the end of an accounting period is to ensure that federal entities record expenditures in the appropriate accounting period and match those expenditures with revenues of that period. The Financial Accounting Standards Advisory Board (FASAB)³ does not believe that recognizing a liability prior to actual receipt or constructive receipt of goods or services should be adopted as a financial accounting standard.

³ On October 19, 1999 the AICPA officially designated FASAB as GAAP.

The Statement of Federal Financial Accounting Standards No.1, paragraph 77, provides that:

When an entity accepts title to goods, whether the goods are delivered or in-transit, the entity should recognize a liability for the unpaid amount of the goods. If invoices or those goods are not available when financial statements are prepared, the amounts owed should be estimated.

We were unable to determine whether USAID's methodology for calculating accrued expenditures and accounts payable for its Washington activities complied with the generally accepted accounting principles. Under USAID's planned statistical methodology for calculating its accrued expenditures and accounts payable, the estimates calculated for Washington would not be supported by actual or constructive receipt of goods and services.

Under its new methodology, the Office of Financial Management performed a trend analysis of the accounts payable calculated and reported during fiscal years 1997 through 1999 and the disbursements for the subsequent accounting periods to establish its accounts payable balance for fiscal year 2000. As a result of the new methodology, for fiscal year 2000, USAID made an adjustment in excess of \$2.3 billion—approximately 88 percent⁴ of the accrued expenditure amount initially calculated by NMS—to more accurately report accrued expenditures and accounts payable balances in its financial statements. Due to time constraints, we were unable to evaluate the new methodology and the reasonableness of the adjustments.

We noted several deficiencies with USAID's obligation balances maintained in NMS that would have been used by USAID in its previous methodology for calculating accrued expenditures and related accounts payable. See Appendix III for additional details.

The OIG will review USAID's new methodology in the future to determine whether it complies with generally accepted accounting principles and whether it reduces audit risk associated with this line item. Therefore, the OIG makes no recommendations for fiscal year 2000.

USAID Took Action To Improve Its Policies and Procedures

USAID took action to improve its policies and procedures and the quality of the financial data recorded in NMS. In prior years, we reported that USAID's unliquidated balances were not routinely reviewed and were not reliable for calculating accrued expenditures and accounts payable. USAID's financial managers agreed that system-generated information based on scheduled completion dates was not consistently reliable.

⁴ \$2.3 billion of the \$2.6 billion (approximately 88 percent) calculated for USAID/Washington accrued expenditures and accounts payable.

During fiscal year 2000 USAID:

- Implemented a project to review and deobligate those unnecessary unliquidated obligations established during fiscal year 1999 and prior periods. As a result, USAID deobligated over 1,200 obligations totaling about \$126 million and revised its policies and procedures for performing periodic 1311 reviews⁵.
- Provided obligation management training to financial management personnel, and
- Revised its Automated Directive System, Chapter 621, “Obligations” on September 11, 2000. This Automated Directive System policy requires assistant administrators and mission directors to certify that these procedures are being followed as a part of their annual budget submission.

The OIG will review USAID’s implementation of these actions during our audit of fiscal year 2001 consolidated financial statement.

MANAGEMENT COMMENTS AND OUR EVALUATION

USAID’s management, in general, agrees with the findings made in our report. The CFO explained that the \$2.3 billion adjustment made to the general ledger accounts was necessary to reverse the incorrect accrual estimates performed by the New Management System (NMS) and to record the accrual estimates derived from the application of the newly implemented accrual methodology. USAID’s management has proposed a new accrual methodology under the new accounting system, PHOENIX, which was placed in operation in December 2000. The OIG is pleased that management has taken steps to improve the agencies accrual estimates with the implementation of the trend analysis methodology used in FY 2000.

We look forward to working with management in reviewing this methodology during the FY 2001 audit of USAID’s accrual estimates.

⁵ 1311-reviews are periodic reviews of USAID unliquidated obligation balances that provide for effective fund management by financial managers.

SCOPE AND METHODOLOGY

SCOPE

For fiscal year 2000, the USAID Office of Inspector General (OIG) agreed with the Office of Financial Management to concentrate audit efforts on the selected major balance sheet items as was done in fiscal year 1999. Accordingly, the scope of this audit was limited to the review of USAID's accrued expenditures and accounts payable balances as of September 30, 2000. Therefore, this report does not contain an opinion about the fairness of the statements taken as a whole.

We did not conduct our audit in accordance with generally accepted government auditing standards because our scope was impaired.

Our primary focus was accrued expenditures and related accounts payable calculated for and reported for USAID/Washington by the New Management System (NMS). USAID reported \$3.4 billion on the balance sheet for accounts payable for fiscal year 2000. The accrued expenditures reviewed by the OIG accounted for approximately 78 percent⁶ of accounts payable.

Due to the limited scope of this audit, internal control testing was limited to those controls used to calculate and report the accounts payable for USAID/Washington.

USAID had no laws and regulations that were material to the calculation and reporting of accounts payable. Therefore, we did not conduct any compliance reviews.

⁶ Accrued expenditures reviewed divided by reported accounts payable as of September 30, 2000 (\$2.6 /\$3.4 billion)

METHODOLOGY

In accomplishing our audit objective, we reviewed the accrued expenses and accounts payable calculated and reported for USAID/Washington.

Specifically we:

- Obtained an understanding of USAID's procedures and processes for calculating accrued expenses and accounts payable.
- Assessed the risks associated with accrued expenditures and accounts payable calculated by the New Management System (NMS).
- Extracted the relevant financial data from NMS after USAID calculated and reported accrued expenditures and accounts payable at September 30, 2000. From this data, we performed analyses of USAID's calculations of accrued expenditures and accounts payable against:
 - 1) Obligations for grants;
 - 2) Obligations with no activity or minimal activity since the migration of financial data from the old Financial Accounting and Control System (FACS);
 - 3) Obligations with no activity from the date they were recorded;
 - 4) Obligations that were 365 days or more past their scheduled completion date;
 - 5) Obligations that were recorded before the actual constructive receipt of goods or services.
- Reviewed USAID's internal controls for reporting accounts payable on its fiscal year 2000 balance sheet.
- Obtained an understanding of USAID's internal controls with respect to compliance with USAID's policies and accounting standards and regulations, applicable to the accounts payable cycle.

A materiality threshold of 5 percent was used. Based on USAID's 1999 Net Cost of Operations, any amount over \$314 million was considered material and included in our review of the USAID 2000 financial statements.

Schedule of Questionable Accrued Expenditures Based NMS Obligation Balances:

Category	Documents	Unliquidated Balance	Accrued Amount	Amount Questioned (Adjustment)
Grant Obligations⁷	2038	\$2,414,368,808.34	\$1,844,784,040.14	\$1,844,784,040.14
Active Services	8	4,851,207.18	4,841,223.07	3,980,796.41
Refunds/Recoveries	47	1,520,598.98	1,520,598.98	1,520,598.98
No Recent Activity	315	25,000,898.62	24,790,992.38	24,790,992.38
Minimal Activity/FACS	151	12,704,630.24	12,257,232.24	12,257,232.24
Ended Services	207	21,712,603.96	21,446,243.78	21,446,243.78
Overaccrued	27	6,505,566.31	6,505,102.71	5,757,106.80
TA's over 12 months	47(OO) 198(AC)	250,710.72 512,065.62	250,710.72 512,065.62	250,710.72 512,065.62
Accrued Expenditure Equals Advance	20	2,811,193.85	2,811,193.85	2,811,193.85
Activity of In/Out Exp.	6	16,859.90	16,859.90	16,859.90
NMS Obligations Only	75	5,396,713.52	5,396,713.52	5,396,713.52
Total	3139	\$2,495,651,857.24	\$1,925,132,976.91	\$1,923,524,554.34

An explanation of each category that the OIG determined was possibly overstated is provided below:

- Grant obligations accounted for 96 percent of USAID's overstated accrued expenditures recorded in the New Management System at September 30, 2000. These obligations were established to fund grants. Advances established for grantees were accrued as expenditures and reported as accounts payable without considering the status of the actual advance liquidations.
- Active services include obligations for personal and non-personal service contracts that are ongoing; the OIG determined that the accrued expenditures for these contracts appear to be excessive.
- Refunds/Recoveries are those obligations in which activity seems to be complete and a refund or recovery was processed; the disbursement reversal increases the unliquidated balance that was fully accrued.
- No recent activity are those obligations for which there has been no activity for more than a year or the projects related to those obligations were complete.
- Minimal Activity/FACS are obligations that were migrated from USAID's Financial Accounting Control System in FY 1997 with minimal to no activity.

⁷ Grant obligations are established to fund projects through advances to grantees for which no accounts payable should be calculated.

⁸ Total questioned accrued expenditures that did not meet FASAB standards, rounded to \$1.9 billion.

- Ended services represents contracts where no salary payments have been made for an extended time indicating employment has ended.
- The over-accrued category represents those obligations with a disbursement history of smaller payments.
- TA's over 12 months represents travel authorizations over 365 days old that were separated into two categories: (1) authorizations with no disbursement or approved vouchers; this may indicate that the travel did not take place, and (2) authorizations that were completed - carrier and per diem disbursements were recorded indicating completion of travel. USAID recorded an accrued expenditure and established accounts payable for the entire unliquidated balance for both categories.
- Accrued expenditure equals advance are those obligations for which accrued expenditures were established that equaled the advanced amounts; USAID accrued the entire unliquidated balance.
- Recorded expenses in/out are transactions in which various entries for disbursements are recorded and reversed, but the full obligated amount remains unused. USAID accrued the entire unliquidated balance.

USAID MANAGEMENT COMMENTS



February 1, 2001

MEMORANDUM

TO: IG/A/FA, Alvin A. Brown

FROM: CFO, Michael T. Smokovich

SUBJECT: Audit of USAID's Accrued Expenditure, Accounts Payable,
And Related Internal Controls for Fiscal Year 2000

We have reviewed the draft report on your audit of the Agency's expense accrual estimates, accounts payable and related internal controls for FY 2000 and generally agree with your findings. As regards the \$2.3 billion in adjusting entries to the standard general ledger accounts, it should be noted that they were necessary to reverse the incorrect accrual calculations performed by the New Management System and to record the accrual estimates derived from the application of the new accrual methodology. This clarification would help users of the statements and your report to fully understand the nature of the adjusting entries.

We look forward to working closely with you on the audit of the accrual estimates for FY 2001. As you know, the Agency long range plan is to have program managers estimate accrued expenditures at the obligation document level and record these estimates into the core accounting system (Phoenix) on a quarterly

basis. However, for the first year of Phoenix operation we will not be able to implement this methodology. Therefore, we plan to use a trend analysis again in FY 2001 to estimate the accrued expenditures at year-end. Hopefully our respective staffs will be able to meet shortly after we finalize the FY 2000 Accountability Report to plan for the FY 2001 audit and to discuss the accrual methodology in particular.

I would like to thank you and your staff for the professional and cooperative manner in which the audit was conducted.

Cc: M/CFO, S. Owens
M/CFO, T. Cully
M/MPI, S. Malone-Gilmer
M/FM, D. Ostermeyer
M/FM/CAR, T. Vapniarek
M/FM/CAR, E. White
M/FM/A, J. Swan