
**Office of the Inspector General
Corporation for National Service**

**Audit of
The Corporation for National and Community Service
Statement of Financial Position
September 30, 1997**

**Report Number 99-01
September 14, 1998**

This report was issued to Corporation management on October 9, 1998. Under the laws and regulations governing audit follow up, the Corporation must make final management decisions on the report's findings and recommendations no later than April 7, 1999, and complete its corrective actions by October 9, 1999. Consequently, the reported findings do not necessarily represent the final resolution of the issues presented.

**Office of the Inspector General
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The Government Corporation Control Act (31 U.S.C. 9101 *et seq.*) requires the Inspector General to audit the financial statements of the Corporation for National and Community Service and to submit the resulting report to the Corporation's Chief Executive Officer, to the chairman of the committee on Government Reform and Oversight of the House of Representatives, and to the Chairman of the Committee on Governmental Affairs of the Senate. However, as OIG has previously reported, material weaknesses in management controls and other deficiencies precluded the required audits for fiscal years 1994, 1995 and 1996.

The enclosed audit report for fiscal year 1997 is limited in its scope because the Corporation determined that, due the nature and significance of weaknesses remaining uncorrected during fiscal year 1997, only its Statement of Financial Position as of September 30, 1997, could be submitted for audit.

OIG engaged KPMG Peat Marwick to audit the Statement of Financial Position. The audit was performed under generally accepted government auditing standards. OIG participated in the planning of the work and evaluated the nature, timing and extent of the procedures to be performed, monitored progress throughout the audit, and reviewed the auditors' report and the work papers supporting its conclusions;¹ we agree with the findings and recommendations presented.

The Auditors' report is qualified because the Corporation was unable to provide sufficient evidence to support (1) its methodology to estimate grant advances and grants payable or the reasonableness of amounts recorded for these line items, and (2) the reasonableness of amounts recorded for unexpended appropriations and cumulative results of operations. Further, KPMG reports material weaknesses in six financial management areas: the overall control environment that sets the tone for the organization, the National Service Trust, cash reconciliations, grants management, financial systems, and financial management. The report also discloses two areas of non-compliance with laws and regulations: the Corporation's failure to establish a system to assess its internal controls and to report in a manner consistent with the Federal Managers' Financial Integrity Act as required by the Government Corporation Control Act, as amended, and the Corporation's substantial non-compliance with Federal financial systems requirements.

We provided the Corporation with a draft of this report for review and comment. The Corporation's response is included as Appendix A.

¹ Because of the limited scope of the audit, OIG also engaged KPMG to perform an auditability assessment of the Corporation, OIG Report Number 98-23, May 15, 1998. This report provides additional information on the Corporation's progress towards correcting material weaknesses and other conditions that we reported in several reports issued since March 1996.

**Office of the Inspector General
Corporation for National Service**

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Corporation for National Service
Contract # 98-743-3002
Task #3

Independent Auditors' Report

Inspector General
Corporation for National Service:

We have audited the accompanying 1997 Statement of Financial Position of the Corporation for National Service (the Corporation). Our report was qualified because we were unable to satisfy ourselves as to the reasonableness of amounts recorded for grant advances, grants payable, and the component balances of net position at September 30, 1997.

In connection with our audit, we considered the Corporation's internal control over financial reporting and tested the Corporation's compliance with certain provisions of applicable laws and regulations that could have a direct and material effect on its 1997 Statement of Financial Position.

As a result of our consideration of internal control over financial reporting, we identified the following conditions:

- **General Control Environment** - The Corporation's general control environment is weak and is not conducive to ensuring that an effective system of internal control is maintained to safeguard assets, produce reliable financial reports, and comply with applicable laws and regulations. Further, management has not established procedures to assess the effectiveness of its internal control structure on an annual basis.
- **National Service Trust** - Procedures to obtain and reconcile membership roster information prepared by program sites to corresponding information on file at the Corporation are ineffective. This information is necessary to validate the accuracy and completeness of the data supporting the calculation of the service award liability.
- **Fund Balance with Treasury** - Reconciliations are not performed in an effective or timely manner.
- **Grants Management** - Adequate procedures for monitoring grantee financial activity and compliance with laws and regulations are not in place; expired grants are not closed out on a timely basis; and a reasonable method for determining outstanding amounts advanced to grantees or for estimating amounts payable to grantees for unreimbursed grant expenses incurred has not been established.
- **Financial Systems** - The Corporation's general ledger system is not adequate to support the financial information needs of the agency, including funds control, or to facilitate the preparation of annual financial statements.

- **Financial Management and Reporting** - The Corporation's organizational structure does not lend itself to effective supervisory or quality control over accounting and financial reporting activity to provide reasonable assurance that accounting records and files are complete, data entry errors are detected and corrected in a timely manner, and that reliable and timely financial reports are prepared.

We consider all conditions identified above to be material weaknesses.

Our tests of the Corporation's compliance with certain provisions of applicable laws and regulations disclosed that the Corporation has failed to assess and report on the effectiveness of its internal control in a manner consistent with the requirements of the Federal Managers' Financial Integrity Act of 1982, as required by the Government Corporation Control Act (31 U.S.C. 9101 *et seq.*). Further, the Corporation is in substantial noncompliance with OMB Circular A-127, Federal Financial Systems.

The results of our audit of the 1997 Statement of Financial Position, our consideration of Internal control over financial reporting, our tests of the Corporation's compliance with certain provisions of applicable laws and regulations, and our responsibilities, are discussed in the remainder of this report.

Opinion on Statement of Financial Position

We have audited the accompanying Statement of Financial Position of the Corporation for National Service as of September 30, 1997. This financial statement is the responsibility of the Corporation's management. Our responsibility is to express an opinion on this financial statement based on our audit.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance that the Statement of Financial Position is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Statement of Financial Position. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall Statement of Financial Position presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 1 to the Statement of Financial Position, management records outstanding amounts advanced to grantees and amounts due to grantees for unreimbursed grant expenses incurred based on estimated spending patterns of the grantees. Additionally, the remaining portion of grant awards authorized but not used is reported as obligated unexpended appropriations. Management could not provide us with sufficient evidence to support the methodology used, or its universal applicability, in computing grant advances or grants payable. Management also could not provide sufficient evidence to support the two primary components of net position – unexpended appropriations (including obligated versus unobligated portions) and cumulative results of operations. As a result, we were unable to satisfy ourselves as to the accuracy of amounts recorded for grant advances or grants payable as of September 30, 1997, or the reasonableness of the amounts reported as components of net position.

In our opinion, based on our audit, except for the effects on the Corporation's 1997 Statement of Financial Position of such adjustments, if any, as might have been determined to be necessary had the Corporation been able to provide sufficient evidence to support the amounts recorded for grant advances, grants payable

and the component balances of net position, the Statement of Financial Position referred to above, presents fairly, in all material respects, the financial position of the Corporation for National Service at September 30, 1997, in conformity with generally accepted accounting principles.

Report on Internal Control Over Financial Reporting

The management of the Corporation is responsible for establishing and maintaining internal control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies and procedures. The objectives of internal control are to provide management with reasonable, but not absolute, assurance that:

- transactions are executed in accordance with laws governing the use of budget authority and with other laws and regulations and government-wide policies identified by the OMB as applicable to the Corporation, that could have a direct and material effect on the Statement of Financial Position;
- assets are safeguarded against loss from unauthorized use or disposition; and
- transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with generally accepted accounting principles.

Because of inherent limitations in internal control, fraud may nevertheless occur and not be detected. Also, projection of an evaluation of internal control to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit, we considered the Corporation's internal control over financial reporting by obtaining an understanding of the agency's internal controls, determined whether these internal controls have been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the Statement of Financial Position, and not to provide assurance on Internal control over financial reporting. Accordingly, we do not express such an opinion.

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are material weaknesses. Reportable conditions are matters coming to our attention that represent significant deficiencies in the design or operation of internal control that could adversely affect the Corporation's ability to record, process, summarize, and report financial data consistent with the assertions of management in the Statement of Financial Position. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the Statement of Financial Position, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted certain matters, described below, involving internal control over financial reporting and their operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. We believe that all of the reportable conditions identified below are material weaknesses.

General Control Environment

The general control environment sets the tone of an organization and thereby influences the level of control consciousness and provides the discipline and structure of an organization. Control environment factors include commitment to competence, management philosophy and operating style, organizational structure, and assignment of authority and responsibility.

The Corporation is subject to the reporting requirements of the Government Corporation Control Act which requires management to provide an annual statement on its internal accounting and administrative controls in a manner consistent with the requirements of the Federal Managers' Financial Integrity Act of 1982 (Public Law 97-255). Although the Corporation has been in existence since 1994, the Corporation's first submission of such a statement was not made until December 1997 as part of its 1995 Annual Financial Report. Moreover, formal procedures to perform an annual assessment of the effectiveness of its internal control structure in meeting the objectives of reliable financial reporting and compliance with laws and regulations have not been established.

We concluded that the Corporation lacks an effective management control environment as evidenced by the volume of material weaknesses and other reportable conditions identified herein, in previous auditability surveys, and other reports issued by its Office of the Inspector General (OIG). Although the Corporation has made significant strides in addressing certain control environment issues, material internal control weaknesses remain which require management's attention. Without a strong general control environment, internal control weaknesses will continue to permeate the organization, increasing risks and inefficiencies and reducing the reliability of financial data.

In order to improve its general control environment, we recommend the Corporation (1) promote an overall strong commitment to competence by implementing an effective performance management system to reward and recognize those employees exhibiting strong competencies and to provide constructive feedback and counseling to those employees performing poorly; and (2) establish procedures to evaluate and report on its internal accounting and administrative controls and take appropriate corrective actions where necessary.

National Service Trust

The Corporation records a service award liability which represents education awards earned by Volunteers in Service to America, AmeriCorps, and National Civilian Community Corps program members for performing authorized community activities. The recorded liability for these service awards is based on actual awards earned by participants who have completed service and on estimated amounts for participants currently enrolled in the program.

The Corporation uses the Trust Fund database (SPAN) to capture the data required to estimate this liability. The integrity of this database and the data capturing processes, as well as the controls over these processes, are essential elements to ensure that the service award liability is based on accurate and complete information.

The membership roster confirmation process, a key control in ensuring the completeness and accuracy of the SPAN database, is currently ineffective as evidenced by significant reconciling differences between roster information prepared at the program sites compared to the corresponding information on file at the

Corporation used to calculate the service award liability. Our audit procedures included extensive detail testing, recomputations, and analytical procedures through which we were able to satisfy ourselves that the computed service award liability was materially correct. However, the weaknesses in the current membership roster confirmation process used to update the SPAN database increase the risk of errors and irregularities, including fraud, which could result in the calculation of a materially incorrect service award liability and in educational awards being paid to members who have not successfully completed the program's requirements.

In order to improve the reliability of member information used to compute the service award liability, we recommend (1) the membership roster confirmation process be improved by decreasing the frequency with which membership rosters are sent to program sites for verification, from a monthly to a quarterly basis, and requiring all sites to send back either the corrected roster or a certification that the rosters are correct and complete and that no changes are necessary; and (2) additional system edit checks be developed to detect data entry and data integrity errors. All errors identified should be promptly investigated and resolved.

Fund Balance with Treasury

Fund Balance with Treasury is the aggregate amount of funds in the Corporation's accounts with Treasury from which it is authorized to make expenditures and pay liabilities. The controls over capturing and reconciling the appropriate information for inclusion in the financial statements are essential to ensure that the related balances are complete and accurate.

The Corporation is not performing Fund Balance with Treasury reconciliation procedures in an effective or timely manner, as evidenced by a difference of more than \$5 million between the Department of Treasury's adjusted fund balance and the Corporation's adjusted fund balance as of September 30, 1997, which remained unresolved until August 1998.

Not reconciling and documenting the reconciliation of Fund Balance with Treasury could result in material misstatements in the financial statements and increases the risk that data in the general ledger is inaccurate or incomplete. In addition, the absence of such procedures increases the risk that a misappropriation of cash could remain undetected and hinders effective cash management. An effective monthly reconciliation would identify and resolve all differences between the Corporation's fund balance and the balance per Treasury.

We recommend that the Fund Balance with Treasury reconciliation be documented and submitted to a supervisor for review and approval within a reasonable period of time after each month end. We also suggest reconciliations be performed at the appropriation level, which may help the Corporation isolate variances to a few specific accounts.

Grants Management

The Corporation awards National and Community Service Act, as amended (42 U.S.C. 12501 *et seq.*) grants and Domestic Volunteer Service Act of 1973, as amended (42 U.S.C. 4950 *et seq.*) grants to state and local governments, institutions of higher education and other not-for-profit organizations.

The proper recognition of grant obligations, advances, and payables in the Statement of Financial Position is dependent on the completeness of grant files and the accurate and timely recording of grant award letters and

contracts, grant close-outs, and information contained in Financial Status Reports (FSR) and Request for Advance or Reimbursements (RAR) forms submitted to the Corporation. Grant award letters and grant contracts represent obligations and should be recorded in the general ledger upon their execution. Grant advances should be recorded in the general ledger when paid and documented by a RAR. Grants payable should be determined by the amount of grant expenses incurred by the grantees as reported to the Corporation on FSRs. Grant close-outs should be routinely processed within a reasonable period following the expiration of the grant period.

Our grants management audit procedures revealed ineffective controls over the timely recording of grant obligations, processing of grant close-outs, and in the proper maintenance of grant files. As a consequence, the Corporation was unable to provide adequate support for material amounts recorded on the 1997 Statement of Financial Position for grant advances, grants payable, or obligated unexpended appropriations due to authorized but unused grant awards. Our opinion on the Statement of Financial Position was qualified because we were unable to satisfy ourselves as to the reasonableness of these recorded amounts.

The Corporation is responsible for ensuring that grantees comply with applicable laws and regulations related to the administration of the respective grant awards. However, our audit procedures revealed that a comprehensive, risk-based program for selecting grantees for financial and programmatic site visits is not in place. Further, an effective procedure for obtaining grantees' Single Audit reports, where required, and resolving noted instances of noncompliance has not been established. Such a grantee monitoring system would help provide the Corporation with assurance that significant grant advance balances maintained by certain grantees were not in excess of prescribed cash management requirements. We found no evidence the Corporation had taken action to investigate the nature of these advances.

We recommend the Corporation take the following actions to improve its grants management process:

1. conduct periodic employee training on the proper procedures for grants processing and file maintenance;
2. develop a timeline to review all active grant files and use the recently developed checklist to ensure complete documentation is on file;
3. develop a spreadsheet tracking system to monitor the status of open grants and accurately estimate outstanding advances due from and amounts payable to grantees;
4. monitor compliance with the Single Audit Act requirements and establish a procedure to obtain Single Audit reports, if required, and resolve identified instances of noncompliance;
5. evaluate methods to expedite the processing of FSRs and develop and implement procedures to record grant expenses in a more timely manner; and
6. close out expired grants on a timely basis.

Financial Systems

Limitations of the financial systems currently in use by the Corporation have contributed significantly to the Corporation's inability to compile reliable and meaningful financial reports for management information and

annual financial reporting purposes on a timely basis. The current financial management system does not provide the Corporation with an effective means for control of financial activity at the detail fund level, thus requiring the Corporation to manually accumulate and summarize this level of information for financial reporting purposes. Numerous detail subsidiary ledgers are maintained separate from the general ledger system by accounting personnel and staff members in other offices to track information not readily available from the current financial management system. Reconciliation of these manual and personal computer based records to the general ledger is time consuming and subject to human error. Manual intervention in preparing these detail reports, which are often not subject to review by a second person, and their use in compiling financial reports, also not subject to review, increases the risk of reporting materially incorrect financial statement amounts and decreases the overall reliability of such reports.

We recommend the Corporation comprehensively evaluate its management information needs and update its information systems and processes for improved system integration, enhanced data integrity checks, funds control, and expanded reporting functions. This project should receive the highest priority attention of management with the goal for completion no later than the end of fiscal year 1999.

Financial Management and Reporting

Key elements in ensuring an effective financial management system is maintained include:

- identification of key financial processes and critical success factors in achieving established goals and objectives;
- clearly communicated assignment of responsibilities, commensurate with capabilities, related timelines, and expected results;
- training of management and employees in relevant financial reporting concepts;
- availability and appropriate use of reference materials and written procedure manuals;
- supervisory review of subordinates work for accuracy and overall reasonableness;
- management review of financial statements, disclosures, and supporting schedules; and
- effective oversight of accounting and financial reporting services provided by outside contractors.

In addition, the Corporation's financial managers should be knowledgeable of current accounting and reporting requirements, be familiar with the financial information system capabilities, have timely access to financial reports such as budget to actual expenditure comparisons, and be committed to quality in all aspects of financial management and reporting.

Currently, the organizational structure of the Corporation as it relates to financial management is in disarray due to significant turnover, staffing shortages, and inexperienced personnel. Although the Corporation is generally aware of its organizational problems, and has hired certain additional personnel to begin to address its staffing issues, a concerted effort to identify key financial processes and critical success factors and assign competent financial managers to those areas they are best qualified to handle has not been made. As a

consequence, quality control in all areas has suffered as evidenced by the prevalence of file maintenance and data entry errors noted throughout our audit. These errors were not detected and corrected by employees or their supervisors until discovered during the audit or as a consequence of the manual preparation of year-end financial statements.

Further, current management has no clearly defined written policies and procedures for the timely and accurate preparation of the financial statements. Although the Corporation has contracted with an outside accounting firm to provide operational and system support for its financial reporting process, oversight of the contractors' performance is limited and responsibility for ensuring the financial statements and related disclosures, supporting schedules, and account analyses are complete and accurate has not been clearly assigned to, or assumed by, anyone at the Corporation.

These financial management weaknesses resulted in potential material misstatements in the Statement of Financial Position, which required us to qualify our independent auditors' report. Additionally, material adjustments, approximating \$2.6 million for Fund Balance with Treasury, \$30 million for Grant Advances, and \$43 million for the Corporation's Service Award Liability, were necessary to correct omissions and mathematical errors made in preparing the Corporation's 1997 Statement of Financial Position.

In order to improve its financial management and reporting processes, we recommend the Corporation:

1. evaluate its organizational structure and staffing requirements to ensure that assignment of responsibility is appropriate considering the experience and capabilities of those assigned, and that incompatible duties are appropriately segregated;
2. develop, document, and implement a methodology for ensuring the Corporation's financial statements, including the related financial statement disclosures, are prepared timely and accurately, in accordance with the provisions of the Government Corporation Control Act;
3. require the completion of a financial disclosure checklist and the documentation of senior management review and approval of the financial statements and related support prior to issuance;
4. ensure that personnel responsible for preparation and review of the financial statements are adequately trained on current accounting and reporting requirements; and
5. assign oversight of contractor performance to a responsible Corporation financial manager.

These conditions were considered in determining the nature, timing, and extent of audit procedures to be performed in our audit of the Corporation's 1997 Statement of Financial Position.

The weaknesses identified during our audit of the Corporation's 1997 Statement of Financial Position were also identified in previous auditability surveys and other reports issued by its OIG including OIG Report 98-23, *Auditability Assessment of the Corporation for National Service at September 30, 1997*, issued July 8, 1998.

These weaknesses continue to exist as of the date of this report. We did not reassess the status of other weaknesses identified in the *Auditability Assessment* during this audit of the Corporation's 1997 Statement of Financial Position due to the nature and extent of the audit procedures applied.

An audit of financial statements conducted in accordance with generally accepted auditing standards and *Government Auditing Standards* is not designed to detect whether the Corporation's financial management systems are Year 2000 compliant. Further, we have no responsibility with regard to the Corporation's efforts to make its systems, or any other systems, such as those of the Corporation's vendors, service providers, or any other third parties Year 2000 compliant, or provide assurance on whether the Corporation has addressed or will be able to address all of the affected systems on a timely basis. These are responsibilities of the Corporation's management.

Report on Compliance with Laws and Regulations

The management of the Corporation is responsible for complying with laws and regulations applicable to the entity. As part of obtaining reasonable assurance about whether the Corporation's Statement of Financial Position was free of material misstatement, we performed tests of the Corporation's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations. However, providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit. Accordingly, we do not express such an opinion.

The results of our tests of compliance with the laws and regulations described in the preceding paragraph, disclosed instances of noncompliance with the following laws and regulations that are required to be reported under *Government Auditing Standards*.

- The Corporation is subject to the reporting requirements of the Government Corporation Control Act, which requires management to provide an annual statement on its internal accounting and administrative controls in a manner consistent with the requirements of the Federal Managers' Financial Integrity Act. The Corporation does not have a system in place to assess the effectiveness of its system of internal control in achieving the objectives of reliable financial reporting and compliance with laws and regulations, and has not submitted its reports on a timely basis.
- The Corporation is in substantial noncompliance with OMB Circular A-127, Federal Financial Systems, which requires Federal entities to establish and maintain a single, integrated financial management system to process and record financial events effectively and efficiently, and to provide complete, timely, reliable and consistent information for decision makers and the public.

The results of our tests of compliance with the laws and regulations, as described above, disclosed no other instances of noncompliance that are required to be reported herein under *Government Auditing Standards*.

We also noted other matters involving internal control over financial reporting and compliance with laws and regulations that we do not consider to be reportable conditions or material noncompliance, that we will report to the management of the Corporation in a separate letter (OIG Report 99-02).

We provided a draft of this report to the Corporation. The Corporation's response to our findings and recommendations is included as Appendix A.

As required by the Government Corporation Control Act, this report is intended for the information of the United States Congress, the President, the Director of the Office of Management and Budget, the Comptroller General of the United States, and the Corporation for National Service and its Inspector General. However, this report is a matter of public record and its distribution is not limited.

KPMG Peat Marwick LLP

September 14, 1998

CORPORATION FOR NATIONAL SERVICE

Statement of Financial Position

September 30, 1997

(Dollars in Thousands)

Assets

Fund Balance with Treasury (note 2)	\$ 707,114
Trust Investments and Interest Receivable, net of amortized premiums and discounts of \$4,543 (note 3)	235,927
Accounts Receivable, net of allowance for doubtful accounts of \$70 (note 4)	2,684
Grant Advances (note 1)	21,582
Property and Equipment, net of accumulated depreciation of \$585 (note 5)	993
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Total Assets	\$ 968,300
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Liabilities

Accounts Payable and Accrued Liabilities (note 1)	\$ 15,937
Service Award Liability (note 6)	192,253
Commission Post-service Benefits Liability (note 7)	1,983
Capital Lease Liability (note 8)	195
Grants Payable (note 1)	73,555
Accrued Annual Leave	2,568
Accrued FECA Liability	3,880
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Total Liabilities	290,371
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Net Position Balances (note 10):	
Unexpended Appropriations:	
Unobligated	163,315
Obligated	329,004
Cumulative Results of Operations	185,610
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Total Net Position	677,929
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Commitments (notes 2 and 9)	
Total Liabilities and Net Position	\$ 968,300
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See accompanying notes to the statement of financial position.

CORPORATION FOR NATIONAL SERVICE

Notes to Statement of Financial Position
(Dollars in Thousands)

September 30, 1997

(1) Summary of Significant Accounting Policies

(a) *Basis of Presentation*

This financial statement has been prepared to report the financial position of the Corporation for National Service (the Corporation), as required by the National and Community Service Trust Act of 1993. The Corporation is not subject to income tax.

(b) *Reporting Entity*

The Corporation for National Service, a government corporation, was created by the National and Community Service Trust Act of 1993 (Public Law 103-82). The Corporation provides grants and other incentives to states, local municipalities and not-for-profit organizations to expand national and community service volunteer activities. The Corporation operates the National Service Trust (the Trust), a fund within the Corporation, to fund education and similar awards made under national and community service programs, including Volunteers in Service to America (VISTA), AmeriCorps, and National Civilian Community Corps (NCCC).

(c) *Basis of Accounting*

The Corporation's financial statements are prepared under the accrual basis of accounting in conformity with generally accepted accounting principles as applicable to government corporations. Under the accrual method, accounts receivable are recognized when earned and liabilities are recognized when a related good or service is received or expense is incurred, without regard to receipt or payment of cash. The Corporation uses budgetary accounting to facilitate compliance with legal constraints and controls over the use of Federal funds.

(d) *Fund Balance with Treasury*

The Corporation does not maintain cash in commercial bank accounts. Cash receipts and disbursements are processed by the U.S. Department of Treasury (Treasury). The fund balances with Treasury represent annual, multi-year, and no-year funds which are maintained in appropriated and trust funds that are available to pay current and future commitments.

(e) *Trust Investments and Interest Receivable*

By law, the Corporation invests funds which have been transferred to the Trust only in interest-bearing Treasury obligations of the United States. These Treasury obligations are referred to as market-based specials, which are similar to government securities sold on the open market, and consist of treasury notes, bills, bonds and one-day certificates.

CORPORATION FOR NATIONAL SERVICE

Notes to Statement of Financial Position (Dollars in Thousands)

September 30, 1997

The Corporation has classified these investments as held-to-maturity at the time of purchase and periodically re-evaluates such classification. Securities are classified as held-to-maturity when the Corporation has the positive intent and ability to hold securities to maturity. Held-to-maturity securities are stated at cost with corresponding premiums or discounts amortized over the life of the investment to interest income using the effective interest method.

Interest receivable represents amounts earned but not received on investments held at year-end. Accrued interest, which is the amount of interest earned on an investment between the date of the last interest payment and the date the security was purchased by the Corporation, is recorded as prepaid interest and included in the interest receivable balance.

(f) *Accounts Receivable*

Accounts receivable represent amounts due to the Corporation primarily from Federal and non-Federal reimbursable agreements, and repayment of advances due from employees. Amounts are shown net of an allowance for doubtful accounts.

(g) *Grant Advances*

The Corporation advances funds primarily in response to grantee drawdown requests to facilitate their authorized national and community service, and domestic volunteer service activities. The cash payments to grantees are accounted for as advances. At the end of the fiscal year the total amount advanced to grantees is compared with the Corporation-funded amount expensed by the grantees. For those grantees with advances exceeding expenses, including accrued expenses, the aggregate difference is reported as the advance account balance.

(h) *Property and Equipment*

The Corporation capitalizes property and equipment at historical cost for acquisitions of \$10,000 and over, with an estimated useful life of 2 or more years. The assets reported, comprised of telephone equipment, computer systems equipment, copiers, computer software and systems, and furniture are depreciated (or amortized) on a straight line basis, using the half year convention, over estimated useful lives, which range from 2 to 10 years.

(i) *Accounts Payable and Accrued Liabilities*

Accounts payable represents amounts due to both Federal and non-Federal entities for goods and services received by the Corporation at the end of the fiscal year. It also represents advance funds received under cost sharing agreements for which expenses were not incurred by the end of the fiscal year. Accrued liabilities represent accruals for payroll and benefits, and the liability for volunteer stipends payable.

CORPORATION FOR NATIONAL SERVICE

Notes to Statement of Financial Position
(Dollars in Thousands)

September 30, 1997

(j) Grants Payable

Grants are made to non-profit organizations, education institutions, and other external organizations. Grants become obligations, but not liabilities, when they are awarded. Grantees may choose to operate on a reimbursable basis, whereby they incur authorized expenses and then request reimbursements. At the end of each fiscal year, the Corporation reports the total amount of unreimbursed authorized grantee expenses as grants payable, based on estimated spending patterns of the grantees.

(k) Service Award Liability

The service award liability represents unpaid earned, and expected to be earned, education awards and eligible interest forbearance costs. This liability, more fully discussed in note 6, is funded by the National Service Trust, established by the National and Community Service Trust Act of 1993.

(l) Commission Post-Service Benefits Liability

The Commission post-service benefits liability represents unpaid earned education awards incurred by the Commission on National and Community Service (the Commission), which has been managed by the Corporation since 1994. This liability, more fully discussed in note 7, is funded by the Commission.

(m) Net Position

The Corporation receives annual and multi-year appropriations to operate its grant program. The Corporation also receives no-year appropriated funds to provide education awards to members. Funds received for education awards remain available indefinitely. Net position includes unexpended appropriations and cumulative results of operations.

(n) Retirement Benefits

The Corporation's employees are eligible to participate in two retirement plans. Employees hired before January 1, 1984 are covered by the Civil Service Retirement System (CSRS) unless they elected to join the Federal Employees Retirement System (FERS) and Social Security during the election period. Employees hired after December 31, 1983 are covered by FERS and Social Security. For employees covered by the CSRS, the Corporation contributes approximately 7% of their gross pay to the Plan. For those employees covered by FERS and Social Security, the Corporation's contributions to the Plan approximate 13% of the gross pay of regular employees. Employees covered by FERS are allowed to participate in the Federal Thrift Savings Plan (TSP) and the Corporation contributes an automatic 1% of the employee's basic pay and matches any employee contribution up to an additional 4% of pay. Employees under the

CORPORATION FOR NATIONAL SERVICE

Notes to Statement of Financial Position (Dollars in Thousands)

September 30, 1997

CSRS Plan may participate in the TSP but will not receive the Corporation's automatic and matching contributions.

(o) Contingencies

Management has determined that there were no material contingent liabilities outstanding as of September 30, 1997 that would have a material effect on the statement of financial position.

(p) Use of Estimates

The preparation of the statement of financial position in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the statement of financial position date. Actual results could differ from these estimates.

(2) Fund Balance with Treasury

This amount represents the cash balances with Treasury, as reflected in the Corporation's records. The composition of the Fund Balance with Treasury by type and classification as of September 30, 1997, is presented below:

	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Appropriated fund	\$ 684,301	—	684,301
Trust fund	—	22,381	22,381
Gift fund	10	422	432
Total	<u>\$ 684,311</u>	<u>22,803</u>	<u>707,114</u>

Of the unrestricted appropriated funds, approximately \$444 and \$34, respectively, are obligated for grants awarded by the Corporation and Corporation operating expenses as of September 30, 1997.

(3) Trust Investments and Interest Receivable

The composition of investments and interest receivable is as follows at September 30, 1997:

Investments	\$ 232,351
Interest receivable	3,576
Total	<u>\$ 235,927</u>

CORPORATION FOR NATIONAL SERVICE

Notes to Statement of Financial Position
(Dollars in Thousands)

September 30, 1997

The amortized cost and fair value of investments securities is as follows at September 30, 1997:

Held-to-maturity securities	Amortized cost	Unrealized gains	Unrealized losses	Fair value
Notes	\$ 224,876	2,298	365	226,809
Bills	7,475	100	—	7,575
Total	<u>\$ 232,351</u>	<u>2,398</u>	<u>365</u>	<u>234,384</u>

The notes held at year-end had an interest rate range of 4.75% to 14.25% and a maturity range from 120 days to approximately 5 years. The bills held at year-end had an interest range of 4.7% to 5.1% and were due to mature within 90 days.

Investments held at September 30, 1997 mature as follows:

Held-to-maturity securities	Amortized Cost	Fair Value
Due in 1 year or less	\$ 47,785	48,174
Due after 1 year up to 5 years	184,566	186,210
Total	<u>\$ 232,351</u>	<u>234,384</u>

(4) Accounts Receivable

Accounts receivable of the Corporation at September 30, 1997, are as follows:

Accounts and reimbursable receivable	\$ 2,754
Less – allowance for loss on receivables	<u>70</u>
Accounts receivable, net	<u>\$ 2,684</u>

CORPORATION FOR NATIONAL SERVICE

Notes to Statement of Financial Position
(Dollars in Thousands)

September 30, 1997

(5) Property and Equipment

Property and equipment is recorded at cost and depreciated over its estimated useful life. Shown below is the composition of Property and Equipment account as of September 30, 1997:

Equipment type	Depreciation method	Service life	Acquisition cost	Accumulated depreciation	Net book value
Telephone	Straight line	6 Years	\$ 348	187	161
Computer systems	Straight line	3 Years	303	158	145
Copiers	Straight line	5 Years	182	35	147
Copiers	Straight line	4 Years	11	11	—
Copiers	Straight line	3 Years	15	10	5
Software	Straight line	2 Years	12	3	9
Systems furniture	Straight line	10 Years	657	173	484
Systems furniture	Straight line	3 Years	50	8	42
Total property and equipment			\$ 1,578	585	993

(6) Service Award Liability - National Service Trust

Individuals who successfully complete terms of service in AmeriCorps programs earn education awards, which can be used to make payments on qualified student loans or cost of attendance at qualified educational institutions. The awards, which can be used for a period of up to seven years, are paid from the National Service Trust. The Trust also pays forbearance interest on qualified student loans during the period members perform community service.

The Corporation records a liability for service awards and forbearance interest costs based on actual awards earned by participants who have completed service and participants currently enrolled in the program that are expected to earn an award based on the Corporation's historical experience.

The service award liability was comprised of the following as of September 30, 1997:

Education awards	\$ 251,945
Interest forbearance	1,557
Total service award liability	253,502
Less – cumulative awards paid	(61,249)
Net service award liability	\$ 192,253

CORPORATION FOR NATIONAL SERVICE

Notes to Statement of Financial Position
(Dollars in Thousands)

September 30, 1997

(7) Post-Service Benefits Liability – Commission on National and Community Service

The former Commission on National and Community Service (Commission) was merged into the Corporation for National Service during fiscal year 1994. With this merger the Corporation assumed any liabilities of the Commission, including those incurred for post-service benefits.

Post-service benefits liabilities from Commission operations differ from those originating within the Corporation in three respects: (1) the trustee is the grantee rather than an agency of the Federal government; (2) the portion of these awards which is funded by the Federal government is specified in each grant agreement, with any remaining amounts funded by the grantee; and (3) the post-service period during which an award is available for use is established by each program grantee, rather than set at seven years for all awardees.

The post-service benefits liability associated with the Commission was estimated based on a review of all grants for which post-service benefits were authorized. The amounts shown below represent the aggregate maximum liability under the assumption that all funds obligated for post-service benefits are still payable to grantees for this purpose, except for the portions that have been drawn down or for which the service benefit expired on or before September 30, 1997.

The Commission post-service benefits liability was comprised of the following as of September 30, 1997:

Education awards	\$	8,086
Less - amounts drawn down		4,450
		<hr/>
Undisbursed awards		3,636
		<hr/>
Less - service benefit expirations		1,653
		<hr/>
Net post-service benefits liability	\$	<u>1,983</u>

CORPORATION FOR NATIONAL SERVICE

Notes to Statement of Financial Position (Dollars in Thousands)

September 30, 1997

(8) Capital Lease Liability

The Corporation has entered into lease agreements for copy machines and systems work-station furniture. These leases vary from 3 to 10 year terms and are deemed to be capital leases. The cost of the copiers and systems workstation furniture has been recorded as property and equipment and the liability for these leases is as shown below:

Future payments due:			
Fiscal year 1998	\$		72
Fiscal year 1999			68
Fiscal year 2000			61
Fiscal year 2001			38
			239
Total future lease payments			239
Less – imputed interest			44
			44
Total capital lease liability	\$		195

(9) Other Leases

The Corporation leases office space through the General Services Administration (GSA). GSA's lease agreement with the building owner has a 10 year term. However, GSA is authorized to reassign the Corporation to other space if and when GSA determines that reassignment would promote and enforce efficient space utilization. The Corporation is not legally a party to any building lease agreements; therefore, the Corporation does not disclose future minimum lease payments on buildings. Additionally, the Corporation leases motor vehicles on an annual basis through GSA under an Interagency Fleet Management Service agreement for the National Civilian Community Corps.

(10) Net Position

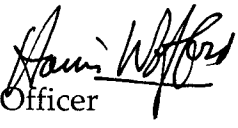
The reported net position consists of unexpended appropriations and cumulative results of operations, which represents the differences between net revenue and expenses since the Corporation's inception. Component funds are separately maintained for the Gift Fund, Trust Fund, and Appropriated Fund. Following is a summary of net position by component as of September 30, 1997:

		Gift Fund	Trust Fund	Appropriated Fund	Total
Unexpended appropriations	\$	—	—	492,319	492,319
Cumulative results of operations		461	118,947	66,202	185,610
Total	\$	461	118,947	558,521	677,929

APPENDIX A – CORPORATION RESPONSE

MEMORANDUM

TO: Luise Jordan
Inspector General

FROM: Harris Wofford, 
Chief Executive Officer

DATE: October 7, 1998

SUBJECT: Response to Draft Report on the Audit of the FY 1997 Corporation
Balance Sheet

We are pleased to have an opportunity to respond to the draft report concerning the audit of the Corporation's 1997 Statement of Financial Position. This qualified opinion on the Corporation's balance sheet is an important step in our overall auditability effort.

The Corporation's responsibility to prepare and present auditable annual financial statements in accordance with generally acceptable accounting principles arises from our status as a government corporation. Established in FY 1994, the Corporation was charged with initiating a range of new National Service programs while also merging into the organization two existing government entities, ACTION and the Commission on National Service, neither of which had previously had a similar reporting requirement. We have been working to resolve the many issues that impeded our ability to produce auditable statements. Part of our plan was to achieve auditability in phases, first seeking an opinion on our balance sheet as a step to a successful audit of our full set of statements. Although the opinion was qualified, the current audit report validates our continued progress and it helps us refine our plans.

The Corporation's first attempt at an independent audit of its financial statements was not successful. In March, 1996 the Inspector General released the first auditability review that listed 99 auditability weaknesses, of which fully 33 were material. All of these served as impediments to an independent audit. As subsequent auditability reviews demonstrated in July 1997 and July 1998, we have worked hard to address our weaknesses, establish necessary controls, and improve our procedures.



Memorandum to Luise Jordan
October 7, 1998
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In March of this year, we put in place a specific auditability plan to address the weaknesses noted in the 1997 IG auditability review. We have been reporting to Congress every 60 days on our progress with that plan. As part of this audit of the 1997 balance sheet, the auditors conducted a comprehensive review of the Corporation's status on previous auditability items. The findings of this most recent review and the weaknesses outlined in this audit report will be merged with the Corporation's current auditability plan so that we have one comprehensive remediation plan that will guide our efforts to achieve and subsequently sustain an unqualified opinion on our annual statements. We are fully committed to this goal.

We appreciate and understand the findings in the audit report. The specific recommendations presented are useful and will find a place in our remediation effort. Similarly we acknowledge the two areas of non-compliance with laws and regulations and are already working to address them. Our current effort to replace our legacy financial system has a clear requirement of achieving compliance with OMB Circular A-127. We agree with the importance of establishing an effective system of self-assessment and reporting on internal controls. New staff have been hired to address this issue.

As I write this reply, we are closing out FY 1998. Personnel are busy with the preparatory work necessary to produce our financial statements by December. The early stages of the FY 1998 audit have already commenced. Action to improve controls and reporting continues apace. Teams are working to replace the financial system and to meet Year 2000 requirements. Others are preparing to introduce new technology to the National Trust operations, including digital imaging capability for document control and automated work flow software to improve efficiency. A task force is at work defining ways to improve and potentially reengineer our grants process, an activity which would respond to many of the audit concerns. An unqualified opinion on our annual financial statements should be a natural by-product of a strong and focused management environment. We are working with great purpose to create that environment. This report marks a further advance along that road.

Thank you for your dedicated work and diligent efforts to help the Corporation improve its management environment.