MEMORANDUM

DATE: December 21, 2017

TO: USAID Chief Financial Officer, Reginald W. Mitchell

FROM: Deputy Assistant Inspector General for Audit, Alvin A. Brown /s/

SUBJECT: Management Letter: OIG Identified Control Deficiencies During the Audit of USAID's Financial Statements for Fiscal Years 2017 and 2016

The Office of Inspector General (OIG) performed an audit of the U.S. Agency for International Development's (USAID) financial statements for fiscal years 2017 and 2016, including consolidated balance sheets as of September 30, 2017, and 2016, and the consolidated statements of net cost, consolidated changes in net position, and combined statements of budgetary resources for the years then ended. We have issued an unmodified opinion thereon in a report dated November 15, 2017. In planning and performing our audit, we considered USAID's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on internal control. We have not considered internal control since the date of our November 15, 2017 report. During our audit, we noted certain matters involving USAID's internal controls that we present in the attachment to this memo for your consideration. The comments and suggestions, all of which have been discussed with the appropriate members of your management team, are intended to improve USAID's internal controls and result in other operating efficiencies.

We appreciate the cooperation and courtesies your staff extended to us during the audit. If you have questions concerning this memo or would like to discuss it, please contact the director of financial audits, Rohit Chowbay, at 202-712-1317.

Attachment

INTERNAL CONTROL DEFICIENCIES IN USAID HEADQUARTERS

Scope of Internal Control Assessment

The scope of USAID's internal control assessment was insufficient. According to Office of Management and Budget guidance (A-123 A),[1] when multiple locations exist, samples should reflect an appropriate cross-section of all locations. However, the internal control assessment team's scope included headquarters and only 2 of 55 missions, both of which were tested remotely. Of the two missions tested, one was tested for only one quarter of fiscal year (FY) 2017. Further, team members tested 6 of 16 key business processes within headquarters and the two missions. Therefore, the scope of USAID's internal control assessment was not broad enough to arrive at a conclusion on internal controls.

According to USAID management, the scope of the testing was limited due to budgetary constraints. However, by limiting the scope management may be providing assurance about internal controls within the organization that is not sufficiently supported. Therefore, we suggest that management conduct appropriate testing that would provide sufficient evidence to support its assertion about the effectiveness of internal control over financial reporting as a subset of the overall Federal Managers' Financial Integrity Act (FMFIA) report.

Employee Separation

Employee separation procedures were not consistently enforced. The Office of Human Capital and Talent Management did not have an exit clearance form for 4 of the 52 separated employees reviewed. The exit clearance form triggers several actions: revocation of the employee's physical and electronic access, return of USAID property (such as badges, keys, and keycards), and collection of outstanding liabilities. Employees who do not submit the form could retain access to computer systems and property, compromising USAID's security and the integrity of its information.

USAID policy states that the administrative management specialists in each bureau and independent office must provide separating employees with an exit clearance form (AID 451-1) 10 business days before departure, along with instructions on completing it.[2] One of the last steps to complete the form is certification by the security office; after that, the separating employee takes the form to the human capital office for filing and transmission for payroll processing.

To comply with its policy, we suggest that USAID enforce the requirement for separating employees to submit their completed forms to the administrative management specialists, who are then responsible for submitting them to the Office of Human Capital and Talent Management.

Review of Service Organization Controls

USAID did not consistently evaluate reports on internal controls submitted by organizations that provide it with certain services (service organizations) to see if the organizations listed any

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[1] OMB Circular A-123, Appendix A (A-123 A).

[2] USAID's Automated Directives System (ADS), chapter 451, "Separations and Exit Clearance."

deficiencies that might affect USAID's financial statements. These organizations—such as the Department of Agriculture, the Department of Health and Human Services, the Department of Labor, and Midland Loan Services—process certain financial transactions for the Agency. The organizations are required to submit to USAID a report containing (1) their assertion that their controls are operating effectively so that the information they provide the Agency is reliable, and (2) the opinion of an outside auditor on the reliability of the organizations' internal controls.[3]

Although USAID had some controls in place to compensate for potential weaknesses in service organization activities, USAID did not analyze whether its complementary controls were adequate. Therefore, we suggest that USAID's chief financial officer design and implement controls to evaluate the assurances provided in the reports submitted by service organizations and demonstrate that USAID has implemented adequate complementary controls.

Advances

USAID's process for accounting for advances was not adequate to ensure that its financial records accurately reflect the status of cash advances to partners, and that funds due to the Agency are promptly recovered. Specifically, we found that the agency was not properly liquidating outstanding advances that were disbursed under contracts, grants, or cooperative agreements. Although USAID headquarters and missions periodically review all advances, the Agency has advances that have been outstanding more than 150 days totaling approximately $36 million as of September 30, 2017. We recognize that $12 million are intragovernmental (intragovernmental payment and collection, or IPAC),[4] and USAID management considers these low risk.

Missions and headquarters are required to ensure that outstanding advances are periodically reviewed so that funds advanced do not exceed immediate disbursement needs.[5] However, Agency policy does not stipulate when an advance should be reported to the contracting or agreement officer to make a debt determination.

To meet federal internal control standards,[6] we suggest that USAID's chief financial officer (1) research all advances outstanding for more than 150 days to determine if they should be recovered, and (2) once a determination has been made and a bill of collection issued, reclassify the advance to an accounts receivable.

Accrual Documentation

Accrual documentation did not always match the reported balance. The contracting officer's representatives did not always provide accrual documentation to validate the modified accrual amounts recorded in the accrual reporting system (ARS) and USAID general ledger. ARS generates an estimated accrued amount for a contract/award based upon the obligations,

[3] Statements on Standards for Attestation Engagements No. 18 (SSAE 18), "Concepts Common to All Attestation Engagements."

[4] IPAC is a way for Federal Program Agencies (FPAs) to transfer funds from one agency to another with standardized descriptive data.

[5] ADS chapter 636, section 636.3, "Program Funded Advances."

[6] GAO Standards for Internal Control in the Federal Government (GAO-14-704G).

vouchers, and period of performance. ARS produces an accrual estimate from an algorithm based on certain assumptions.

Using in-depth knowledge of the contract/award, the contracting officer's representative (COR) modifies the estimated accrual amount for any unpaid and anticipated vouchers. This modified accrual is documented and supported on the COR accrual worksheet. From a judgmentally selected sample of 53 modified accruals valued at approximately $804 million, the COR could not provide documentation to support the modified accrual amount recorded in ARS and the general ledger for 4 which were valued at approximately $12 million. Projecting the unsupported accruals in our sample to all modified accruals in ARS for the period (worth $1.2 billion), we estimated that the balance was misstated by $22 million.

Therefore, we proposed that USAID's chief financial officer (CFO) adjust the accounts payable balance by $22 million. However, in accordance with OMB Bulletin 17-03, the CFO chose to report the error on the management representation letter.

Unliquidated Obligations

USAID did not consistently review unliquidated obligations (ULOs) to determine if they should be deobligated to be made available for other purchases. At the end of FY 2013, we identified approximately $128 million in ULOs that did not have disbursements for 3 or more years. We recommended that USAID review them to determine if they should be deobligated so that the funds could be put to better use. In FY 2012, USAID established a deobligation team dedicated to reviewing and closing out procurement obligations without activity for more than 3 years and developed an automated deobligation web tool to deobligate nonprocurement obligations.

During FY 2017, the team deobligated approximately $82 million of outstanding obligations that were made available in the Phoenix accounting system for reprogramming. Using the automated deobligation web tool, USAID deobligated an additional $12 million with no disbursements for more than 3 years. Although USAID has made progress monitoring its ULOs, as of September 30, 2017, we identified $12 million in unliquidated obligations with no disbursements for more than 3 years that might be available for deobligation.

We suggest that USAID management conduct annual reviews of ULOs without disbursements for 3 or more years and deobligate those that are no longer needed.

Local Currency Trust Fund (Modified Repeat Finding)

USAID's controls over audits and financial reviews of local currency trust funds (LCTF) were ineffective. We tested 10 trust funds at 10 missions and determined that audits or financial reviews of nine trust funds were not completed in accordance with policy:[7]

- One fund was not audited or reviewed.
- Eight audits or reviews were not conducted within the required period (biannually).

[7] ADS chapter 627, "Local Currency Trust Fund Management."

The missions were not conducting their audits or financial reviews once every 2 years but were auditing multiple years at a time. Mission controllers did not provide reasons for not conducting the audits and financial reviews biannually.

Without the required audits and reviews, mission controllers cannot verify whether trust funds were expended for the purposes designated in the trust fund agreements.

Additionally, the LCTF financial reviews being conducted by missions were not centrally monitored, as ADS 627 requires mission controllers to send completed financial reviews to mission directors, not to headquarters. Without this monitoring, USAID headquarters has no way of knowing whether the financial reviews conducted by missions are being done correctly.

Therefore, we suggest that the USAID chief financial officer:

1. Verify that mission controllers comply with ADS 627 in conducting financial audits and reviews.
2. Update policies and procedures to require the USAID Audit Performance and Compliance Division to track the financial reviews missions conduct when disbursements are below the $300,000 threshold.

USAID Purchase Cardholders

USAID's controls to ensure that purchase cardholders follow the policy directives and required procedures were not always effective. Specifically, we found 11 of 48 purchase cardholders circumventing the policies and requirements by not obtaining authorizations before making purchases. Cardholders were not adequately supervised to ensure compliance with established policies and procedures. As a result, unauthorized purchase card transactions totaling $86,576 were considered improper transactions and had to be ratified to become legitimate.[8]

We suggest that USAID management enhance its policies and procedures to ensure cardholders are adequately monitored for compliance with purchase card policies.

Loan Subsidiary Ledgers

USAID did not identify the cause of differences between its general ledger and its loan subsidiary ledger, which is maintained by Midland Bank, its loan services provider. During USAID's monthly reconciliation of the two ledgers, Office of CFO staff found differences totaling $2 million as of September 30, 2017. They did not adjust the ledgers or research the differences because Agency management did not prioritize these actions in FY 2017. Further, USAID relied on an ad hoc analysis to support certain general ledger posting amounts because the Agency does not have a subsidiary ledger for loan guarantee liability amounts. Relying on the subsidiary ledger, or an ad hoc analysis for general ledger totals, without researching discrepancies increases the risk that the financial statements may be misstated. For example, cumulative years of not reconciling the ledgers resulted in an adjustment of $26 million in FY 2017 that corrected errors made in FY 2009.

[8] ADS chapter 331, section V, "Six Steps in the Buying Process."

We suggest that USAID's chief financial officer develop written policies and procedures to resolve differences between the loan subsidiary ledger and the general ledger, to meet federal internal control standards.[9]

Travel Vouchers

Cardholders' travel activities were not adequately monitored to ensure that they submitted their travel vouchers within the required timeframe. Specifically, 15 of the 45 travel vouchers we reviewed were not submitted within 5 business days of completion of travel.[10] Without adequate monitoring and timely submission of travel vouchers, funds that are no longer needed for travel will not be deobligated and made available for other purposes. Therefore, we suggest that USAID management enhance its policies and procedures to ensure cardholders are adequately monitored for compliance with travel policies.

Internal Use Software

The CFO lacked a control process for ensuring accuracy of the Agency's internal use software (IUS) balance. Although the CFO is responsible for maintaining the general ledger accounts for capitalized property and operating materials and supplies,[11] we found that the CFO heavily relies on the chief information officer (CIO) to determine whether the IUS meets capitalization requirements. No review or validation is conducted by the CFO to ensure accuracy of the capital internal use software reported in USAID financial statements. Consequently, the CIO's determinations have a direct effect on USAID financial statements without any supervision or review by the CFO.

Therefore, we suggest that the CFO implement a control process to review and ensure the accuracy of USAID's internal use software balance.

INTERNAL CONTROL DEFICIENCIES AT MISSIONS

We identified the following internal control deficiencies in the 10 missions included in our audit.

Unfunded Accrued Annual Leave (Repeat Finding)

Missions did not consistently provide accurate annual leave balances to the Office of the CFO. One mission reported inaccurate, unfunded accrued annual leave balances for Foreign Service Nationals and third-country nationals for the second and third quarters of FY 2017, because it used erroneous hourly rates and salary grades. As a result of the inaccuracies, the Separation Trust Fund account was not accurately reported. In addition, one mission did not have evidence that the calculation was reviewed or approved by a supervisor or mission executive officer.

Chief Financial Officer's Bulletin No. 08-1002 states that mission controllers must perform an accurate calculation of the liability for the current fiscal year per employee and in total as determined in accordance with the local compensation plan.

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[9] GAO's Standards for Internal Control in the Federal Government indicates that management should "design control activities to achieve objectives and respond to risks."
[10] ADS chapter 633, section 633.3.5, "Travel Voucher Processing Requirements."
[11] ADS chapter 629, "Accounting for USAID-Owned Property and Internal Use Software."

Therefore, we suggest that the CFO coordinate with mission directors and mission controllers to conduct a more thorough review of the unfunded accrued annual leave balances before quarterly submission to the Office of the CFO.

Travel Vouchers (Repeat Finding)
Employees at three missions did not submit their travel vouchers within the required timeframe (i.e., within 5 business days of trip completion, or every 30 calendar days for extended travel).[12] As a result, the missions were unable to make unliquidated balances available for other purposes. We have reported this finding continually for the past 3 years, and we continue to suggest that the CFO's office coordinate with mission directors and mission controllers to stress to mission personnel the importance of submitting travel vouchers within the established timeframe.

Accrued Expenses (Modified Repeat Finding)
Nine missions had deficiencies in calculating, documenting, and recording quarterly estimates of accrued expenses:

- One mission had misstated two project accruals because of accounting/processing errors.
- One mission had one accrual that was not properly approved and another accrual that erroneously included a payment as a part of the accrual calculation.
- One mission had two travel advances carried over as accruals for 2 years that had not been deobligated.
- Two missions recorded four accruals without adequate supporting documentation.
- Five missions recorded six accruals that did not match the accrual supporting documentation.

The contracting officer's representative is responsible for maintaining the official accrual documentation so that it is readily available for audit, and for notifying the obligating official to deobligate excess or unneeded funds.[13] The accruals should be based on an analysis of the projected expenditure rate or actual expenditures for an activity.

Therefore, we suggest that USAID's chief financial officer continue efforts to validate quarterly accrued expenses reported by the missions.

[12] ADS chapter 633, "Financial Management Aspects of Temporary Duty Travel."
[13] ADS chapter 631, "Accrued Expenditures."