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AUDIT REPORT
ON
FISCAL YEAR 1985 OBLIGATIONS
AUDIT REPORT NO. 0-000-87-01
February 6, 1987

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D. C. 20503

February 6, 1987

MEMORANDUM FOR C/AID, Marshall D. Brown
AA/PPC, Richard E. Bissell
FROM: RIG/A/W, *Mervin F. Boyer, Jr.*
SUBJECT: Audit Report No. 0-000-87-01
Report on Fiscal Year 1985 Obligations

This report presents the results of an audit of "Year-End Obligations" for fiscal year 1985. The Counselor to the Agency has agreed that comparisons of fourth quarter program and operating expense obligations will be made, that deviations from the OMB standard will be explained and that the data will be retained for subsequent review by the Inspector General; therefore, upon issuance of this report the one recommendation contained in it will be considered closed.

Background

The audit was made at the request of the AID Administrator to determine if the Agency complied with guidance on the prevention of wasteful year-end spending provided by the Office of Management and Budget (OMB) Memorandum, No. M-85-18, dated June 13, 1985; the Federal Managers' Financial Integrity Act of 1982; the OMB Circular No. A-123 on Internal Controls, dated August 16, 1983; and the Office of Federal Procurement Policy Memorandum, dated June 3, 1985.

Each year the OMB instructs U.S. Government agencies to eliminate wasteful year-end spending practices. In particular, the OMB is concerned with the prevention of obligation of funds simply to avoid their lapsing at year-end, and the elimination of last minute procurements on which sufficient time is not available to ensure reasonable cost and accountability.

The Inspector General has issued three prior audit reports on AID year-end spending practices: Report No. 83-73, dated June 20, 1983, covering fiscal year 1982; Report 84-36, dated September 27, 1984, covering fiscal year 1983; and Report No. 85-16, dated June 13, 1985, covering fiscal year 1984. These prior reports concluded in essence that the Agency's obligation patterns exceeded OMB guidelines. All recommendations contained in these prior reports had been closed at the start of the current audit.

Audit Objectives and Scope

The objectives of the audit were to: (1) determine the degree of AID's compliance with OMB guidelines on year-end spending, (2) test the validity of obligations made in the fourth quarter of the fiscal year, and (3) determine the adequacy of internal controls related to the sub-systems used to monitor progress on obligations during the year.

The audit covered \$8.2 billion in AID obligations for fiscal year 1985. This included program obligations of \$7.8 billion and operating expense obligations of \$397 million. Fourth quarter obligations were compared to the OMB standard to determine if the Agency complied with the year-end spending limitation; a sample of 43 transactions was judgmentally selected and reviewed for validity; and a limited review was made of internal controls.

The audit was performed intermittently during the period March through September 1986, and included discussions and/or reviews at various AID/Washington offices, namely: the Office of the Counselor to the Agency, the Bureau for Program and Policy Coordination, and the Bureau for Management including the Office of Financial Management, and the Office of Procurement. Audit results were discussed with the management officials of these offices as the audit progressed, and their written comments in response to a draft report have been included in or otherwise considered in the preparation of this final report.

The examination was made in accordance with generally accepted government auditing standards.

Results of Audit

Despite concerted actions taken by AID to improve year-end spending practices, the Agency has been unable to bring actual fourth quarter obligations in line with the OMB standard. However, no deficiencies were noted in our reviews of fourth quarter procurement transactions and internal controls.

Our review of fourth quarter procurement transactions included a sample of 43 transactions, totaling \$65.8 million, selected from 271 such transactions with a value of \$100,000 or more each, processed by the Office of Procurement in the fourth quarter of fiscal year 1985. Results of the review indicated that these procurements were undertaken to meet the legitimate needs of the Agency and were within the guidelines prescribed by the OMB for year-end spending.

AID has not been able to achieve the OMB fourth quarter obligation standard in fiscal year 1985 as well as in prior fiscal years dating back to 1980 - The OMB standard requires that obligations in the fourth quarter of the fiscal year be no higher than the average of obligations made in the first three quarters of the year. However, the Agency has been unable to achieve this

standard for reasons that are beyond its direct control, such as delays in obligations because of the late receipt of funds under Continuing Resolutions, delays in obligations of Economic Support Funds because of programming complexities, delays in obligations because of national policy considerations and delays in obligations because of the late receipt of funds under supplemental appropriations. No recommendation is being made with regard to the Agency's inability to meet the OMB fourth quarter obligation standard because of the external nature of the factors involved.

Discussion - The OMB standard requires that; "obligations for the fourth quarter of the fiscal year are no higher than the average of the first three quarters, except where seasonal requirements, essential program objectives, or leadtimes justify a higher level."

Although the Agency slightly improved its overall performance against the OMB standard in fiscal year 1985, it still obligated 36 percent of total funds, or \$2.9 billion in the fourth quarter of the fiscal year. This compares with a rate of 38 percent for fiscal year 1984, and an OMB standard of 21 percent for both years. The inability of the Agency to meet the OMB standard has been a longstanding and intractable problem which is reflected in performance on both program and operating expense obligations.

Program obligations accounted for 95 percent of AID's total obligations of \$8.2 billion in fiscal year 1985. AID has been unable to meet the OMB standard on program funds for fiscal years 1980 through 1985. Actual fourth quarter obligations during this period have ranged from 36 percent to 43 percent of total program obligations, and the OMB standard has been exceeded by 15 to 24 percentage points.

PROGRAM OBLIGATIONS
Fiscal Years 1980 to 1985
Dollars Millions and Percent

<u>Fiscal Year</u>	<u>Total Obligations</u>	<u>Obligated Fourth Quarter</u>	<u>OMB Standard 1/</u>	<u>Fourth Quarter Obligations in Excess of Standard</u>
1980	\$3,467	41%	20%	21%
1981	\$3,536	43%	19%	24%
1982	\$4,658	36%	21%	15%
1983	\$4,896	41%	20%	21%
1984	\$5,675	39%	20%	19%
1985	\$7,755	36%	21%	15%

1/ Average percent of funds obligated in first three quarters of the fiscal year.

Operating expense obligations for fiscal year 1985 totaled \$397 million or 5 percent of total AID obligations. Of this amount, the Agency obligated \$125 million (31%) in the fourth quarter of the fiscal year. In our prior operating expense reviews for fiscal years 1982 and 1984, the percentages were 31 percent and 32 percent, respectively. This means that the Agency exceeded the OMB standard by 8 to 9 percentage points for these three years when the OMB standard was a uniform 23 percent. More importantly, however, is the fact that operating expenses show a relatively uniform distribution pattern throughout the year as illustrated by quarterly operating expense obligations for fiscal years 1984 and 1985.

OPERATING EXPENSE OBLIGATIONS				
Percentage of Funds Obligated Each Quarter				
<u>Fiscal Year</u>	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
1984	20%	23%	25%	32%
1985	21%	23%	25%	31%

Although AID has taken and continues to take positive actions to improve its procedures to facilitate the prompt and orderly obligation of funds, the Agency has been unable to achieve the OMB fourth quarter obligation standard in fiscal years 1980 through 1985. The Agency's inability to meet the OMB standard is primarily due to a number of major external factors that are beyond its direct control. Some of these major factors, which have occurred with sufficient frequency over the years to be considered a way of doing business at AID, are:

- Delay of obligations because of uncertain funding levels and delayed receipt of funds created by congressionally mandated Continuing Resolutions.
- Delay of Economic Support Fund obligations because of legislative requirements for setting the Operational Year Budget and apportionments on a country-by-country basis.
- Delay of obligations because of national policy considerations - OMB, Treasury, and AID itself often have major concerns which delay obligation dates until political or economic objectives are successfully negotiated with U.S., host country and multilateral organizations.
- Inability to obligate funds in the initial quarters because significant amounts of funds are received late in the fiscal year by supplemental appropriations.

Given the results of audits performed to date, we believe future audits of "Year-End Obligations" should be limited to those areas

and years in which the Agency's fourth quarter obligation performance against the OMB standard varies significantly from the Agency's past experience. For the Agency to implement this audit approach, it will be necessary for the Agency to provide from its existing data base the required statistical comparisons of actual fourth quarter program and operating expense obligations to the OMB standards and explanations for any deviations from the standards. The Office of Inspector General can review these comparisons to make a decision as to the need for an audit.

Recommendation No. 1

We recommend that the Counselor to the Agency in coordination with the Bureau for Program and Policy Coordination and the Bureau for Management make statistical comparisons of actual fourth quarter program and operating expense obligations to the OMB standards. Any deviations from the standards should be explained and the data retained for subsequent review by the Inspector General.

Management Comment - Management suggested no changes to the text of the report and stated that it found the recommendation "useful" and would "... provide the IG at the end of each fiscal year a full explanation of any deviations from OMB's government-wide fourth quarter obligation standards."

Review of Internal Controls

The audit did not cover the internal controls associated with the Agency's overall integrated funds control and accounting system used to track and control appropriations, apportionments, allotments, budget allowances, obligations and expenditures. This system, described in AID Handbook 9, Chapter 1, Appendix 1A, is usually covered by a separate audit or a series of audits dealing with selected aspects of the system. The current review looked at the various sub-systems used to monitor and provide oversight of obligational activities throughout the year. Such sub-systems include comparison of actual performance against objectives established by the Operational Year Budget, oversight and follow-up activities carried out by the Counselor to the Agency with the participation of Technical and Geographic Bureaus and control exercised by the Offices of Financial Management and Procurement over certain types of procurements and year-end activities. No instances were noted in the audit to indicate any significant weaknesses in the sub-system internal controls reviewed.

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