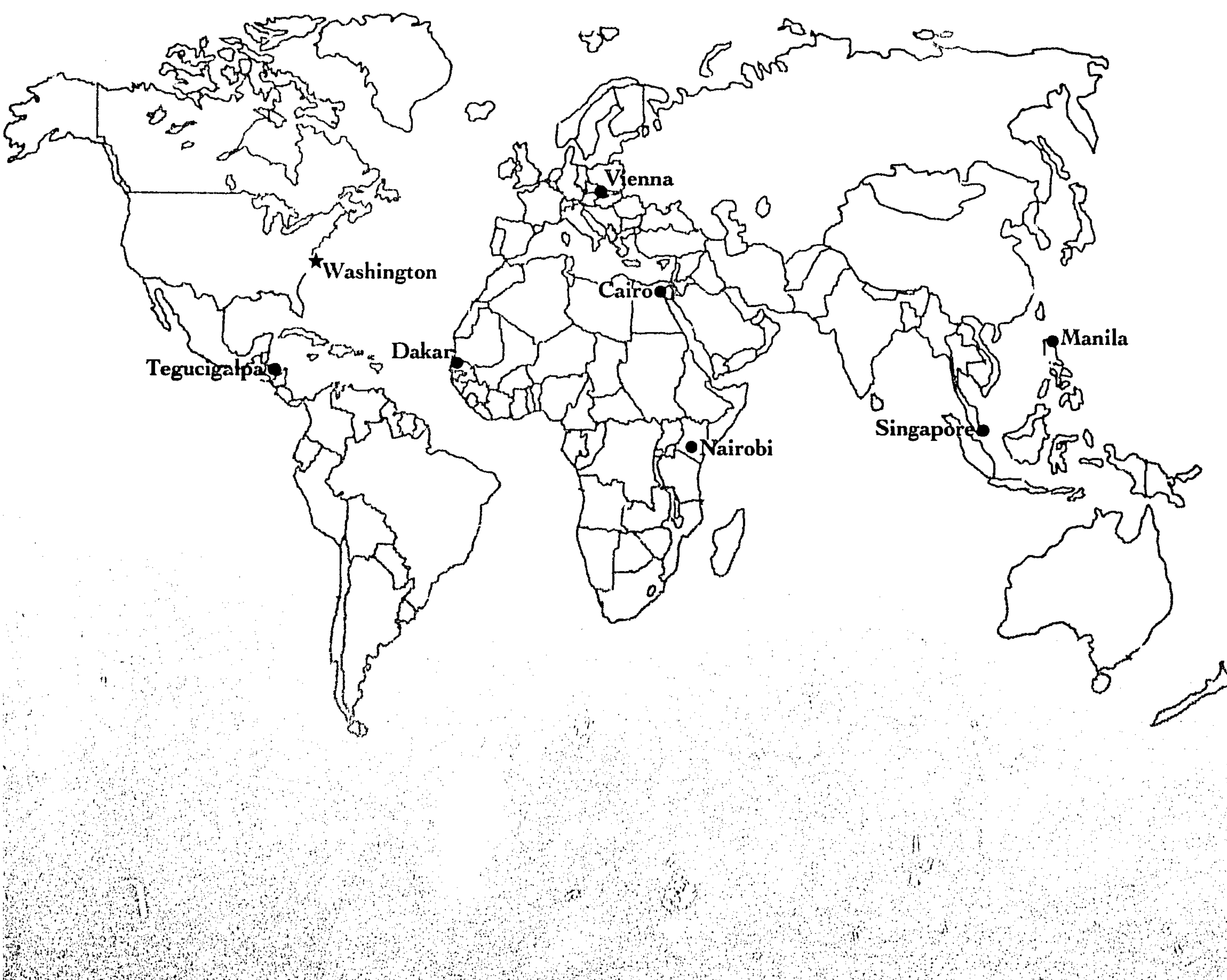
PD-ABE-928

Financial Audits

AUDIT OF THE HOUSING AND OTHER CREDIT GUARANTY PROGRAMS' FISCAL YEAR 1991 ANNUAL FINANCIAL STATEMENT UNDER THE CFOs ACT OF 1990

Report No. 0-000-92-001
July 31, 1992



INSPECTOR GENERAL

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

Agency for International Development
Washington, D.C. 20523

July 31, 1992

Assistant Inspector General
for Audit

MEMORANDUM FOR AA/FA, Richard A. Ames
AA/PRE, Ralph S. Blackman

FROM: AIG/A, John P. Competello

SUBJECT: Audit Report on A.I.D.'s Housing and Other Credit Guaranty Programs for Fiscal Year 1991

The Office of the Inspector General, in conjunction with the Certified Public Accounting firm of Price Waterhouse, completed the audit of A.I.D.'s Housing and Other Credit Guaranty Programs for Fiscal Year 1991. This report is being transmitted to you for your action.

In preparing the report we reviewed your comments on a previously submitted draft report. A summation of your comments has been included in the Executive Summary and after the appropriate audit objectives. Your comments are presented in their entirety in Appendix VII.

Your comments stated that you were in general agreement with the 13 recommendations in the report and that you intended to include a plan to address and resolve the issues in the Chief Financial Officer's five-year plan to be submitted to OMB by the end of August. However, as of July 31, 1992, the 13 recommendations are open and unresolved. In addition to submitting your plan to OMB please respond to my office within 30 days, indicating actions taken to implement the recommendations.

We appreciate the cooperation and courtesies extended to my staff and Price Waterhouse during the audit.

PD-ABE-928

AUDIT OF THE HOUSING AND OTHER CREDIT GUARANTY PROGRAMS' FISCAL YEAR 1991 ANNUAL FINANCIAL STATEMENT UNDER THE CFOs ACT OF 1990

Audit Report No. 0-000-92-001
July 31, 1992

EXECUTIVE SUMMARY

Background

The Agency for International Development's (A.I.D.) Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement includes the activities of the Housing Guaranty Program and the Agricultural and Productive Credit and Self-Help Development Program. The Agricultural and Productive Credit and Self-Development Program is inactive and account balances are immaterial.

The Housing Guaranty Program (HG) was established by Title III, Sections 221, 222, 223, and 238c of the Foreign Assistance Act of 1961 (FAA), as amended, to help Less-Developed Countries (LDCs) improve housing availability to low-income urban families.

A.I.D.'s Office of Housing and Urban Programs, in the Bureau for Private Enterprise and A.I.D.'s geographic bureaus jointly administer the A.I.D. Housing Guaranty Program. This program enables the United States private sector to provide to foreign governments, new construction and home improvement loans for low-income families. The program also finances LDC infrastructure improvements, such as for water and waste systems.

The HG charges fees to loan borrowers for the loan guaranties. The enabling legislation intended for the fees to meet costs incurred in connection with the Program. In order to meet obligations incurred for the payment of claims under the loan guaranties the HG may, to the extent that reserves are not sufficient, borrow from time to time from the Treasury. Under Credit Reform, which was effective as of October 1, 1991, significant changes occurred in the way the HG is funded; the cost of new loans and operating costs will be funded through direct appropriations and Treasury borrowings rather than through accumulated earnings supplemented by Treasury borrowings. As of September 30, 1991, the Program had active loan guaranties totalling $2.5 billion. As much as $150 million in new loan guaranties are anticipated for fiscal year (FY) 1992 and $95 million for FY 1993.

Pursuant to the provisions of the Chief Financial Officer's (CFOs) Act of 1990, the Housing and Other Credit Guaranty Programs are required to prepare an Annual Financial Statement, which includes the presentation of program and financial performance information, beginning in fiscal year 1991. The Office of the Inspector General is required to audit these Annual Financial Statements. To fulfill our responsibility, we contracted with the independent certified public accounting firm of Price Waterhouse to perform, under our general oversight, the financial audit for FY 1991. In addition, we performed certain audit procedures concerning the presentation of management performance information required by the Office of Management and Budget (OMB). This report presents the results of the audit.

Audit Objectives

We contracted with the certified public accounting firm of Price Waterhouse to audit, under our general oversight, the fiscal year 1991 financial statements of the Housing and Other Credit Guaranty Programs in accordance with generally accepted auditing standards, Government Auditing Standards, and Office of Management and Budget (OMB) Bulletin 91-14, "Audit Requirements for Federal Financial Statements".

The audit objectives were to determine whether: the financial statements of the Housing and Other Credit Guaranty Programs presented fairly the financial position, results of operations, reconciliation to budget and cash flows (see page 4); the internal control structure was adequate (see page 5); and A.I.D.'s Housing and Other Credit Guaranty Programs' management had complied with laws and regulations for those transactions and events that may have a material effect on the financial statements (see page 11).

Additionally, the Office of the Inspector General for Financial Audits performed certain audit procedures to determine whether the Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement complied with program and financial performance reporting guidance contained in OMB Bulletin No. 91-15, "Guidance on Form and Content on FY 1991 Activity", and OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures?" (See pages 13 and 21.)

The audit field work was conducted from March 1992 through July 1992. Appendix I contains a complete discussion of the scope and methodology for this audit.

Summary of Audit

Price Waterhouse was unable to, and did not express an opinion on the financial statements, and we concur. The accounting records maintained by the Housing and Other Credit Guaranty Programs did not provide sufficient evidence supporting various transactions and account balances to permit the application of adequate auditing procedures nor was Price Waterhouse able to apply alternative auditing procedures to satisfy themselves regarding various account balances, and automated systems were inadequate to facilitate audit testing. The Housing and Other Credit Guaranty Programs did not have an adequate internal control structure. The audit disclosed eight internal control reportable conditions. Seven of the reportable conditions were classified as material weaknesses. Most of the material weaknesses concerned the lack of adequate formal, documented policies and procedures for Financial Management/Loan Management (FM/LM). The audit disclosed three instances of material noncompliance with laws and regulations pertaining to the Debt Collection Act of 1982, the Budget and Accounting Procedures Act of 1950, and the Federal Managers' Financial Integrity Act (FMFIA). The Housing and Other Credit Guaranty Programs' Annual Financial Statement did not fully comply with OMB program and financial performance reporting guidance. (See Audit Findings section below.)

The audit also disclosed several noteworthy issues:

- During fiscal year 1991 the HG continued to incur losses. The Program incurred a net loss of $34 million and had to borrow $48 million from the U.S. Treasury to sustain operations. As a result, borrowing now totals $130 million. (See pages 24 and 25.) Under the Credit Reform Act of 1990 (PL 101-508), which was effective as of October 1, 1991, repayment of the pre-fiscal year 1992 Treasury debt will be funded through a permanent indefinite appropriation (see page 2).

- The HG guaranty fee structure needs to be reassessed to see if a risk-based structure is feasible, in light of developmental objectives. The HG generally charged a front end fee of one percent and an annual fee of one-half percent. These fees were set at the same level regardless of a country's repayment ability. Starting in fiscal year 1992, discretionary funds will be appropriated based on subsidy calculations. These subsidies could be reduced if a risk-based fee structure is deemed to be a feasible alternative to the current fee structure. (See page 5.)

- The lack of adequate policies and procedures is prevalent in many areas, as evidenced by the internal control weaknesses (see pages 6 through 11). The CFOs Act of 1990 envisions the enhancement of financial management systems and controls, and improving financial reporting practices and the reliability of generated financial information. In light of the challenges presented by the CFOs legislation, it is imperative that management maintain an accounting and financial management system that provides timely, accurate and relevant information. The HG and Financial Management/Loan Management (FM/LM) must make the elimination of material internal control weaknesses a priority. This may very well require deployment of additional staff to focus on the problem areas and meet the demands of the CFOs Act. Toward this end, FM/LM has made headway towards correcting internal control problems disclosed in the fiscal year 1990 financial statement audit; 13 of our 14 recommendations resulting from that audit have been resolved or closed and FM/LM has indicated they will provide us evidence shortly which, in their opinion, will result in closure of most of these recommendations by September 30, 1992. (See Appendix VIII)

- In our opinion, the internal control weaknesses described in this report collectively meet the OMB's definition of a material weakness. Accordingly, the agency should include the HG as a material weakness in the 1992 Federal Managers Financial Integrity Act (FMFIA) report. (See pages 10 and 11.)

Audit Findings

Disclaimer of Opinion

Price Waterhouse was unable to, and did not express an opinion on the financial statements, and we concur. The accounting records maintained by the Housing and Other Credit Guaranty Programs did not provide sufficient evidence supporting various transactions and account balances to permit the application of adequate auditing procedures. Also, Price Waterhouse was unable to apply alternative auditing procedures to satisfy themselves regarding various account balances, and automated systems were inadequate to facilitate audit testing. (See page 4.)

Internal Controls

The Housing and Other Credit Guaranty Programs did not have an adequate internal control structure. The audit disclosed eight reportable conditions. Seven of the reportable conditions were classified as material weaknesses. As defined by generally accepted auditing standards, a material weakness is a reportable condition in which the design or operation of specific elements of the internal control structure did not reduce to a relatively low level, the risk that errors or irregularities, in amounts that would be material to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. The material weaknesses pertained to the following: (1) management has not adequately evaluated the HG for attaining legislative objectives in a cost effective manner, (2) lack of formal policies and procedures and an automated accounting system, (3) insufficient monitoring of the paying and transfer agent, (4) source documentation was not adequately maintained, (5) lack of collection procedures for claims receivable collection, (6) lack of documented formal guidelines or systems to identify loans which require claim payments or to minimize late fees and penalties paid on behalf of the borrower, and (7) the HG Central Reserve Bank Account was not maintained in a U.S. Treasury account. Additionally, the Agency did not include the HG as a material weakness in the latest Federal Managers' Financial Integrity Act (FMFIA) report. (See page 5.)

Compliance with Laws and Regulations

The audit disclosed three instances of material noncompliance pertaining to the Debt Collection Act of 1982 with respect to collection procedures and maintenance of lender information, the Budget and Accounting Procedures Act of 1950 with respect to maintaining funds outside the U.S. Treasury, and the Federal Managers' Financial Integrity Act with respect to maintaining adequate internal controls and reporting material internal control weaknesses. (See page 11.)

OMB Financial and Program Performance Reporting Guidance

The Housing and Other Credit Guaranty Programs' Annual Financial Statement did not fully comply with OMB's program and financial performance reporting guidance. Specifically, the review disclosed that (1) the HG Annual Financial Statement did not present the extent to which the program achieved its goals and objectives, (2) the program performance information that was provided in the 1991 statement was not adequately supported or always accurate, and (3) although the Overview did contain some financial performance information, additional financial performance and management measures/indicators or analyses were needed. Fiscal year 1991 was the first year that the Housing and Other Credit Guaranty Programs were required to present program and financial performance information in an Annual Financial Statement; management recognizes the need to develop performance measures in future years that will provide a more complete presentation of financial and program results, measured against appropriate goals and objectives. (See pages 13 through 26.)

Cost and Debt of the
<u>Housing Guaranty Program</u>

In connection with our review of the Annual Financial Statement presentation of financial performance measures, we performed some additional analyses. These analyses indicated the following:

- The HG lost $55,979,000 for fiscal year 1989, $82,190,000 for fiscal year 1990, and $33,906,000 for 1991. These amounts represent total operating costs less fees and other revenues. The loss (or net operating cost) is an important indicator because it represents an indication of what the HG costs the taxpayer. (See page 23.) Under the Credit Reform Act of 1990 (PL 101-508), which was effective as of October 1, 1991, net costs of the program will be funded predominantly through appropriations. (See page 2.)

- The HG owed $130,000,000 to the U.S. Treasury as of September 30, 1991. The amount owed to the U.S. Treasury has progressively increased since 1987. The interest expense to the HG on this level of borrowing is about one million dollars per month, which we believe is significant. Based on the 1990 financial statement audit performed by Price Waterhouse, we recommended that A.I.D. management devise a plan to repay these debts (see our Report No. 0-000-92-01-N dated December 11, 1991). In March 1992 management advised us that an Agency committee is developing a plan to repay this debt. Additionally, under the Credit Reform Act of 1990, repayment of pre-fiscal year 1992 Treasury debt will be funded through a permanent indefinite appropriation. (See page 24.)

Summary of Recommendations

This report includes nine recommendations for action by the Associate Administrator for Finance and Administration, and four recommendations for action by the Assistant Administrator for Private Enterprise. The recommendations for the Associate Administrator for Finance and Administration pertain to: developing accounting policies and procedures and continuing efforts towards automating the accounting system, proper monitoring of the paying and transfer agent, developing collection procedures for claims collection, developing a system to identify necessary claim payments, proper reporting and custody of A.I.D. funds, determination of whether the Annual Financial Statement should encompass all applicable programs, development of additional financial performance measures/indicators, development of guidance for implementation of the CFOs Act requirements, and including the Housing Guaranty Program (HG) as a material weakness in the next FMFIA report. (See pages 6 through 11, 17, and 21.) The recommendations for the Assistant Administrator for Private Enterprise concern evaluating the HG for attaining legislative objectives in a cost effective manner, developing policies/procedures for retaining source documentation, the development of program performance measures/indicators, and the development of a system to collect performance measure data. (See pages 6,8 and 17.)

Management Comments and Our Evaluation

We provided a draft copy of this report to the Chief Financial Officer and the Assistant Administrator for Private Enterprise, as well as various other Financial Management and HG officials who were involved in this audit. In commenting on the draft report, management provided some discussion of the merits of the HG, the impact of the LDC debt crisis on the program, the impact of credit reform, and comments on program and financial management systems. Management indicated they were in general agreement with our recommendations and that a plan to address and resolve the recommendations will be prepared by the end of August 1992.

We would like to clarify an issue raised in paragraph three of management's response (see Appendix VII). The first sentence of paragraph three states that "The Audit Report states that the HG program is intended to be self-supporting and should therefore revise its fee structure upward". Our recommendation No. 1b is that "We recommend that the Assistant Administrator for Private Enterprise, in conjunction with the Associate Administrator for Finance and Administration, reassess the current guaranty fee structure to determine if adoption of a risk-based fee structure is feasible, in light of developmental objectives." (See page 6.) We believe that the adoption of a risk-based fee structure could reduce the cost of future loan guaranties. However, a change in fee structure would have to be considered in conjunction with feasibility, particularly in terms of developmental objectives.

Appendix VII presents a complete text of management's comments to the draft of this report.

Office of the Inspector General

Office of the Inspector General
July 31, 1992

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INTRODUCTION

Background

The Agency for International Development (A.I.D.) administers the Housing Guaranty Program (HG) and the Agricultural and Productive Credit and Self-Help Community Development Program, programs established by Congress to stimulate the participation of the private sector in the economic development of Less-Developed Countries (LDC). These programs operate as revolving funds.

The HG was established by title III, Sections 221, 222, 223, and 238c of the Foreign Assistance Act of 1961 (FAA), as amended, to help host countries to improve the level of housing available to the less advantaged portions of their populations. Through this program, the United States private sector provides long term financing for low-income shelter (e.g., new construction loans, home improvement loans, etc.) and neighborhood infrastructure upgrading programs (e.g., water, sewer, etc.) in developing countries. U.S. private sector lenders provide unsecured financing at commercial rates (a lower rate can be charged due to lower risk brought about by the U.S. guaranty) to a host country borrower for financing loans to eligible host country resident borrowers. A.I.D. charges a fee for its guaranty; A.I.D. charges the borrower an initial (front-end) fee of one percent of the loan amount, paid at the time of disbursement. A.I.D. also charges an annual guaranty fee of one-half of one percent on outstanding loan balances. The guaranty fee is used to pay for program administrative expenses available to pay claims covered by the guaranties. The enabling legislation intended for the fees to meet costs incurred in connection with the program. In order to meet obligations incurred for the payment of claims under the loan guaranties the HG may, to the extent that reserves are not sufficient, borrow from time to time from the Treasury.

The HG is jointly managed by The Office of Housing and Urban Programs within A.I.D.'s Bureau for Private Enterprise (PRE) and A.I.D.'s geographic bureaus. There are also seven Regional Housing and Development Offices (RHUDOs) which are the overseas components of the Office of Housing and Urban Programs. The Loan Management Division in the Office of Financial Management (Financial Management/Loan Management) carries out the responsibilities of "Controller" for the HG. Financial Management/Loan Management maintains the official A.I.D. accounts and the accounting controls over the assets, liabilities, and capital of the HG.

As of September 30, 1991 the total principal amount of guaranties issued and outstanding could not exceed $2,558 million at any one time (this limitation can be increased by Congress). As of September 30, 1991, total authorized and outstanding guaranties were $2,553 million. The HG anticipates issuance of up to $150 million of new guaranties in fiscal year 1992 and approximately $95 million of new guaranties in fiscal year 1993. This does not include any additional guaranty programs which may be proposed by the Administration.

The Housing Guaranty Program is subject to the Federal Credit Reform Act of 1990 (PL 101-508) which was effective as of October 1, 1991. The primary objective of Credit Reform is to identify the costs inherent in federal credit programs so that they may be compared more easily with the costs of other federal spending. Consequently, commencing in fiscal year 1992, the program's activities will be funded through direct appropriation and borrowings from Treasury rather than through retained earnings accumulated over the years. Accordingly, the Housing Guaranty Program's financial presentation of its credit activities will change in 1992 and subsequent years as deficiencies are anticipated in the budget process and funded in advance through appropriations.

The Agricultural and Productive Credit and Self-Help Community Development Program (Productive Credit Guaranty Program) is inactive; no additional guaranties have been issued under this program since 1988. It is included in this audit because there are still outstanding guaranty balances on the books, however these balances are immaterial.

Pursuant to the provisions of the Chief Financial Officer's (CFOs) Act of 1990, the Housing and Other Credit Guaranty Programs are required to prepare an Annual Financial Statement, which includes the presentation of program and financial performance information, beginning in fiscal year 1991. The Office of the Inspector General is required to audit these Annual Financial Statements. To fulfill our responsibility, we contracted with the independent certified public accounting firm of Price Waterhouse to perform, under our general oversight, the financial audit for FY 1991. In addition, we performed certain audit procedures concerning the presentation of management performance information required by the Office of Management and Budget. This report presents the results of the audit.

Audit Objectives

We engaged the certified public accounting firm of Price Waterhouse to audit, under our general oversight, A.I.D.'s Housing and Other Credit Guaranty Programs' fiscal year 1991 financial statements to answer the following objectives:

- Did the Housing and Other Credit Guaranty Programs' fiscal year 1991 financial statements and the notes to the financial statements present fairly in all material respects the financial position, operations and government equity (deficiency), cash flows, and reconciliation to budget in accordance with applicable accounting standards?

- Did the Housing and Other Credit Guaranty Programs have an adequate internal control structure?

- Did the Housing and Other Credit Guaranty Programs comply with laws and regulations that could have a direct and material effect on the financial statements and certain other laws and regulations designated by OMB and A.I.D.?

Additionally, the Office of the Inspector General for Financial Audits performed certain audit procedures to answer the following objectives:

- Did the Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement comply with program performance reporting guidance contained in OMB Bulletin No. 91-15, "Guidance on Form and Content on FY 1991 Activity", and OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures"?

- Did the Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement comply with financial performance reporting guidance contained in OMB Bulletin No. 91-15, "Guidance on Form and Content on FY 1991 Activity", and OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures"?

In answering these objectives, we relied on Price Waterhouse's assessments of internal controls and compliance with laws and regulations. Our audit procedures were sufficient to provide reasonable assurance that our answers to the above audit objectives are valid. Furthermore, when we found problem areas, we performed additional work to:

- identify the cause and effect of the problem; and

- make recommendations to correct the condition and cause of the problem.

The audit field work was conducted from March 1992 through July 1992. Appendix I contains a complete discussion of the scope and methodology for this audit.

REPORT OF AUDIT FINDINGS

Did the Housing and Other Credit Guaranty Programs' financial statements and the notes to the financial statements present fairly in all material respects the financial position, operations and government equity (deficiency), cash flow, and reconciliation to budget in accordance with the applicable accounting standards?

Price Waterhouse was unable to, and did not, express an opinion on the financial statements. We concur with Price Waterhouse. The disclaimer of opinion resulted from scope restrictions relating to the condition of the Housing Guaranty Program's (HG) underlying accounting records and systems. The accounting records and systems did not provide sufficient evidence supporting various transactions and account balances to permit the application of adequate auditing procedures. Also, Price Waterhouse was unable to apply alternative auditing procedures to satisfy themselves regarding various account balances.

The HG account balances that were unsupported and the nature of the insufficient accounting records and systems included:

- claims receivable and outstanding guaranties were not adequately supported by accounting records or automated systems which identified the related lenders and host country administrators,

- weaknesses in the general accounting systems and in the controls surrounding them could cause errors that would affect the Housing and Other Credit Guaranty Programs' financial statements, and

- A.I.D. had not analyzed its unapplied disbursements account to determine any effect on the accounts of the HG.

Also, due to the inadequate records and systems, Price Waterhouse could not apply alternative auditing procedures to satisfy themselves regarding cash, accounts payable, accrued expenses and other liabilities, claims receivable, and furniture and equipment. (See Price Waterhouse's Report on the Principal Statements, Appendix III.)

Did the Housing and Other Credit Guaranty Programs have an adequate internal control structure?

The Housing and Other Credit Guaranty Programs did not have an adequate internal control structure. The audit disclosed eight reportable conditions relating to significant deficiencies in the design or operation of the internal control structure that could adversely affect the organization's ability to record, process, summarize, and support financial data consistent with the assertions of management in the financial statements. Seven of the reportable conditions were classified as material weaknesses. As defined by generally accepted auditing standards, a material weakness is a reportable condition in which the design or operation of specific elements of the internal control structure does not reduce to a relatively low level, the risk that errors or irregularities, in amounts that would be material to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. In addition, we found that the Agency did not include the Housing Guaranty Program (HG) as a material weakness in its 1991 FMFIA report. We believe the pervasiveness of internal control problems to be such that the Agency should include this as a material weakness in the 1992 report. The material weaknesses and our recommendations for corrective action are discussed below. (See the Price Waterhouse Report on Internal Controls for details of the material weaknesses and recommendations, Appendix V.)

A.I.D. has not Adequately Evaluated the HG for Attaining Legislative <u>Objectives in a Cost Effective Manner</u>

A.I.D. has not adequately evaluated the HG to determine that it is attaining legislative objectives in a cost effective manner, as evidenced by the following conditions:

- A.I.D.'s fee structure was not risk based. The HG generally charged a front end fee of one percent and an annual fee of one half percent. These fees were set at the same level regardless of a country's repayment ability. Starting in fiscal year 1992, under Credit Reform, discretionary funds will be appropriated based on subsidy calculations. These subsidies could be reduced if a risk based fee structure is deemed to be a feasible alternative to the existing structure.

- The HG has incurred substantial interest cost on debt to the U.S. Treasury. Since 1987, the Program has had to increasingly borrow from Treasury to sustain operations. These borrowings totaled $130,000,000 as of September 30, 1991. Interest expense on this debt will be approximately $12 million per year for the next six years, and lesser amounts thereafter through the year 2000. Repayment of the debt is scheduled to occur during fiscal years 1997 through 2000. Elimination or prepayment of this debt would substantially reduce the interest expense to the HG.

Because of the changing legislative requirements and economic conditions in which the HG operates, querying of standard operating procedures is desirable. High management turnover coupled with limited resources contributed to a lack of formal, written policies concerning fee assessment and cash management, and routine reassessment of significant operating practices. The deficit financial condition of the program was not mitigated since management was not required by written procedures to conduct routine reassessments of fee structure and cash management. The lack of routine reassessments of fee structure and cash management may have contributed to the fact that original appropriations together with fees collected no longer cover administrative and operating expenses. Additionally, the fee structure impacts the subsidy appropriations required to operate the Program under Credit Reform.

<u>Recommendation No. 1:</u> **We recommend that the Assistant Administrator for Private Enterprise, in conjunction with the Associate Administrator for Finance and Administration:**

a. discuss with the Office of Management and Budget the options to prepay or eliminate the U.S. Treasury debt,

b. reassess the current guaranty fee structure to determine if adoption of a risk-based fee structure is feasible, in light of developmental objectives,

c. analyze all other policies based on precedent and historical practice, and

d. document, and formalize into a comprehensive manual which has been approved by appropriate management officials, the policies identified in recommendation No. 1c.

Inadequate Policies/Procedures
and Manual Accounting System

Financial Management/Loan Management's (FM/LM) policies and procedures were not formalized and documented; nor was the accounting function automated. OMB Circular A-127, "Financial Management Systems", and the "GAO Policy and Procedures Manual, Title 2 -- Accounting" require that all Government agencies establish and maintain effective financial management systems that are well documented. The A.I.D. handbooks did not address certain activities that are unique to the HG's financial operations, and policies and procedures specific to FM/LM had not been developed. The design of an automated general ledger was in process, but had not been completed. These factors resulted in frequent errors in financial statement reporting. The audit identified seven areas where discrepancies could be attributed to the lack of guidance and a predominantly manual accounting system.

> **Recommendation No. 2: We recommend that the Associate Administrator for Finance and Administration develop, formalize, document, and publish policies and procedures for Financial Management/Loan Management and continue efforts towards automating the accounting system.**

Insufficient Monitoring of
Paying and Transfer Agent

The activities of the paying and transfer agent were not sufficiently monitored. Both OMB Circular A-123, "Internal Control Systems", and the Budget and Accounting Act of 1950 require that Government agencies maintain adequate systems of internal control. The reasons for the lack of monitoring was a lack of personnel resources and the fact that oversight has not been a priority. Since Loan management relies on loan status reports and requests for claim payments submitted by this agent, the lack of monitoring may have resulted in errors in the claims receivable balance as well as other data. Additionally, the lack of monitoring may have resulted in A.I.D. monies earning less than optimal interest income.

> **Recommendation No. 3: We recommend that the Associate Administrator for Finance and Administration develop policies and procedures requiring sufficient monitoring of the paying and transfer agent.**

Original Source
Documentation Not Maintained

Numerous source documents, including contracts, were inadequately maintained in the Office of Housing and FM/LM. GAO's "Policy and Procedures Manual for Guidance of Federal Agencies" requires that an accounting system be supported by appropriate source documentation. Responsibility for maintenance of documents had not been formally established by the Office of Housing or FM/LM, filing space was limited, and state-of-the-art filing systems were not taken advantage of. As a result, due to the number of contracts and other documents which were not available, management's assertions in the financial statements were unsupported and appropriate source documents would not be available should a legal dispute arise.

Recommendation No. 4: We recommend that the Assistant Administrator for Private Enterprise, in consultation with the Associate Administrator for Finance and Administration, develop effective policies and procedures for maintaining original source documentation, including defining custodial responsibility.

Claims Receivable Collection
Procedures are Inadequate

FM/LM followed informal procedures for collecting outstanding claims receivable. Documented collection procedures are essential to the effective collection of outstanding receivables because they allow for standardization and accountability, as well as the development of financial management performance measurement related to receivables collection. Management has not made collection of outstanding claims receivable a priority, and attempting to collect claims from debtors, which in many cases was a host country government, was a cumbersome and time consuming process. The lack of formal documented procedures in this area contributed to the HG's losses realized on claims receivable.

Recommendation No. 5: We recommend that the Associate Administrator for Finance and Administration establish and document collection procedures to be followed when attempting to collect outstanding claim receivables.

Lack of a System to Identify
Necessary Claim and Other Payments

FM/LM's procedures for identifying necessary claim payments were informal and documented formal guidelines or systems to identify loans for which claim payments would be necessary were nonexistent. Actual practices followed were about the same for each claim, however the time periods in which these activities were performed varied widely. Additionally, it appears that payments of borrower late fees or penalties may have been paid unnecessarily. OMB Bulletin 91-05, "Guidance Management of Guaranteed Loans", requires that agencies effectively administer their guaranteed loan programs. Apparently this breakdown in accountability occurred because FM/LM did not make accurate, timely recognition of claims payable a priority. This situation resulted in losses being incurred due to untimely or inaccurate identification of claims, as well as unnecessary payment of late fees and interest on behalf of the borrower.

> **Recommendation No. 6: We recommend that the Associate Administrator for Finance and Administration develop documented formal guidelines and a system to identify loans for which claim payments will be necessary and to minimize late fees and penalties paid on behalf of the borrower.**

All A.I.D. Funds not
Under U.S. Treasury Custody

Funds held in the Central Reserve Bank Account (CRBA) at Riggs National Bank were not under U.S. Treasury custody, nor were they originally reflected on the balance sheet. Generally accepted accounting principles require that all assets in the possession of an organization be reflected on the balance sheet (statement of financial position) and GAO Title 7 requires that these funds be held by the U.S. Treasury. The CRBA funds were not handled correctly because: (1) the nature of the CRBA has changed over time, and (2) since insufficient records were not maintained, it was only recently that a reconstruction of the account indicated that substantially all of these funds (an average balance of approximately $350,000) belonged to A.I.D. For the host country guaranteed loans serviced by the CRBA, the claims receivable balance before audit adjustments was understated because claim loss recognition was not handled correctly.

Recommendation No. 7: We recommend that the Associate Administrator for Finance and Administration report the Central Reserve Bank Account (CRBA) balance to Treasury as funds which are available to operate the Housing Guaranty Program and take steps to comply with GAO Title 7.

Material Weaknesses not Specifically Cited in Federal Managers' Integrity Act Report

Under the Federal Managers' Financial Integrity Act (31 U.S.C.3512[c]) and Office of Management and Budget (OMB) implementing policies, A.I.D's management is responsible for establishing and maintaining adequate internal controls that reasonably assure:

-- Obligations and costs comply with applicable law.

-- All assets are safeguarded against waste, loss, unauthorized use, and misappropriation.

-- Revenues and expenditures applicable to agency operations are recorded and accounted for properly so that accounts and reliable financial and statistical reports may be prepared and accountability of the assets may be maintained.

Section 3512 (d) of the law requires that the head of each agency prepare an annual report stating whether the agency's internal controls meet these standards and describing any material weaknesses in its internal controls. Within A.I.D., the Management Control Review Committee (MCRC) is responsible for reviewing internal control assessments prepared by A.I.D.'s components and recommending to the Administrator which internal control problems should be reported as material weaknesses.

The Office of Management and Budget (OMB) Circular A-123 defines a material weakness as one which would:

-- significantly impair the fulfillment of an agency component's mission; deprive the public of needed services; violate statutory or regulatory requirements; significantly weaken safeguards against waste, loss, unauthorized use or misappropriation of funds, property, or other assets; or result in a conflict of interest.

An August 3, 1991 memorandum from the OMB states that, since the above factors are judgmental and can be widely interpreted, each material weakness should meet one or more of the following additional criteria:

- merits the attention of the agency head/senior management, the Executive Office of the President, or the relevant Congressional oversight committee;
- exits in a major program or activity;
- could result in loss of $10 million or more, or 5 percent or more of the resources of a budget line item; or
- its omission from the report could reflect adversely on the management integrity of the agency.

In our opinion, the internal control weaknesses described in this report collectively meet the definition of a material weakness. Therefore, the Office of the Inspector General believes that the Agency should specifically include the HG among the material weaknesses to be reported to the President and the Congress at the end of the current fiscal year under the provisions of the Federal Managers' Financial Integrity Act (FMFIA).

> **Recommendation No. 8: We recommend that the Associate Administrator for Finance and Administration include, as a material weakness, the Agency's Housing and Other Credit Guaranty Programs among the material weaknesses to be reported at the end of the current fiscal year in the Federal Managers' Financial Integrity Act (FMFIA) report.**

Did the Housing and Other Credit Guaranty Programs comply with laws and regulations that could have a direct and material effect on the financial statements and certain other laws and regulations designated by OMB and A.I.D.?

The audit disclosed that the HG did not comply with all laws and regulations that may have directly affected the financial statements and other laws and regulations specified by A.I.D. and OMB. Specifically, the HG did not comply with applicable provisions of the Debt Collection Act of 1982 with respect to the billing and collection of claims receivable, the Budget and Accounting Procedures Act of 1950 with respect to maintaining funds outside the U.S. Treasury, and the Federal Managers' Financial Integrity Act (FMFIA) of 1982 with respect to the establishment of internal administrative and accounting controls, and reporting material internal control weaknesses in the annual FMFIA reports. These are considered to be material instances of noncompliance.

Price Waterhouse tested for compliance with the following laws:

- Federal Managers' Financial Integrity Act of 1982
- Title III of the Foreign Assistance Act of 1961, as amended,
- Chief Financial Officers Act of 1990,
- Budget and Accounting Procedures Act of 1950,
- Debt Collection Act of 1982,
- Prompt Payment Act.

Noncompliance: Debt
<u>Collection Act of 1982</u>

Noncompliance with the Debt Collection Act of 1982 resulted from inadequate collection procedures with respect to claims collection, and inaccurate and/or noncurrent lender and host country information contained in the recently implemented Housing Guaranty Portfolio Management System (HGPMS).

Noncompliance: Budget and
<u>Accounting Procedures Act of 1950</u>

The HG did not comply with the Budget and Accounting Procedures Act of 1950 because program funds of approximately $350,000 on average were maintained at a commercial bank and were not reported in the program's financial reports to Treasury. The Budget and Accounting Procedures Act of 1950 requires that the program's systems conform to the accounting principles, standards, and related requirements prescribed by the Comptroller General of the United States. In GAO's "Policies and Procedures Manual for Guidance of Federal Agencies", Title VII, Fiscal Procedures, the Comptroller General requires that except where Congress may have specifically legislated to the contrary, all public funds must be deposited in accounts maintained by the U.S. Treasury.

Noncompliance: Federal
Managers' Financial Integrity Act

A.I.D. management has not ensured compliance with the requirements of the Federal Managers' Financial Integrity Act (FMFIA) of 1982 to establish internal administrative and accounting controls for the HG. Additionally, A.I.D.'s most recent FMFIA report did not reflect the material weaknesses of the HG internal control system. (Also see comments on page 11.)

For additional information concerning the noncompliances refer to the Price Waterhouse Report on Compliance with Laws and Regulation (see Appendix VI).

Did the Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement comply with program performance reporting guidance contained in OMB Bulletin No. 91-15, "Guidance on Form and Content on FY 1991 Activity", and OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures"?

A.I.D.'s Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement did not fully comply with OMB program performance reporting guidance. The HG's Annual Financial Statement includes some program descriptive information, however, it does not give a complete and clear picture of the Program's performance during fiscal year 1991. Fiscal year 1991 was the first year the Housing and Other Credit Guaranty Programs were required to present program performance information in an Annual Financial Statement; management recognizes the need to develop program performance measures in future years that will provide a more complete presentation of Program results, measured against appropriate goals and objectives.

Specifically, the review disclosed that (1) the HG's Annual Financial Statement did not present the extent to which the program achieved its goals and objectives, and (2) the program performance information that was provided in the 1991 statement was not adequately supported or always accurate.

The following sections discuss these two issues.

A.I.D. Needs to Improve Its Presentation of Housing Guaranty Program Performance

What is the Purpose of the Overview and Supplemental Sections?

The purpose of the Overview section of the Annual Financial Statement is to provide the reader with a clear and concise understanding of the reporting entity's activities, accomplishments, financial results and condition, problems, and needs. It should tell the reader whether and how well the mission of the reporting entity is being accomplished and what, if anything, needs to be done to improve either program performance or financial performance.

A key section of the Overview is the entity's discussion of program performance. This section should present the significant results achieved by the reporting entity's programs during the past year and compare those results to the entity's mission. According to OMB's February 5, 1992 guidance on "Financial Statements and Performance Measures" this section should include objective, measurable data that disclose the manner in which the entity's program(s) performed. The information in this section is intended to help the reader determine how well the program is performing, including achieving its intended results.

The Supplemental Financial and Management Information section is to support information presented in other parts of the Annual Financial Statement. Appropriate tables and charts and detailed information supporting the program performance discussion in the Overview section should be included in this section.

Program Performance information must be meaningful both to those officials with responsibility for an entity's management and operations and to those officials with oversight responsibility. In summary, program performance information is intended to help program managers and others make decisions about program objectives and practices.

Do the Overview and Supplemental Sections Provide Adequate Program Performance Information?

The HG's Annual Financial Statement Overview section (see Appendix II) does not adequately describe program performance or link program performance to financial results or condition. The Statement does not provide the reader with the basis for assessing how well the program was performing. The statement did not include a Supplemental section.

In order to assess how well a program is performing, one must first identify its objectives and then how best to measure progress toward reaching these objectives.

OMB guidance recognizes that some program objectives may not lend themselves easily to quantifiable measures. Nevertheless, the guidance states that these objectives should also be identified in the Overview. In determining the measures for inclusion in the Overview, OMB guidance suggests that potential users be consulted to determine what they believe are appropriate measures and that both "output" and "outcome" (impact) type measures be provided.

The HG was established to assist in providing long-term financing for low-income shelter and neighborhood infrastructure upgrading programs in developing countries. Besides the objective of financing the construction of housing units and other infrastructure improvements, the program is aimed at supporting policy reforms and other institutional changes which facilitate access to shelter by low-income families on a national basis. U.S. private sector lenders provide the capital for these housing projects based on an A.I.D. guaranty of repayment of principal and interest. In return for the guaranty, A.I.D. charges borrowers certain guaranty fees and requires participating governments sign a guaranty to A.I.D. for the repayment of the loan and outstanding interest paid by A.I.D. on behalf of the borrower. It is intended that these fees meet the cost incurred in connection with the program.

The Overview section provides the reader with good background information on how the program has evolved and major factors effecting it since its inception in 1961. In addition, the section provides some information on program outputs. For example, the statement provides:

- a breakdown of outstanding active loan balances by region by year since fiscal year 1987;

- gross amount of losses incurred due to defaults of loan payments and devaluation of local currencies;

- amounts and construction results for seven expired housing guaranty loans;

- estimation of the total number of shelter solutions that have been built under the program during the 25 year period 1961 through 1988;

- amounts and expected construction results of loans authorized in fiscal year 1991, and amounts and actual results of loans with disbursements in fiscal year 1991; and

- a brief description of current housing guaranty activities in selected countries.

In our opinion, this information, although informative, does not provide the reader with a basis for gauging how well the program is performing. The information basically tells the reader that shelter solutions have resulted from the program and that more shelter solutions are expected. There is no information on the extent that the program has impacted on improvements in the living conditions of developing countries; changing detrimental housing policies and practices; and expanding resources for low-income shelter purposes. Furthermore, because much of the performance information given is cumulative, one cannot relate program performance to the 1991 financial performance.

Why Didn't A.I.D. Provide Better Program Performance Information?

There are several key reasons why the HG's Annual Financial Statement does not provide useful program performance information. First, there was the uncertainty of the level of program performance information that was expected to be presented in the Annual Financial Statement. When the Agency began preparing its Annual Financial Statement in early January, OMB had not issued specific guidance for the Overview and "Supplemental Financial and Management Information" sections. This guidance was not issued until February 5, 1992, only two months before the Annual Financial Statement was to be completed. Agency officials stated they were caught off-guard in regard to the level of performance information expected by OMB.

Second, the Office of Housing and Urban Programs does not have an automated data system to report the type of program performance information envisioned by OMB guidance. HG performance information is primarily maintained in the field on a project by project basis. It appeared that the Regional Housing and Urban Development Offices had developed performance indicators to gauge progress and impact of their housing guaranty projects. Unfortunately, the Washington Housing Office had yet to design a system that could capture worldwide uniform housing performance data. Presently, the Washington Housing Office requests performance data from its field offices whenever information is required, such as for the annual report and the Annual Financial Statement. Although the Housing Office has not developed its own uniform program performance indicators, we were told that it planned to incorporate World Bank housing performance measures in the A.I.D. Housing Investment Guaranty program.

Third, there was little evidence of top A.I.D. management involvement in decisions relating to the content of the Annual Financial Statement and its preparation. OMP Bulletin No. 91-15 requires A.I.D.'s Chief Financial Officer (Associate Administrator for Finance and Administration) to prepare a policy bulletin or guidance memorandum that will guide agency fiscal and management personnel in the preparation of the Annual Financial Statement. The personnel responsible for the preparation of the Annual Financial Statement said they did not receive any written guidance. The limited involvement of top management gave the impression to some that the preparation of the Annual Financial Statement was not a high priority and therefore limited attention was given to its preparation. In addition, there was no attempt made by those responsible for preparing the Statement to contact potential users of the Statement for their recommendations on program performance indicators.

Finally, even if the HG Annual Financial Statement provided appropriate program performance information (i.e., outputs and outcomes), its usefulness in terms of comparing it to the program's financial results would be somewhat diminished by the fact that the HG was not the sole contributor to those outputs and outcomes. For example, the Annual Financial Statement does not encompass training and assistance grants programs, which also contributed to the same outputs and outcomes as the HG program.

What is the Effect of Inadequate Reporting of Program Performance?

Because the HG's Annual Financial Statement did not provide adequate program performance information the Statement had limited value to managers and others interested in the program's administration and impact.

What Can be Done to Improve the Program Performance Presentation in Future Statements?

In our opinion, the following actions would contribute to improving the program performance presentation in the HG's Annual Financial Statement:

Recommendation No. 9: **We recommend that the Associate Administrator for Finance and Administration prepare a policy bulletin or guidance memorandum that will guide Agency fiscal and program personnel in the preparation of future Annual Financial Statements, and establish responsibilities and timetables. This bulletin or memorandum should include the specific data requirements of OMB Bulletin No. 91-15 with which the Program cannot comply and setting goals for when such data will be available.**

Recommendation No. 10: **We recommend that the Assistant Administrator for Private Enterprise, in consultation with Statement users and others involved with developing performance measurements such as the Center for Development Information and Evaluation, reaffirm program goals and objectives and determine appropriate program performance indicators, both "output" and "outcome" (impact) related, that can be linked to financial results and that provide the**

reader with a complete and clear picture of the Housing Guaranty Program's performance during the preceding year.

Recommendation No. 11: We recommend that the Assistant Administrator for Private Enterprise, once appropriate indicators have been identified, in consultation with the Regional Housing and Urban Development Offices, design and implement an automated data information system and procedures to compile, record, and update the data.

Recommendation No. 12: We recommend that the Associate Administrator for Finance and Administration, in consultation with the Assistant Administrator for Private Enterprise, determine whether the Annual Financial Statement should encompass all of the Housing and Urban Development Programs, so that all programs contributing to the outputs and outcomes are presented.

Support Documentation and Accuracy Issues

What are OMB's Support Documentation Requirements?

Program performance information should be reliable. OMB guidance requires agencies to be able to support program performance claims with adequate support documentation and that they retain this information in a manner suitable for review. Agencies should generally collect and maintain performance data regularly throughout the year to support the management process, not just once a year to satisfy annual financial reporting requirements. To the extent possible, performance data should be made available in an automated format such that reentry of the data is minimized. Data should also be obtained for several previous periods, when possible, so that trends and relationships can be available for analysis. The guidance further states that if adequate support documentation is not available, management should describe why it is not available and its plan for meeting the reporting requirements in future Annual Financial Statements.

Is Program Performance Information Reliable and Adequately Supported?

We did not perform sufficient tests to comment fully on the reliability of the performance information. Based on our limited testing, we were able to verify the accuracy of selected authorized amounts and output projections presented in the Overview by tracing the information back to source documents maintained either in the Office of Housing and Urban Programs or in the Regional Housing and Urban Development Offices that we visited. However, we identified that some information on claimed outputs was partially based on estimates and some information was subject to misinterpretation. For example, in the Overview section it is stated that:

> The HG has had a significant impact on the developing world. It is estimated that through the first twenty-five years of the program (1963-1988) more than 650,000 shelter solutions (including sites and services and core units, home improvement loans, urban upgrades and community facilities) have been built for low-income families by funding provided by the program.

This statement was based on information compiled by a contractor for the Housing Office on program accomplishments during the program's first twenty-five years. The contractor created spreadsheet only supports 637,640 shelter solutions. A Housing Official stated that he increased the contractor generated data to reflect accomplishments that were not readily quantifiable. The Statement did not identify housing solution outputs for the subsequent three year period 1989 -1991.

Some information in the Overview section was subject to misinterpretation. For example, amounts shown as disbursed in fiscal year 1991 did not necessarily correspond with the number of housing units reportedly constructed. The Statement indicates that $5.0 million was disbursed under a housing guaranty in Chile which resulted in the construction of 200 units or an average of $25,000 per unit. Documents in the Office of Housing show that as of December 31, 1991, the private Chilean housing cooperatives had disbursed $1.3 million of the available $5.0 million under the housing guaranty borrowing and generated 200 home mortgage loans or an average of $6,565 per loan.

Why Isn't the Program Performance Information Better Supported?

The Regional Housing and Urban Development Offices appear to gather and maintain substantial program performance information, but it is generally on a project by project basis. The Housing Office in Washington does not have an automated data information system to facilitate the tracking and reporting of program accomplishments. Presently, the Office of Housing in Washington must periodically contact field offices for this type of information.

What Is the Effect of Inadequately Supported Program Performance Information?

Program performance information that is not supported by adequate documentation and systems is more likely to be unreliable than information that is supported.

What Can be Done to Improve the Reliability of
Program Performance Information in Future Statements?

In our opinion, the actions shown in Recommendation No. 10 (above) would contribute to improving the reliability of the program performance information in the HG's Annual Financial Statement.

Candidates for Program Performance Measures

Presented below are some potential candidates for program performance measures:

- provide additional data in the Overview on number of Full Time Equivalents (i.e. FS, GS, PSCs and FSNs) at headquarters and each Regional Housing and Urban Development Office,
- identification of significant policy changes achieved by published law and/or regulations,
- number of delinquent loans compared to the total number of loans outstanding,
- comparison of total Full Time Equivalents to the number and dollars of loans outstanding by Regional Housing and Urban Development Office,
- type of shelter solution (e.g. new construction, home improvement, urban upgrade, etc.),
- number of water & sewer connections (infrastructure),
- average cost of shelter solution by country -- this could be broken down further to provide details of down payment and loan amount,
- median income by country/project,
- average income of borrowers by country/project.

The above measures are suggested as ideas only and we have not made a determination as to whether this data is currently available or analyzed their appropriateness in detail.

Did the Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement comply with financial performance reporting guidance contained in OMB Bulletin No. 91-15, "Guidance on Form and Content of FY 1991 Activity, and OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures"?

The HG's Overview section Annual Financial Statement provided limited financial performance information, but did not fully comply with the OMB financial performance reporting guidance in that minimal financial performance measures/indicators were presented. The applicable OMB financial performance reporting guidance specifies the types of financial performance measures and indicators envisioned. HG's Annual Financial Statement's presentation of financial performance information was limited. The lack of comprehensive financial performance reporting information diminished the Statement's usefulness.

> Recommendation No. 13: **We recommend that the Associate Administrator for Finance and Administration develop and include additional financial performance and management indicators in the fiscal year 1992 Annual Financial Statement.**

The HG's Overview contained a discussion of the program's viability as a self-sustaining entity until the mid '80s, followed by a discussion of necessary appropriations and Treasury borrowing since then. The Overview presented a breakdown of the effect of the cost of borrowing on cash available for fiscal year 1991. It also presented a table showing loans, fees, and interest receivables for the period 1987 through 1991. However, the fiscal years 1987 through 1989 shown on the table apparently did not include the effects of a prior period adjustment in fiscal year 1990, which would significantly increase the allowance for doubtful accounts for those years. Additionally, the Overview also discusses recent improvements in the accounting and financial information systems and internal controls.

OMB Bulletin No. 91-15, dated September 10, 1991, indicates that "the Overview should include a narrative discussion and analysis of the financial condition of the reporting entity. This discussion should present information based on the results of an analytical review of relevant financial and performance data on the programs, activities, and funds that make up the reporting entity" and that "in preparing the Overview of the Reporting Entity, agencies should refer to the guidance contained in the March 1991 United States General Accounting Office (GAO) study titled "FINANCIAL REPORTING - Framework for Analyzing Federal Agency Financial

Statements". Additionally, OMB's February 5, 1992 guidance reiterates the suggested utilization of the GAO study in presenting the financial performance and indicates that "the Overview of the Reporting Entity should also provide a quick and easy understanding of how the entity is faring financially and, to the extent possible, the future financial implication of the entity's current condition".

The HG's Annual Financial Statement did include some financial information, but did not fully comply with the OMB financial performance reporting guidance in that the presentation of financial performance measures/indicators was limited.

The HG Annual Financial Statement presentation of financial performance information was limited for two reasons. First, the financial management system did not currently accumulate appropriate information to facilitate presentation of financial performance information. Second, OMB did not issue specific guidance on the Overview and Supplemental Financial and Management Information sections until February 5, 1992, only about two months before the Annual Financial Statement was due to OMB.

The lack of additional financial performance information in the form of indicators reduced the usefulness of the Annual Financial Statement to the user. The Statement user would not necessarily be able to get a quick and easy understanding of how the entity is faring financially.

Fiscal year 1991 was the first year the Housing and Other Credit Guaranty Programs was required to develop financial performance information in an Annual Financial Statement. Management recognizes the need to develop financial performance measures/indicators in future years that will provide a more complete presentation of the Program's financial results.

To supplement the financial performance information presented in the Overview, we have applied some of the analytical techniques and measured some of the attributes suggested in the General Accounting Office study mentioned above. Our purpose for doing this was to provide some additional analyses which, in our opinion, would be beneficial to Statement users, including Congress, the A.I.D. Administrator, and other decision makers. Financial performance information reflects accountability for Government programs and can be useful in making decisions and determining the allocation of Government resources to public policy alternatives.

Since the HG is a revolving fund we have focused our analysis on operating results, financial obligations, and financial conditions. These attributes are important in assessing the HG's current cost, ability to meet obligations without additional funding and their future demand for Federal resources. Our supplemental financial analyses follow.

Operating Costs

Operating Costs	Fiscal Year 1989 (000)	1990 (000)	1991 (000)	Avg. Change
Total Costs And Expenses (1)	$ 80,950	$ 109,544	$ 66,099	$ (7,426)
Fees and Interest Revenues (2)	$ 24,971	$ 27,354	$ 32,193	$ 3,611
Net Operating Cost (1)-(2)	$ 55,979	$ 82,190	$ 33,906	$(11,037)
Percentage Change	-	+ 46.8%	-58.8%	- 6.0%

The net operating cost (computed above) measures the cost of operating the program. The costs of operating (or net loss of) the HG were $56 million for fiscal year 1989, $82.2 million in fiscal year 1990, and $33.9 million for fiscal year 1991. The net operating cost decreased between fiscal year 1990 and fiscal year 1991 because a significant portion of high risk debt came due during the year which caused the reserve account to actually decrease by $3.2 million, thus creating a negative balance of in the provision (expense) account of $1.9 million. In a revolving fund such as the HG, a positive operating cost amount indicates that the fund cannot sustain itself and that additional funding is necessary. Thus, the higher the cumulative operating cost over time, the weaker a fund's financial condition.

Two of the most significant items of cost are the provisions for uncollectible receivables (bad debts) and interest on Treasury borrowing. These expenses for the period 1989 through 1991 are as follows:

Description	Fiscal Year 1989 (000)	1990 (000)	1991 (000)	Avg. Change
Prov. for Uncollectible Claims	$ 25,230	$ 36,913	$ 51,101	$ 12,936
% Change	-	+46.3 %	+38.4 %	+42.4 %
Prov. for Losses on Guaranties	$ 45,234	$ 60,667	$ (1,881)	$(23,558)
% Change	-	+34.1 %	-103.1%	-34.5%
Interest Expense	$ 4,447	$ 5,856	$ 9,344	$ 2,449
% Change	-	+31.7 %	+59.6 %	+45.7 %

Financial Obligations

The most significant liabilities of the HG are the borrowings from the U.S. Treasury and the reserve for guaranty losses. These costs for the period 1989 through 1991 are as follows:

		Fiscal Year		
Description	1989 (000)	1990 (000)	1991 (000)	Avg. Change
Borrowing from U.S. Treasury	$ 58,000	$ 82,000	$ 130,000	$ 36,000
Percentage Change	-	+41.4 %	58.6 %	50.0 %
Reserve for Guaranty Losses	$ 632,188	$ 685,625	$ 682,418	25,115
Percentage Change	-	+8.5%	-.8%	+3.9%

These liabilities are generally increasing. The HG obtained additional funding by borrowing from Treasury to meet shortfalls.

As of September 30, 1991 the HG has borrowed $130,000,000 from the U.S. Treasury to maintain operations. The interest on this level of borrowing is about one million dollars per month. As a result of the 1990 financial statement audit (Report No. 0-000-92-01-N), we recommended that A.I.D. management devise a payment plan to liquidate this mounting debt. As of March 1992, management indicated that an Agency committee, composed of representatives from FA/FM/LM, FA/B and PRE, is developing a plan to repay the borrowing. Under the Credit Reform Act of 1990 (PL 101-508), which was implemented as of October 1, 1991, repayment of the pre-fiscal year 1992 Treasury debt will be funded through a permanent indefinite appropriation.

The financial information relating to a program's financial obligations is important because financial obligations represent a future demand for resources, thus a future cost to taxpayers.

Financial Position

The purpose in analyzing the financial condition of any program is to determine whether the program has adequate resources to carry out its operations and satisfy its obligations as they become due.

Following is an analysis of the HG's cash flow. For our purposes, we have limited this analysis to showing the net cash before financing and after considering financial borrowing. In order to project future cash needs, a detailed analysis of cash sources as well as future outflows must be performed. Our analysis is as follows:

Description	Fiscal Year 1989 (000)	Fiscal Year 1990 (000)	Fiscal Year 1991 (000)	Avg. Change
Net Increase (Decrease) in Cash Before Financing Activity	$ (10,818)	$ (37,501)	$ (44,485)	$(16,834)
Percentage Change	-		-246.6 %	-18.6 %-
132.6 %				
Treasury Borrowing	$ 13,000	$ 24,000	$ 48,000	$ 17,500
Percentage Change	-	+84.7 %	+100.0 %	+92.4 %
Net Increase(Decrease) in Cash	$ 2,182	$ (13,501)	$ 3,515	$ 667
Percentage Change	-	+518.7 %	-74.0 %	222.4%

Another indicator that can be used to measure a program's solvency is the debt-to-asset ratio, which indicates the ability of an entity to meet its obligations with all its assets. A comparison of this ratio over time is a gauge of the financial soundness of a program. This ratio computed for the HG is as follows:

Description	Fiscal Year 1989 (000)	Fiscal Year 1990 (000)	Fiscal Year 1991 (000)	Avg. Change
Total Liabilities (1) (1)	$ 697,566	$ 773,494	$ 823,723	$ 61,623
Total Assets (2)	$ 44,439	$ 38,177	$ 54,500	$ 5,307
Debt-to-Asset Ratio(1)/(2)	15.7/1	20.2/1	15.1/1	-

As shown above, assets increased at an average of $5.3 million while liabilities increased an average of $61.6 million per year. Thus, the ratio indicates that the program is in financial difficulty and will need additional appropriations, should liabilities continue to exceed assets.

Other Comments

Financial condition is a multi-faceted concept. The use of a single measure alone will not reveal the financial condition of an entity. However, providing several indicators will help analysts and Statement users form conclusions about the financial condition of an entity. Additionally, some of the above indicators could be refined further by adjusting to "constant dollars" (i.e. adjusting for inflation), where applicable.

Candidates for Financial Performance Measures

Presented below are some potential candidates for financial and financial management performance measures:

- percent of bad debts to total loans outstanding
- payments made and total payments due during the year presented by country
- number of delinquent loans compared to the total number of loans outstanding
- consider providing receivable information by country
- consider the use of the measures and indicators discussed in OMB's February 5, 1992 guidance
- measurement of the percentage of claims collected and average time to collect
- measurement of the amount of time between when a prepayment is received by Financial Management/Loan Management (FM/LM) and when it is remitted to the lender

The above measures are suggested as ideas only and we have not made a determination as to whether this data is currently available or analyzed their appropriateness in detail.

SCOPE AND METHODOLOGY

Scope

Pursuant to the provisions of the Chief Financial Officer's (CFOs) Act of 1990, the Office of the Inspector General is required to conduct audits of the Housing and Other Credit Guaranty Programs' Annual Financial Statement beginning with the fiscal year 1991 Statement. To fulfill our responsibilities under the Act, the Inspector General/Financial Audits contracted with the certified public accounting firm of Price Waterhouse to perform, under our general oversight, and in accordance with generally accepted auditing standards, Government Auditing Standards, and the requirements of OMB Bulletin No. 91-14, "Audit Requirements for Federal Financial Statements", an audit of the 1991 financial statements. The field work was performed from March 1992 through July 1992 primarily at A.I.D. Headquarters in Washington, D.C.. Field Testing was performed at the Regional Housing and Urban Development Offices and A.I.D. Missions in Quito, Ecuador and Kingston, Jamaica.

In addition, we performed certain audit procedures to determine whether the Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement complied with financial and program performance reporting guidance contained in Office of Management and Budget (OMB) Bulletin No. 91-15, "Guidance on Form and Content on FY 1991 Activity", and OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures". Our objective was not to provide an opinion on overall compliance with the CFOs Act, but rather to determine the extent to which applicable OMB guidance was followed in preparing the Annual Financial Statement, and to highlight areas where improvement was desirable and would be of benefit to financial statement users. In answering these audit objectives, we relied on Price Waterhouse's assessments of internal controls and compliance with laws and regulations. The audit procedures were limited to assessing the adequacy of financial and program performance information presented in the Housing and Other Credit Guaranty Program's Annual Financial Statement for fiscal year 1991. Our audit tests were sufficient to provide reasonable assurance that our answers to the audit objectives were valid. The field work was performed during May through July 1992 primarily at A.I.D. Headquarters in Washington, D.C.

Limited work was also performed at the Regional Housing and Urban Development Offices in Quito, Ecuador and Kingston, Jamaica.

Methodology

The methodology for each audit objective was as follows:

Audit Objectives One through Three

The first three audit objectives were:

- Did the Housing and Other Credit Guaranty Programs' fiscal year 1991 financial statements and the notes to the financial statements present fairly in all material respects the financial position, operations and government equity (deficiency), results of operations, cash flows, and reconciliation to budget in accordance with the applicable accounting standards?

- Did the Housing and Other Credit Guaranty Programs have an adequate internal control structure?

- Did the Housing and Other Credit Guaranty Programs comply with laws and regulations that could have a direct and material effect on the financial statements and certain other laws and regulations designated by OMB and A.I.D.?

In order to achieve these objectives we contracted with the certified public accounting firm of Price Waterhouse to audit, under our general oversight, the fiscal year 1991 financial statements of the Housing and Other Credit Guaranty Programs in accordance with generally accepted auditing standards, Government Auditing Standards, and Office of Management and Budget (OMB) Bulletin 91-14, "Audit Requirements for Federal Financial Statements". We approved Price Waterhouse's scope of work, monitored audit progress, accompanied them on some of the site visits, and performed other procedures we considered necessary.

Audit Objective Four

The fourth audit objective was to determine whether the Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement complied with program performance reporting guidance contained in OMB Bulletin No. 91-15, "Guidance on Form and Content on FY 1991 Activity", and OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures"?

To accomplish the objective, we reviewed the CFOs Act, implementing OMB guidance, and other pertinent materials; analyzed the Statement and other applicable program reports and documents; and interviewed A.I.D. officials responsible for the actual preparation of the Statement. We also discussed with officials in A.I.D's Center for Development Information and Evaluation Agency efforts to develop program performance indicators. We did not perform sufficient tests to determine the reliability of performance information presented in the Statement.

In addition, we selected key program performance information presented in the statement and assessed the adequacy of supporting documentation. We did not perform "end-use" checks to verify the accuracy of reported accomplishments, however, we compared the selected information with that reported in the program's annual report to the Congress to see if the program office was consistent in its reporting of performance information.

Audit Objective Five

The fifth audit objective was to determine whether the Housing and Other Credit Guaranty Programs' fiscal year 1991 Annual Financial Statement complied with financial performance reporting guidance contained in OMB Bulletin No. 91-15, "Guidance on Form and Content on FY 1991 Activity", and OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures"?

To accomplish the objective we reviewed the Annual Financial Statement, the CFOs Act, implementing OMB guidance, and other pertinent materials. We also held discussions with those who prepared the Annual Financial Statement.

To supplement the financial performance information presented in the Overview section of the Annual Financial Statement we applied some of the analytical techniques discussed in OMB Bulletin No. 91-15, OMB's February 5, 1992 guidance, "Financial Statements and Performance Measures", and the March 1991 United States General Accounting Office (GAO) study titled "FINANCIAL REPORTING - Framework for Analyzing Federal Agency Financial Statements". Our supplemental financial analysis was based primarily on the financial statement for the fiscal years 1989 through 1991. The fiscal year 1989 financial statement is unaudited, and opinions were not expressed on the fiscal year 1990 and 1991 statements. Thus, we are unable to attest to the accuracy of this financial data. Our supplemental financial analysis of the HG focused on the following financial attributes: (1) operating cost, (2) financial obligations, and (3) financial position.

AGENCY FOR INTERNATIONAL DEVELOPMENT'S HOUSING AND OTHER CREDIT GUARANTY PROGRAMS

September 30, 1991

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HOUSING AND OTHER CREDIT GUARANTY PROGRAMS

PROGRAM OVERVIEW

The Agency for International Development (A.I.D.) administers the Housing Guaranty Program and the Agricultural and Productive Credit and Self-Help Community Development Program. These programs were established by Congress to stimulate the participation of the U.S. private sector in the economic development of less-developed countries. These programs operate as revolving funds, subject to the appropriation process.

The Agricultural and Productive Credit and Self-Help Community Development Program (Productive Credit Guaranty Program) was instituted with the addition of Section 222A to the Foreign Assistance Act of 1961 in 1974. A $3 million revolving fund was instituted by the enabling legislation for use on the Productive Credit Guaranty Program. The Agency for International Development was authorized through September 30, 1988 under the Productive Credit Guaranty Program to issue full faith and credit guaranties of the U.S. Government to private lending institutions, cooperatives, and nonprofit development organizations in five Latin American countries.

The Housing Guaranty Program was established by Title III, Sections 221, 222 and 238c of the Foreign Assistance Act of 1961, as amended, to assist in providing long-term financing for low-income shelter and neighborhood infrastructure upgrading programs in developing countries. U.S. private sector lenders provide financing at commercial rates for projects undertaken by eligible resident borrowers. The repayment of the principal and interest be guaranteed through A.I.D. by the full faith and credit of the U.S. Government. This guaranty promotes U.S. lender participation in providing financing at lower interest rates. In return, A.I.D. charges the borrowers guaranty fees and also requires that governments of the borrowers sign a guaranty to A.I.D. for the repayment of the loan and outstanding interest paid by A.I.D. on behalf of the borrower. The fees charged to borrowers are comprised of an annual fee of one-half of one percent of the unpaid principal balance of the guaranteed loan, and an initial charge of one percent of loan amount. All fees together with resulting earnings are held in a revolving fund account maintained by the Treasury of the United States. The enabling legislation intended for the fees to meet cost incurred in connection with the program.
The Housing Guaranty Program functions as a hard loan window much like the International Bank for Reconstruction and Development (IBRD). The majority of IBRD development projects are funded on terms comparable to those of the Housing Guaranty Program and to the same set of clients.

The total principal amount of guaranties issued and outstanding under this title cannot exceed $2.558 million at any one time. Generally, the face value of guaranties issued with respect to housing in any country does not exceed $25 million in any fiscal year, and

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the average face value of guaranties issued in any fiscal year does not exceed $15 million.

The program data reported in the following overview and analysis does not fully represent program results nor is the data presented all taken from systems designed to report evaluative results. Systems to record, compile and analyze data on program performance are not currently in place. Therefore, the requirement that the Chief Financial Officer develop and maintain an integrated agency accounting and financial management system, including financial reporting and internal controls, which provides for the systematic measurement of performance, cannot be currently met.

The chart below provides a breakdown of loans authorized by region.

(in Thousands)					
Loans Authorized - Active Loans					
Region	**FY1987**	**FY1988**	**FY1989**	**FY1990**	**FY1991**
Africa	274,431	250,431	253,239	253,239	212,206
Asia	324,753	384,960	448,710	513,750	575,400
Latin America	971,384	983,241	978,243	952,256	946,658
Near East	536,993	561,993	586,993	591,500	1,002,000
Inter-Regional	54,594	39,329	30,067	30,067	65,067
TOTAL	$2,162,155	$2,219,954	$2,297,252	$2,340,812	$2,801,331
Less Payments	216,290	212,339	243,026	252,652	248,051
Total Authorized and Outstanding	$1,945,865	$2,007,615	$2,054,226	$2,088,160	$2,553,280

The Office of Housing and Urban Programs

The Office of Housing and Urban Programs, in the Bureau for Private Enterprise, helps developing countries respond to their shelter and urbanization needs and administers the A.I.D. Housing Guaranty Program. The Office develops strategies for program planning, management and capital investment to benefit low-income urban families. Regional Housing and Urban Development Offices, located in all of the developing regions of the world, advise A.I.D. Missions and co-manage with them most of A.I.D.'s capital and technical assistance programs for housing and urban development. The Office works closely with local officials to promote policies that improve municipal and environmental management and that expand affordable shelter, water and sanitation services, access to housing finance, land tenure, decentralization, training of local officials, and partnerships with the private sector. These assistance programs follow A.I.D.'s general emphasis on economic growth, reliance on market forces and individual initiative, and democratization principles.

Claims History and Credit Reform

For the past year Housing Guaranty Program officials have participated in a Government-wide effort to prepare for implementing the Credit Reform Act of 1990. Under this law, Federal credit programs, beginning in Fiscal Year 1992, will have appropriations for cost of the credit transaction up front rather than at the time losses occur. The important management implication for the Housing Guaranty program is that funds will be appropriated upon issuance of new guaranties sufficient to cover the estimated costs over the life of the loan. To date, these costs have not been appropriated in advance of the credit transactions. Under the new requirements, the Housing Guaranty Program, in Fiscal Years 1992 and 1993, will budget a subsidy of about 15 cents for every dollar guarantied.

The attached Statement of Financial Position and the discussion which follows summarizes actual claims experience to date. These claims, totalling approximately $266 million, fall into three categories:

1. Losses due to greater than anticipated devaluation of the local currency in relation to the U.S. dollar and not covered by host country guaranties. This is true of most projects authorized prior to 1968 and resulted in losses of approximately $39 million.

2. Defaults of payments by the borrower that have been rescheduled of approximately $133 million.

3. Defaults of payments that have not been rescheduled totalling $94 million.

With the worsening of the debt crisis in the mid 80s, management began to take steps to provide guaranties to more creditworthy recipients. In addition, in 1988 Housing Guaranty debt came under the sanction authority of Section 620(q) of thc Foreign Assistance Act of 1964, as amended, and Section 518 of the Fiscal Year 1985 Foreign Assistance Appropriation Act. These sanctions provide for the discontinuance of assistance when debt reaches either 6 months or 1 year in age. The policy of the U.S. Government to reschedule debt mitigates the effect of these sanctions on collections.

In addition to taking responsible action to reduce losses, a loan loss reserve was developed to provide a reasonable estimate of future losses. These potential losses will be re-estimated annually and adjusted as appropriate. Hopefully, the efforts of the international community to assist in development will indeed result in more positive performance by some of those nations which currently have significant amounts outstanding.

It must be borne in mind, however, that the Housing Guaranty program is not an international bank portfolio. Rather it is one piece of development assistance that does play a role in furthering A.I.D.'s development goals and subsequently U.S. foreign policy.

PROGRAM PERFORMANCE

Program Trends and Current Program Description

The Housing Guaranty Program has gone through a significant change over the last two decades. The early programs were similar to other U.S. Government housing loan programs; whereby the borrower was the homeowner and the guaranty was given on behalf of the homeowner to the lender (i.e., the U.S. investor). These financial arrangements resulted in some losses to A.I.D. because the value of foreign currencies (the homeowner's currency) exceeded estimates of devaluation. Total losses from these projects are projected at $38.5 million (over the life of the program).

In FY1991 several of these types of housing arrangements expired. The results of these borrowings are:

Loan Number	Amount	Houses/Apts. Completed	Losses Incurred
517-HG-005 A01	$ 2,118,036	325	$ 842,957
504-HG-001 A01	1,185,935	400	-0-
525-HG-005 A01	962,834	323	176,469
527-HG-006 A01	604,421	132	566,743
529-HG-006 A01	5,912,076	815	31,637
529-HG-008 A01	2,890,029	570	991,752
529-HG-012 A01	20,000,000	4166	-0-
TOTALS	$33,673,331	6731	$2,610,046

After the foreign exchange problem began to occur, there was a change in the guaranty that required the host government to provide A.I.D. with a guaranty to guard against currency losses.

The earlier emphasis on housing construction, detailed in the expired agreements, has also changed over time. Housing Program guaranties may be issued for neighborhood upgrading, improved utilities services or other infrastructure improvements. Virtually all guaranties are for the support of policy reforms and other institutional changes which facilitate access to shelter by low-income families on a national basis. These more ambitious goals have made the program more difficult to evaluate and measure the full results of the financial arrangements.

The Housing Guaranty Program has had a significant impact on the developing world. It is estimated that through the first twenty-five years of the program (1963-1988) more than 650,000 shelter solutions (including sites and services and core units, home improvement loans, urban upgrades and community facilities) have been built for low-income families by funding provided by the program. This data was gathered in preparing the twenth-fifth year history of the program. FY1991 authorizations are projected to finance some 70,000 low-income shelter solutions. The program legislation requires that the shelter and related infrastructure financed be suitable for families with incomes below the median. Of much greater importance has been the permanent impact on host country policies and institutions, including creation of more innovative methods of construction, improved community infrastructure and improved financing techniques for the benefit of low-income families.

Listed below are two charts reflecting financing provided in FY1991 and the results or planned results of these financial arrangements.

Loan Guaranty Authorizations in FY1991

Authorization	Country	Amount	Estimated Number of Units to be Constructed
271-HG-008	Israel	$400,000,000	12,300
513-HG-010	Chile	40,000,000	2,750
608-HG-003	Morocco	5,500,000	1,300
497-HG-003	Indonesia	25,000,000	6,500
150-HG-009	Portugal	5,000,000	150
386-HG-011 386-HG-012	India	6,250,000 5,400,000	8,185
999-HG-001	Eastern Europe	35,000,000	800
492-HG-002	Philippines	25,000,000	38,200

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Loan Guaranty Disbursements in FY1991

Loan Number	Country	Amount	Number of Units Constructed
271-HG-008 A01	Israel	$400,000,000	12,300
513-HG-009 A01	Chile	5,000,000	200
150-HG-007 A01	Portugal	25,000,000	760
386-HG-008 A01	India	25,000,000	12,114
497-HG-004 A01	Indonesia	25,000,000	6,424

Country Program Descriptions

India

The Housing Finance System Program provides resources to support development of an institutional and regulatory framework for a network of private housing finance institutions throughout the country. Current efforts are focused on strengthening the supervisory role of the National Housing Bank as the apex institution in the housing finance system.

Indonesia

In 1988 USAID/Jakarta established a $100 million Housing Guaranty Program (497-HG-001) to address major problems facing the municipal finance system, including local resource mobilization, infrastructure cost recovery, and public-private partnerships in urban service provision. In FY1991 the fourth tranche of $25 million was authorized under the policy-based HG Program.

Philippines

This loan was an element in the Military Bases negotiations. The Decentralization of Shelter and Urban Services (DSUD) project was approved in 1990 with $50 million in Housing Guaranty resources (492-HG-001) and a $4 million grant (492-0388). The DSUD Program Agreement, signed in 1991, specifies policy actions designed to: (a) develop a sustainable system of city government finance; (b) improve the delivery of urban services and infrastructure; and (c) improve access to urban services by low income households. In FY1991 the second tranche of $25 million was authorized.

Morocco

The purpose of this $5.5 million loan (608-HG-003) is to support the development of a self-sustaining system of financing for the annual production of 4,000 fully-serviced low-income plots. The National Shelter Upgrading Agency, (ANHI), is making land available to the private sector for the production of shelter affordable to low-income families.

Portugal

As an element in base-rights negotiations, a $55 million Housing Guaranty Program was designed to increase private sector production of low income housing. The Program has two elements: 1) broadening the range of financing available to local developers for investments in land, infrastructure, community facilities, upgrading clandestine neighborhoods and deteriorating inner cities, and 2) increasing the supply of construction and mortgage financing available for low-income housing. A $5 million loan was authorized in FY1991 as the third phase of the program.

Chile

This policy-based $40 million sector program is designed to re-involve the private sector in low-income mortgage financing, encourage the revitalization of downtown Santiago and support small-scale environmental initiatives.

Eastern Europe

A $35 million Housing Guaranty program for Eastern Europe was authorized in August 1991. This Program will promote private sector housing demonstration projects in the region and encourage the development of the housing industries of private Eastern European entrepreneurs.

Israel

In March 1991, A.I.D. authorized a $400 million Housing Guaranty for Israel to finance the purchase of new and existing housing by Soviet immigrants arriving in Israel. By the end of May, the total amount had been disbursed to cover eligible mortgages.

The FY1991 guaranty authorizations included three Congressionally-mandated programs: Israel, Eastern Europe and Chile. The guaranty to Israel was unique in that it is more than 20 times the amount of the average guaranty and contracting occurred within the same fiscal year. The size of the financing resulted in A.I.D. allowing several unique features in the Israeli borrowing. A.I.D.'s fiscal agent was bypassed and fees were reduced. The borrowing was packaged so that the most favorable market would accrue to the borrower. This would also result in a reduced exposure for the Housing Guaranty

Program. The Eastern Europe guaranty is also somewhat unique in that the program is designed as a regional program addressing housing concerns in Poland, the Czech and Slovak republics and in Hungary. The loan to Chile, which does not involve Government of Chile participation, incorporates an innovative currency swap arrangement which serves to insulate the private sector borrower from currency devaluation.

FINANCIAL PERFORMANCE

Recent Financial Management Improvements

There was a non-federal audit of the FY1990 financial statements. The purpose of that audit, requested concurrently by the Office of Housing and Urban Programs and the Office of Financial Management, was to determine with the assistance of an independent accounting firm, a more reasonable estimate of potential losses from Housing Credit activity. The audit accomplished that purpose, but also revealed a number of financial management material weaknesses. Although the audit was not completed until late in FY1991, a number of major steps have been taken to correct the weaknesses.

First, an automated system to perform the servicing part of the guaranty accounting was in process during the time of the audit. That system is now functioning even as it undergoes additional changes and refinements. Second, the manual general ledger system has been dropped as of September 30, 1991 and a somewhat automated Lotus system will be used during the current fiscal year. While it would be preferable to maintain normal systems as new systems are being developed and tested, staff are not able to do both.

Final reports are expected from a contractor that will provide the means or options available:

- to improve estimates for credit reserves
- to monitor accounting operations that affect the program but are not managed by the Loan Management Division (both in Washington and overseas)
- to establish and to maintain auditable property records to fix other material weaknesses in accounting operations.

The results of this improvement program should be in place before the current audit is completed.

Financial Performance

A.I.D. managed the Housing Guaranty Program as a self-sustaining activity from its inception until the 1980s. Initial reserves and fee income were sufficient to cover operating expenses and losses including the first major financial problem; losses on foreign exchange that would not allow home purchasers to payoff mortgages in dollars. However, the international debt crisis had significant financial impact on the program beginning about 1985 and required a change in approach, e.g., seeking appropriations or borrowing authority.

To sustain the program an appropriation of $40 million was received in 1986. At about this same time a proposal to refinance rescheduling by offering a guaranty to the lender was tried. While this did infuse about $25 million in cash into the program (1987-1988) there was also an increase in poor performing debt as well.

To maintain the program on a business-like basis, borrowing authority was sought from Congress and approved in FY1986. The first borrowing occurred in FY1987. In FY1991, $48 million was borrowed to bring the total borrowed to $130 million. The effect of the cost of borrowing on cash available can be illustrated by an analysis of 1991 cash requirements.

Entity	Amount in Millions	Percentage
Borrowing	$48.0	N/A
Interest	9.3	19.4
Other Operating Expenses	7.4	15.4
Other Cash Requirements (claim payments less income and recoveries)	31.3	65.2

The most significant program cost is the cost of paying claims and maintaining rescheduled debt and uncollected income. Total claims paid in FY1991 were (in thousands) $64,889 and recoveries amounted to $18,058 with a net of $46,831. In addition, uncollected revenue increased by $7,254 to a total of $51,949.

The second most significant cost to the program is the interest on funds borrowed. Interest expense will equal about 25% ($11 million) of the total cost of the pre-1992 portfolio in FY1992. A staff committee is now studying this problem to develop a plan to repay these loans.

As shown below the amounts of loans, fees and interest receivables from foreign countries has increased steadily each year from $111.6 million as of September 30, 1987 to $281.9 million as of September 30, 1991 (see next page):

(In Thousands)					
	FY1987	FY1988	FY1989	FY1990	FY1991
Fees Receivable	19,266	28,268	36,891	44,695	51,949
Loans Receivable	92,348	118,608	139,720	170,391	227,387
TOTAL	0.00	146,876	176,611	215,086	279,336
Less: Allowance for Doubtful Accounts	2,000	5,000	5,000	159,586	235,100
Total Receivables	109,614	141,876	171,611	55,500	44,236

In addition to current program cash losses, by the end of FY1991 a reserve was established for $682,418 (in thousands) to cover outstanding guaranties. While it may be arguable that, indeed, sovereign debt will be collected, the potential for loss must be and has been recognized in the financial statements. Without identifying losses associated with individual transactions and deducting the Israeli transaction from FY1991 authorizations, anticipated losses are approximately 33%, consistent with the total portfolio loan loss ratio.

As mentioned above, beginning in FY1992 the program will change significantly. Appropriations will be made to cover the claim losses and pay interest on the borrowing for the pre-FY1992 guaranty operations. There will be a new appropriation account to pay the cost, up front, for guaranties issued and to pay operating expenses of the program.

AGENCY FOR INTERNATIONAL DEVELOPMENT
HOUSING AND OTHER CREDIT GUARANTY PROGRAMS
FINANCIAL STATEMENTS
FOR THE YEARS ENDED
SEPTEMBER 30, 1991 AND 1990
AND
REPORTS OF PRICE WATERHOUSE

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Office of Government Services
1801 K Street, N.W.
Washington, DC 20006
Telephone 202 296 0800

Price Waterhouse

To the Administrator
and the Inspector General
of the Agency for International Development

Report of Independent Accountants

We were engaged to audit the financial statements of the Housing and Other Credit Guaranty Programs of the Agency for International Development (A.I.D.) as of and for the years ended September 30, 1991 and 1990. These financial statements are the responsibility of A.I.D.'s management.

A lack of accounting records and automated systems has resulted in insufficient evidence to support various transactions and account balances to permit the application of adequate auditing procedures. The account balances affected, and the nature of the insufficient records and systems include: (1) claims receivable and outstanding guaranties are not adequately supported by accounting records or automated systems which identify the lenders and host country administrators to which they relate; (2) weaknesses in the general accounting systems and in the controls surrounding them could cause errors that would affect the Housing and Other Credit Guaranty Programs' financial statements; and (3) A.I.D. has not analyzed its unapplied disbursements account to determine the effect, if any, on the accounts of the Housing and Other Credit Guaranty Programs.

Because we were not able to apply alternative auditing procedures to satisfy ourselves regarding cash, accounts payable, accrued expenses and other liabilities, and claims receivable, and because automated systems were inadequate to facilitate audit testing, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the aforementioned financial statements.

We have reviewed the financial information presented in management's "Program Overview" of the Housing and Other Credit Guaranty Programs. This information has been presented by management for the purpose of additional analysis. Such information has not been audited by us and, accordingly, we do not express an opinion on it. Our review of this information is addressed, however, in the ninth paragraph of our accompanying report on compliance with laws and regulations.

Price Waterhouse

Washington, D.C.
July 17, 1992

AGENCY FOR INTERNATIONAL DEVELOPMENT
HOUSING AND OTHER CREDIT GUARANTY PROGRAMS
STATEMENTS OF FINANCIAL POSITION
SEPTEMBER 30, 1991 AND 1990

APPENDIX IV-1

(Dollars in Thousands)

	SEPTEMBER 30, 1991	SEPTEMBER 30, 1990 (RECLASSIFIED)
ASSETS:		
Fund Balance with Treasury (Note 4)	$9,250	$1,776
Central Reserve Bank Account (Note 5)	266	561
Investment in U.S. Government Obligations (Note 6)	0	3,959
Fees Receivable, net of allowance for doubtful amounts (Note 7)	7,441	6,733
Claims Receivable, net of allowance for doubtful amounts (Note 8)	8,858	14,836
Rescheduled Claims Receivable, net of allowance for doubtful amounts (Note 9)	27,936	9,514
Furniture and Equipment, net of depreciation (Notes 2 and 10)	679	738
Other Assets	70	60
Total Assets	$54,500	$38,177
LIABILITIES AND GOVERNMENT DEFICIENCY:		
Accounts Payable, Accrued Expenses and Other Liabilities	$3,265	$2,633
Unamortized Origination Fees (Note 2)	2,906	0
Interest Payable	5,134	3,236
Borrowings from U.S. Treasury (Note 11)	130,000	82,000
Reserve for Guaranty Losses (Notes 2 and 12)	682,418	685,625
Total Liabilities	823,723	773,494
Government Deficiency:		
Unrestricted (Note 13)	(769,223)	(739,354)
Restricted - Productive Credit Guaranty Program (Note 13)	0	4,037
Total Government Deficiency	(769,223)	(735,317)
Commitments and Contingencies (Note 16)		
Total Liabilities and Government Deficiency	$54,500	$38,177

The accompanying notes are an integral part of the financial statements.

AGENCY FOR INTERNATIONAL DEVELOPMENT
HOUSING AND OTHER CREDIT GUARANTY PROGRAMS
STATEMENTS OF OPERATIONS AND GOVERNMENT EQUITY (DEFICIENCY)
FOR THE YEARS ENDED SEPTEMBER 30, 1991 AND 1990

(Dollars in Thousands)

	YEAR ENDED SEPTEMBER 30, 1991	1990 (RECLASSIFIED)
REVENUES:		
Fees	$31,945	$27,053
Interest on Investment in U.S. Government Obligations (Note 6)	248	301
Total Revenues	32,193	27,354
EXPENSES:		
Provisions for Uncollectible Claims and Fees Receivable	51,101	36,913
Provision (Credit) for Losses on Guaranties (Note 12)	(1,881)	60,667
Depreciation	239	185
Salary and Administrative Expenses	7,296	5,923
Interest	9,344	5,856
Total Expenses	66,099	109,544
Deficiency of Revenues over Expenses	($33,906)	($82,190)
GOVERNMENT EQUITY (DEFICIENCY):		
Appropriated Capital	$87,043	$87,043
Accumulated Equity (Deficiency), beginning of year	(822,360)	34,104
Current year deficiency	(33,906)	($82,190)
Prior period adjustments (Note 15)	0	(774,274)
Accumulated Equity Deficiency, end of year	(856,266)	(822,360)
Government Deficiency	($769,223)	($735,317)
Unrestricted-Housing Guaranty Program	(769,223)	(739,354)
Restricted-Productive Credit Guaranty Program (Note 13)	0	4,037
	($769,223)	($735,317)

The accompanying notes are an integral part of the financial statements.

AGENCY FOR INTERNATIONAL DEVELOPMENT
HOUSING AND OTHER CREDIT GUARANTY PROGRAMS
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 1991 AND 1990

APPENDIX IV-3

(Dollars in Thousands)

	YEAR ENDED SEPTEMBER 30, 1991	1990 (RECLASSIFIED)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Deficiency of Revenues over Expenses	($33,906)	($82,190)
Adjustments to Reconcile Deficiency to Net Cash Used by Operating Activities:		
Provision for Uncollectible Claims and Fees Receivable	51,101	36,913
Provision (Credit) for Losses on Guaranties	(1,881)	60,667
Depreciation	239	185
Claim Payments, net of recoveries	(57,038)	(35,954)
Claim Losses Realized	(1,326)	(7,230)
(Increase) in Fees Receivable, before provision	(7,215)	(7,842)
(Increase) Decrease in Other Assets	(10)	387
Decrease (Increase) in Central Reserve Bank Account	295	(561)
Increase (Decrease) in Accounts Payable, Accrued Expenses and Other Liabilities	632	(2,342)
Increase in Unamortized Origination Fees	2,906	0
Increase in Interest Payable	1,898	834
Net Cash Used by Operations	(44,305)	(37,133)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of Furniture and Equipment	(180)	(368)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings From Treasury	48,000	24,000
Net Increase (Decrease) in Cash	3,515	(13,501)
Cash and Cash Equivalents, beginning of year	5,735	19,236
Cash and Cash Equivalents, end of year	$9,250	$5,735

The accompanying notes are an integral part of the financial statements.

AGENCY FOR INTERNATIONAL DEVELOPMENT
HOUSING AND OTHER CREDIT GUARANTY PROGRAMS
Notes to Financial Statements
For the years ended September 30, 1991 and 1990

Note 1. Entity and Mission

The Agency For International Development (A.I.D.) administers the Housing Guaranty Program and the Agricultural and Productive Credit and Self-Help Community Development Program, programs established by Congress to stimulate the participation of the private sector in the economic development of less-developed countries. These programs operate as revolving funds, subject to the appropriation process. Although they no longer receive appropriations, they are authorized to borrow from the U.S. Treasury.

The Housing Guaranty Program was established by Title III, Sections 221, 222, 223, and 238c of the Foreign Assistance Act of 1961 (FAA), as amended. The purpose of this act is to assist in providing long-term financing for low-income shelter and neighborhood infrastructure upgrading programs in developing countries. U.S. private sector lenders provide unsecured financing at commercial rates for projects undertaken by eligible resident borrowers. The repayment of the principal and interest is guarantied through A.I.D. by the full faith and credit of the U.S. Government. This guaranty promotes U.S. lender participation in providing financing at lower interest rates. In return, A.I.D. charges the borrowers guaranty fees and also requires that the Host Country government of the borrowers sign a full faith and credit guaranty to A.I.D. for the repayment of the loan and outstanding interest paid by A.I.D. on behalf of the borrower. The fees charged to borrowers are comprised of an annual fee of one-half of one percent of the unpaid principal balance of the guarantied loan, and an initial charge of one percent of the amount of the loan. All fees together with earnings thereon are held in a revolving fund account maintained by the U.S. Treasury. The enabling legislation intended for the fees to meet costs incurred in connection with the program.

The total principal amount of guaranties issued and outstanding under this title cannot exceed $2,558 million at any one time. Generally, the face value of guaranties issued with respect to housing in any country does not exceed $25 million in any fiscal year, and the average face value of guaranties issued in any fiscal year does not exceed $15 million.

The Agricultural and Productive Credit and Self-Help Community Development Program (Productive Credit Guaranty Program) was instituted with the addition of Section 222A to the FAA in 1974. A $3 million revolving fund was established by the enabling legislation for use on the Productive Credit Guaranty Program. The Agency For

International Development was authorized through September 30, 1988 under the Productive Credit Guaranty Program to issue full faith and credit guaranties of the U.S. Government to private lending institutions, cooperatives, and nonprofit development organizations in five Latin American countries. Since 1988, no additional guaranties have been issued under this program.

Note 2. Summary of Significant Accounting and Reporting Policies

Basis of Accounting

The financial statements are prepared in accordance with Generally Accepted Accounting Principles (GAAP). Revenues are recognized when earned and expenses are recognized when a liability is incurred.

Cash Equivalents

The Housing Guaranty Program defines Funds with U.S. Treasury and all investments in U.S. Government Obligations as cash equivalents. Since investments in U.S. Government Obligations are short-term highly liquid investments with maturities of three months or less, they are presented as cash equivalents in the Statements of Cash Flows.

Fees Receivable, Claims Receivable and Rescheduled Claims Receivable

Fees receivable are charged for guaranties outstanding and for guaranty origination. Claims receivable and rescheduled claims receivable are due from Host Country governments as a result of defaults under the Housing Guaranty Program. Receivables are stated net of an allowance for uncollectible amounts.

Reserve for Guaranty Losses

The reserve for guaranty losses provides for losses inherent in the guaranty operation. This reserve is a general reserve available to absorb losses related to guaranties outstanding and commitments to guaranty, both of which are off-balance sheet commitments. The provision for losses on guaranties is based on management's evaluation of the guarantied loans. This evaluation is based upon analyses of the prior loss experience related to the developing country and credit risk assessments which incorporate evaluations of the economic and political conditions which could affect the country's repayment ability. The evaluations take into consideration such factors as the existence of other Host Country government guaranties, transfer risk, assessments of Host Country credit risks by other federal financial assistance program sponsors, and the projected political stability within the country.

Depreciation

Furniture and Equipment are stated at cost less accumulated depreciation. Depreciation of Furniture and Equipment is computed on a straight-line basis over a 10 year period for Residential Furniture and Equipment and over 7 years for Office Furniture and Equipment.

Unamortized Origination Fees

Origination fees in excess of direct origination costs are deferred and recognized over the life of the guaranty as an adjustment to fee income.

Reclassification

The balance in the Central Reserve Bank Account has been reclassified from Accounts Payable in the 1990 financial statements to conform to the 1991 balance sheet presentation. Other minor reclassifications were made to the statement of operations for the year ended September 30, 1990, to conform to the 1991 presentation.

Note 3. Intra-government Transactions

The Housing Guaranty Program is subject to the financial decisions and management controls of Agency for International Development (A.I.D.), which in turn is subject to the financial decisions and management controls of the Office of Management and Budget (OMB). As a result of these relationships, the program's operations may not be conducted nor its financial position reported as they would be if the Housing Guaranty Program were an autonomous entity.

A.I.D. is reimbursed by its programs for miscellaneous agency support costs quarterly. Personnel costs charged to the Housing Guaranty Program are based on A.I.D. agency-wide estimated staffing requirements rather than actual personnel usage.

As discussed in Note 14, the Housing Guaranty Program does not account for those aspects of the pension liability, assets, and expense which are the responsibility of the U.S. Office of Personnel Management and the Federal Retirement Thrift Investment Board.

Note 4. Fund Balance with Treasury

The funds with U.S. Treasury include the funds for the Housing Guaranty Program and the Productive Credit Guaranty Program. The Productive Credit Guaranty Program funds were restricted for use thereon through fiscal year 1990. In 1991, management of the Housing Guaranty Program was informed that it could use these funds for the Housing Guaranty Program. These funds are therefore no longer restricted.

Note 5. Central Reserve Bank Account

In prior years, the Housing Guaranty Program required borrowers to deposit reserves designed to offset claims resulting from borrower defaults in trust into the A.I.D. Central Reserve Bank Account (CRBA) at a commercial bank in the United States. Interest accrued to the benefit of the borrowers and reserve account balances were to be refunded to the borrowers upon loan maturity. However, due to borrower defaults, the account no longer contains borrower monies and is now comprised entirely of A.I.D. funds.

Note 6. Investment in U.S. Government Obligations

The investment in U.S. Government Obligations at September 30, 1990, consisted of funds held for use in the Productive Credit Guaranty Program. During 1991, management determined that these funds were no longer needed by the Productive Credit Guaranty Program and the investments were liquidated and the funds used for Housing Guaranty Program purposes.

Note 7. Fees Receivable

Fees are charged to the borrower by A.I.D. for the guaranty. A one-time 1% fee based on the total amount of the loan is paid to A.I.D. upon contract ratification. Additional annual fees are charged at the end of each anniversary year based on the outstanding guaranty balance. This annual fee, which is .5% of the outstanding guaranty balance, is accrued on a monthly basis.

Fees receivable from major borrowing regions, net of the allowance for doubtful amounts, at September 30, 1991 and 1990 consist of the following (in thousands):

	Year Ended September 30, 1991	Year Ended September 30, 1990
Africa	$ 4,037	$ 2,134
Asia	567	-
Latin America	46,692	42,126
Near East	652	473
Total Fees Receivable	51,948	44,733
Less: allowance for uncollectible amounts	(44,507)	(38,000)
Fees Receivable, net	$ 7,441	$ 6,733

Changes in the allowance for uncollectible amounts were as follows (in thousands):

	Year Ended September 30, 1991	1990
Balance, beginning of year	$38,000	$31,075
Provision Charged to Operations	6,507	6,925
Balance, end of year	$44,507	$38,000

Note 8. Claims Receivable

When the Housing and Other Credit Guaranty Programs guaranty a loan, they require that Host Governments also guaranty payment of the loans. When the borrower on a guarantied loan defaults, the programs make claim payments to the lender and obtain the right to recover such payments from the Host Government. Claims receivable are established for receivables arising from these Host Government guaranties. Claims receivable by geographical area at September 30, 1991 and 1990 net of an allowance for doubtful amounts, were (in thousands):

	Year Ended September 30, 1991	1990
Africa	$ 7,027	$ 7,827
Latin America	85,476	98,205
Near East	1,749	1,343
Total Claims Receivable	94,252	107,375
Less: allowance for doubtful amounts	(85,394)	(92,539)
Claims Receivable, net	$ 8,858	$ 14,836

Changes in the allowance for doubtful amounts were as follows (in thousands):

	Year Ended September 30, 1991	1990
Balance, beginning of year	$ 92,539	$ 79,098
Provision Charged to Operations	38,380	27,666
Reschedulings	(45,525)	(14,225)
Balance, end of year	$ 85,394	$ 92,539

Note 9. Rescheduled Claims Receivable

The Housing Guaranty Program periodically reschedules claims according to the terms of bilateral agreements which are negotiated and agreed upon by the Paris Club, an informal group of governments which arranges the rescheduling of debts owed to or guarantied by government agencies. Frequently, terms of rescheduling agreements require that previously accrued interest be capitalized. When claims in non-performing status are rescheduled under these terms, interest for the non-performing period is included in the rescheduled principal amount, and capitalized as part of the new agreement.

Rescheduled claims receivable net of an allowance for doubtful amounts, at September 30, 1991 and 1990 were as follows (in thousands):

	Year Ended September 30, 1991	1990
Africa	$ 31,502	$ 22,497
Latin America	101,310	40,156
Near East	323	322
Total Rescheduled Claims	133,135	62,975
Less: allowance for doubtful amounts	(105,199)	(53,461)
Rescheduled Claims Receivable, net	$ 27,936	$ 9,514

Changes in the allowance for doubtful amounts were as follows (in thousands):

	Year Ended September 30, 1991	1990
Balance, beginning of year	$ 53,461	$36,913
Provision charged to operations	6,213	2,323
Rescheduled Claims	45,525	14,225
Balance, end of year	$105,199	$53,461

Note 10. Furniture & Equipment

Furniture and equipment at cost as of September 30, 1991 was $1,218 thousand less accumulated depreciation of $539 thousand. At September 30, 1990, furniture and equipment at cost was $1,780 thousand less accumulated depreciation of $1,042 thousand.

Note 11. Borrowings from U.S. Treasury

Until the end of fiscal year 1991, the Housing and Guaranty Program had unlimited authority to borrow directly from the U.S. Treasury. Subsequent to September 30, 1991, pursuant to the Credit Reform Act of 1990, the program will be financed primarily by appropriations and will be authorized to borrow from Treasury for short-term cash needs. The program must continue to service and repay its existing borrowings, using appropriated funds as necessary.

As of September 30, 1991 and 1990, the Housing Guaranty Program's outstanding debt matures as indicated below (dollars in thousands):

Maturity	Average Rate on Outstanding Balance	Year Ended September 30, 1991	Year Ended September 30, 1990
9/30/1996	8.51%	$ 20,000	$20,000
9/30/1997	8.78%	25,000	25,000
9/30/1998	8.85%	13,000	13,000
9/30/1999	8.50%	24,000	24,000
9/30/2000	8.25%	48,000	-
		$130,000	$82,000

Interest paid during the year ended September 30, 1991 was $7.4 million, and during the year ended September 30, 1990 was $5 million.

Note 12. Reserve for Guaranty Losses

The reserve for guaranty losses provides for losses inherent in the guaranty program. Changes in the reserve for guaranty losses for fiscal years 1991 and 1990 were as follows (in thousands):

	Year Ended September 30, 1991	Year Ended September 30, 1990
Reserve, beginning of year	$685,625	$632,188
Provision (credit) charged to operations	(1,881)	60,667
Claim losses realized	(1,326)	(7,230)
Reserve, end of year	$682,418	$685,625

Note 13. Government Equity (Deficiency)

Government Equity (Deficiency) consists of appropriated capital and accumulated earnings (deficiencies) of the Housing Guaranty Program, and the equity of the Productive Credit Guaranty Program. Appropriated Capital is the total of funds appropriated to the Housing Guaranty Program since its inception. The Housing Guaranty Program operates as a revolving fund and thus accumulates earnings and deficiencies over time. The equity of the Productive Credit Guaranty Program consists of a $3 million transfer from unrestricted accumulated earnings of the Housing Guaranty Program in 1974, plus the accumulated earnings of the Productive Credit Guaranty Program since its inception. In prior years, the equity of the Productive Credit Guaranty Program was restricted for the use of the Productive Credit Guaranty Program only, however, subsequent to September 30, 1991, management of the Housing Guaranty Program was informed that the Productive Credit Guaranty Program equity could be used for other Housing Guaranty Program purposes. Consequently the balance is not considered restricted on the Statement of Financial Position at September 30, 1991. As discussed in Note 15, in 1990 two prior period adjustments were recorded to the 1989 unrestricted accumulated earnings.

Note 14. Pensions

Housing Guaranty Program employees are covered by Civil Service Retirement System (CSRS) or the Federal Employee Retirement System (FERS). For CSRS, 7 percent of the employees' gross earnings is withheld and the Housing Guaranty Program contributes a matching amount. For FERS, 0.8 percent of employees' gross earnings are withheld and the Housing Guaranty Program contributed approximately 13 percent in 1991 and 1990. An additional 6.2 percent of the FERS employees' gross earnings are withheld and sent to the Social Security System. Additionally, foreign direct-hire personnel are covered by the Foreign Service Pension System (FSPS). Under FSPS, 1.3 percent of employees' gross earnings is withheld and the Housing Guaranty Program contributed 21.9 percent in 1991 and 1990.

Employees may elect to participate in the Thrift Savings Plan (TSP). Based on employee elections, 0 to 5 percent of CSRS employee gross earnings are withheld and 0 to 10 percent of FERS and FSPS employee gross earnings are withheld. FERS and FSPS employee elections are partially matched up to a total of 5 percent of earnings. FERS and FSPS employees also receive an automatic 1 percent contribution.

Although the Housing Guaranty Program funds a portion of employee pension benefits and makes necessary payroll withholdings, it has no liability for future payments to employees under the programs, nor is it responsible for reporting the assets, actuarial data, accumulated plan benefits, or any unfunded pension liability. Reporting of such amounts is the responsibility of the U.S. Office of Personnel Management and the Federal Retirement Thrift Investment Board. Data regarding actuarial present value of accumulated benefits, assets available for benefits, and unfunded pension liability are not allocated to individual departments and agencies.

Note 15. Prior Period Adjustments in fiscal year 1990

The accompanying financial statements for fiscal year 1990 include the effects of changes in accounting principles affecting prior years, as discussed below, because, in management's opinion, adoption of the new principles represented a change to more appropriate methods. Both of these changes were accounted for as prior period adjustments in the fiscal year 1990 and 1989 financial statements.

During 1990, Housing Guaranty Program management adopted a policy of reserving for anticipated losses on outstanding guaranties to better reflect credit risk associated with its portfolio in accordance with generally accepted accounting principles. In addition, management significantly increased the allowance for uncollectible claims. Credit risks associated with providing financial guaranties on the indebtedness of developing countries increased the allowance consistent with the aforementioned policies adopted for outstanding guaranties. The balance of Government Equity (Deficiency) at September 30, 1989, has been restated from amounts reported prior to 1990 to reflect a retroactive charge of $774 million.

Note 16. Commitments and Financial Instruments With Off-Balance Sheet Risk

In addition to the risks associated with its claim receivables, A.I.D. is subject to credit risk for financial instruments not included in its Statement of Financial Position. These financial instruments are guaranties on unsecured loans which provide principal and interest repayment protection to U.S. lenders against political and economic risks of lending to developing countries. A.I.D. does not hold collateral or other security to support its off-balance sheet risk. However, for most guaranties, a third-party guaranty from the Host Country government of the debtor is required for principal and interest disbursed by A.I.D. on behalf of the borrower.

The total financial guaranties committed by the Housing Guaranty Program, including loans pending contractual agreements, at September 30, 1991, amount to $2.8 billion. Of the total authorized guaranties, $2.3 billion have been contracted, and $13 million of the contracted guaranties remain to be disbursed. The remaining $500 million are commitments made by A.I.D. which will result in outstanding guaranties upon contract completion. Outstanding guaranties and guaranty commitments that management estimates may ultimately result in uncollectible claims have been reflected as a liability in the financial statements.

Limitations on the amount of guaranties which may be committed under the Housing Guaranty Program are established by Congressional legislation.

A summary of contract issuing authority by region at September 30, 1991 is as follows (in thousands):

Congressional Authority (Section 221)	$2,558,000
Less: Repayments on Section 223(d) not available for new guaranties	(1,960)
	$2,556,040

Total Loan Guaranties	**Authorized**	**Contracted**
Africa	$ 369,206	$ 280,302
Asia	575,400	390,000
Latin America	946,658	821,908
Near East	845,000	811,240
Inter-Regional	65,067	-
	2,801,331	2,303,450
Less: Partial Payments	(248,051)	-
Total Loan Guaranties	$2,553,280	$2,303,450

Partial repayments have been made on the total authorized amount, reducing the total outstanding guaranties to less than the total Congressionally Authorized amount.

Note 17. Subsequent Events -- Credit Reform

The Housing Guaranty Program is subject to the Federal Credit Reform Act of 1990 (PL 101-508) which was effective as of October 1, 1991. The primary objective of Credit Reform is to identify the costs inherent in federal credit programs so that they may be compared more easily with the costs of other federal spending. Consequently, commencing in fiscal year 1992, the program's activities will be funded through direct appropriation and borrowings from Treasury rather than through retained earnings accumulated over the years. Accordingly, the Housing Guaranty Program's financial presentation of its credit activities will change in 1992 and subsequent years as deficiencies are anticipated in the budget process and funded in advance through appropriations.

Note 18. Reconciliation of Expenses to Budgetary Outlays

The reconciliation of expenses to budgetary outlays is as follows (in thousands):

	Year Ended September 30, 1991	1990
Total Expenses	$66,099	$109,544
Adjustments to Total Expenses:		
Capital Expenditures - Fixed Assets	180	368
Claim Payments, net of recoveries	57,038	35,954
(Increase) Decrease in Payables	(2,530)	1,508
Increase in Receivables	7,225	7,455
(Decrease) Increase in Funds at commercial bank	(295)	561
Accrued Expenses not requiring outlays	(48,041)	(90,555)
Net Expenses	79,676	64,835
Less: Collections	(35,099)	(27,354)
Budgetary Outlays	$44,577	$37,481

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Appendix V

To the Administrator
and the Inspector General
of the Agency for International Development

Report of Independent Accountants on Internal Controls

We were engaged to audit the financial statements of the Housing and Other Credit Guaranty Programs (Housing Guaranty Program) of the Agency for International Development (A.I.D.) as of and for the year ended September 30, 1991 and have issued our report thereon dated July 17, 1992.

In planning and performing our audit of the financial statements of A.I.D.'s Housing Guaranty Program as of and for the year ended September 30, 1991, we considered its internal control structure. The purposes of this consideration were to: (1) determine our auditing procedures for the purpose of expressing our opinion on the financial statements; and (2) determine whether the internal control structure meets the objectives identified in the following paragraph. This included obtaining an understanding of the internal control structure policies and procedures and assessing the level of control risk relevant to all significant cycles, classes of transactions, or account balances; and for those significant control policies and procedures that have been properly designed and placed in operation, performing sufficient tests to provide reasonable assurance that the controls are effective and working as designed to prevent or detect material errors in the financial statements.

The management of the Housing Guaranty Program is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are: to provide management with reasonable, but not absolute, assurance that obligations and costs are in compliance with applicable laws; funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports in accordance with applicable accounting standards; and to maintain accountability over assets. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected.

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Also, projection of any evaluation of the structure 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.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories: origination of guaranties, cash receipts, claims receivable, investments, purchasing, cash disbursements, salaries and benefits, fixed assets, accounts payable and accrued expenditures, U.S. Treasury borrowings, project monitoring, and financial statement preparation and reporting.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants and Office of Management and Budget (OMB) Bulletin 91-14. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the organization's ability to ensure that obligations and costs are in compliance with applicable laws; funds, property and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports in accordance with applicable accounting standards; and to maintain accountability over assets.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not disclose all reportable conditions that are also considered to be material weaknesses as defined above.

MATERIAL WEAKNESSES

The Agency has not adequately evaluated the Housing Guaranty Program to ensure that it is meeting its legislative objectives in the most cost effective manner. This may have contributed to the deficit position of the program. Under Credit Reform, current practices, if continued in future years, could impact A.I.D. as a whole.

Condition:

(1) *A.I.D. is incurring significant interest costs on debt owed to the U.S. Treasury.*

It has been necessary over the past four years for the Housing Guaranty Program to borrow funds from the U.S. Treasury to make claim payments on defaulted loans, thereby fulfilling the faith and credit guaranty of the United States. Those borrowings have reached $130 million as of September 30, 1991. The Housing Guaranty Program incurs $1 million each month in interest expense on the borrowings from the U.S. Treasury. Under Credit Reform, the program will receive nondiscretionary appropriations to repay the borrowings. Interest costs resulting from this debt will be $12 million a year for the next six years, and lesser amounts thereafter through the year 2000. Repayment of the debt principal is scheduled to occur during 1997 through 2000.

(2) *A.I.D. has adopted a fee structure which is not risk-based.*

Countries which are classified as credit worthy are charged fees at the same rate as those which are considered to be significantly greater credit risks. An upfront fee of 1% and an annual fee of .5% of the outstanding guaranty balance are charged to borrowers regardless of repayment ability and notwithstanding the existence of a host country guaranty. This fee structure should be analyzed considering both developmental and financial implications. For fiscal years 1992 and beyond, discretionary funds will be appropriated based upon subsidy calculations. These subsidies could be reduced if a risk-based fee structure is deemed to be a feasible alternative to the existing structure.

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Cause:

The dynamics of the economic conditions of the less developed countries has resulted in the need to reevaluate the program's fee requirements. High management turnover, resulting from Foreign Service rotation requirements, coupled with limited resources has contributed to the lack of establishing formal, written policies concerning fee assessment and cash management. This has also contributed to infrequent reevaluation of the legislative and regulatory requirements as new policies are adopted and as changes in the targeted environments occur.

Effect:

The deficit financial condition of the program was not mitigated since management was not required by written policies to conduct periodic reassessments of fee structure and program borrowing requirements. The original appropriations, together with the fees collected, no longer cover all operating and administrative costs of the program. Borrowings have been consistently required over the past four years rather than on a "time-to-time" basis.

Further, the fee structure impacts the subsidy appropriations required to operate the program under Credit Reform.

Recommendation:

Management should continue to address with OMB the opportunities for prepayment or cancellation of the Housing Guaranty Program's debt to the U.S. Treasury.

Conduct an econometric study to determine the most effective fee structure which could reduce the subsidy requirement while remaining in conformance with the spirit of the program mission.

All policies based on precedent and historical practice should be analyzed, documented, formalized into a comprehensive manual, and approved by appropriate management. Policies and procedures should be reassessed periodically based on evaluations of program objectives, economic conditions of the developing countries, and recent or amended legislation.

Loan Management's policies and procedures have not been adequately formalized and documented; nor have the general accounting functions been automated. Consequently, controls are ineffective and errors occur in the recordkeeping and reporting functions.

Condition:

Inconsistencies and errors occur in the Housing Guaranty Program's financial operations as a result of inadequate written policies and procedures specific to the Housing Guaranty Program. Agency-wide handbooks do not address certain activities related directly to the Housing Guaranty Program's financial operations. This lack of guidance, and lack of consistent application of operating procedures, causes inconsistencies in day-to-day financial operations and accounting practices, and results in excessive training time for new personnel. Consequently, financial information is not presented accurately nor timely.

For example, the following discrepancies have been noted in the accounting records and functions which have resulted in weaknesses in controls and errors in the financial statements prepared by management prior to the audit. Although the effects of these discrepancies have been corrected in the audited financial statements, they are indicative of the types of errors which occur regularly, given the weak general accounting systems.

(1) All source documentation is recorded in either the general ledger or various and sundry workpapers which flow to the trial balance or directly to the financial statements. As a result, the original books of entry were incomplete and the financial statements had more transactions reported than did the general ledger. Also, transactions were included in the financial statements which were not included in the trial balance.

(2) Transactions related to the Funds held with the U.S. Treasury were not properly reported in the financial statements. The books are adjusted to reflect the balance as reported by the U.S. Treasury, thus the financial statements include unanalyzed reconciling differences in the Funds with U.S. Treasury balance. These differences were netted in accounts payable rather than being analyzed and recorded in the correct accounts.

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(3) The report of Loans Authorized and Not Under Contract at September 30, 1991 does not contain two guaranties that were issued in fiscal year 1991 -- one for Morocco, and one for India totalling $10.9 million. This resulted in an understatement of the total principal amount of guaranties issued and outstanding as of September 30, 1991, as reported in the Financial Summary Report (W-239).

(4) Intraagency transactions were not eliminated for the consolidation of the financial statements. Due to the failure to eliminate reciprocal transactions between the Regional Housing and Urban Development Offices (RHUDOs) and Washington, accounts were overstated.

(5) The following discrepancies were noted in the recordation of the Claims Receivable balance.

- Claim payments recorded in the subsidiary ledger for two loans did not agree to the supporting Statements of Amounts Due And Unpaid (prepared by Loan Management). This would have resulted in an understatement of the claims receivable balance at September 30, 1991.

- Loan Management maintains a balance of approximately $350,000 in the Central Reserve Bank Account (CRBA) at Riggs National Bank. When the balance exceeds this amount at the end of a month (due to recoveries from borrowers), management makes claim payments with the excess funds. These claim payment transactions, resulting from activity in the CRBA, are not recorded in the general ledger because they are not paid out of the Housing Guaranty Account at the U.S. Treasury. Loan Management should have recorded receivables resulting from claims paid out of the CRBA for Host Country Guarantied projects. Consequently, the claims receivable balance was understated by disbursements paid on behalf of two countries processed through this account.

(6) Loan Management recognizes expenses in its financial records as obligations are created. In turn, Loan Management recognizes accrued liabilities as the total monies obligated less disbursements against these obligations. In doing so, Loan Management includes in its operating expenses and accrued liabilities costs for goods that have not yet been

received. This method of accruing liabilities is not consistent with generally accepted accounting principles because it results in including in expenses and liabilities costs for goods and services not yet received.

(7) Guaranty authorizations have been identified which did not receive fund clearance by Financial Management. Since guaranty authorization is sometimes obtained by the Mission via telephone, controls are bypassed, and unreported guaranties have resulted. This could also result in delays in processing claims and inadvertently exceeding Congressional authorization limits.

Cause:

Formal policies and procedures specific to Loan Management have not been established, documented, and published. Additionally, the accounting functions are primarily manual, thereby contributing to compilation errors and inconsistencies in the financial operating and reporting procedures.

Effect:

Controls imbedded in the procedures are ineffective because the procedures are informal and inconsistently applied. Furthermore, errors in financial statement reporting occur frequently and are not promptly detected. Orientation of newly hired personnel is extended since documentation is not available to facilitate their learning process.

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Recommendation:

Policies and procedures should be formalized, documented, and published. The handbooks should be specific and should address the routine functions of personnel from staff levels to management levels. Procedures should make clear the: (1) responsible party; (2) accountable party (i.e. authorizing official); (3) required frequency of the duty; (4) forms/checklists and reports necessary to facilitate the function; and (5) reporting requirements to management.

Additionally, desktop procedures with step-by-step instructions should be developed at the staff level and reviewed for completeness, efficiency, and effectiveness of duties. Staff should be required to understand the purposes of the functions as well as their proper execution. This will facilitate inquiry and analysis by personnel.

Procedures should include the proper flow of all types of documents into and out of Loan Management. The sending party, receiving party, and purpose of report should be documented. Additionally, the proper recording of the information gathered should be documented.

For instance, information should flow as follows with no exceptions:

- source documentation to workpapers;
- workpapers to subsidiary ledgers;
- subsidiary ledgers to general ledger;
- general ledger to trial balance; and
- trial balance to financial statements.

Procedures should include specific formats, review checklists, and variance tracking mechanisms for conducting reconciliations. Variances should not be left unresolved for more than a one month period. Additionally, to ensure that the reconciliation function is being carried out, management should review the reconciling workpapers and indicate approval and ensure explanation of unresolved variances.

Furthermore, automation of the accounting functions specific to the Housing Guaranty Program is overdue. The design of an automated general ledger is underway, and its design should consider remedies to deter the aforementioned discrepancies from occurring. For instance, the design should consider:

- requiring consistent input of information for processing. For example, the "accrual module" should require three data entries, preferably through an interface to the Financial Accounting and Control System (FACS). Specifically, these entries are: (1) invoices approved for payment but not yet paid; (2) invoices which have been assigned a Bureau Voucher Number (to produce an adjustment to liabilities for invoices received, not yet approved); and (3) invoices received after "closing" for services received in the prior period, yet billed in the subsequent period (for "cut-off" liabilities);

- automatically performing reconciliations and "balancing" functions between subsidiary and general ledgers, to produce exception reports for management alerting them of out-of-balance conditions;

- recognizing account numbers which should be eliminated as part of the generation of a consolidated financial statement. (The system should also have the capability of producing unconsolidated statements for management analysis purposes);

- generating management reports which indicate performance (e.g. an Aged Receivables Report -- to measure collection efforts and Advice-of-Charge resolution), and track trends and variances (e.g., nonexpendable disbursement fluctuations by RHUDO).

A.I.D. does not conduct sufficient monitoring of the Paying and Transfer Agent.

Condition:

The Paying and Transfer Agent (PTA) is relied upon heavily to manage a material portion of the guaranty portfolio. The borrowers are required to contract with this agent for the services of remitting payments to current note-holders and transferring fees to both the lender and A.I.D. Under this agreement, the Paying and Transfer Agent: (1) maintains information on the transfer of guaranteed notes, thus tracking current lenders; (2) bills the borrower for the total payment due, including principal, interest, A.I.D. fees, and other fees; (3) manages the debt servicing of the loans, including transferring payments to lenders and to A.I.D. and notifying all parties when delinquencies and defaults occur; and (4) disbursing funds on behalf of A.I.D. to lenders for claims against A.I.D. resulting from defaulted loan payments.

A.I.D. requires that the borrower contract with the PTA prior to guaranty authorization. This contract reduces A.I.D.'s administrative workload since contact with numerous lenders need not be maintained. Accordingly, A.I.D. relies on loan status reports and requests for claim payments submitted by this agent. However, Loan Management does not conduct oversight procedures to ensure that this contracted agent is performing its delegated responsibilities in conformance with contractual requirements, and that the information provided A.I.D. is accurate.

Cause:

Resources are limited and, as a result, oversight responsibilities have been neglected.

Effect:

As a result of the absence of A.I.D.'s oversight of the PTA, A.I.D. has no assurance that the Claims Receivable balance is correct, nor that it has optimized interest earnings from repayments submitted by borrowers. Since the PTA reports loan status to A.I.D., and Claim Receivables are recorded directly from these reports without further verification, a misstatement in the Claims Receivable balance would go undetected by A.I.D. Additionally, A.I.D. relies solely on the PTA to report payments submitted by the borrowers. Accordingly, A.I.D. has no mechanism to ensure that funds are posted to A.I.D.'s account within the contracted timeframe since onsite reviews of PTA records are not conducted.

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Recommendation:

Management should re-prioritize the monitoring function over the PTA. Although it seems more critical to perform all of the daily routine functions rather than dedicating resources to a function which appears less productive, one of the most material aspects of the Housing Guaranty Program is managed by an outside party and should be overseen. In spite of the fact that the authority has been contracted, the responsibility to ensure that the program is being administered properly remains with A.I.D. management. Consequently, procedures should be formally developed to monitor the PTA's functions. The monitoring staff should possess appropriate loan management experience. The monitoring process over the management of the portfolio will be facilitated through the recent implementation of the Housing Guaranty Portfolio Management System which was used during this audit to reveal errors in reporting by the PTA.

In the interim, monitoring should include at a minimum:

- For recoveries to the CRBA account, Loan Management should require the PTA to fax a copy of the incoming telex accompanying the payment which shows the date and time received. Loan Management should reconcile these telexes against the monthly bank statements to ensure that the Central Reserve Bank Account (CRBA) is credited in a timely fashion;

- For claim payments made through the CRBA on behalf of borrowers, Loan Management should send a letter to the borrowers stating that a payment was made on their behalf. This would facilitate a mitigating control to ensure that all borrower payments have been captured in the loan status reports;

- Even though the claim amounts for CRBA-kept loans are dictated by Loan Management produced payment schedules, Loan Management should reconcile the payment schedules against the PTA's monthly disbursements to ensure the payment amounts are accurately and completely recorded in the proper period;

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- Loan Management must monitor the activities of the PTA more closely. Loan Management should routinely compare PTA amortization schedules and bills against amortization schedules produced by Loan Management.

Source documentation, including contracts, has been inadequately maintained in the Office of Housing resulting in an inability to support management's assertions in the financial statements and to defend A.I.D. should legal disputes arise.

Condition:

Numerous documents and contracts are required to support the operations of the Housing Guaranty Program. These documents are necessary to ensure everything from the legality of the projects to the assertions in the financial statements, including the:

- veracity of financial transactions, such as claims disbursements, fees and claims receivable, and disbursements from escrow accounts;

- legality of the projects originated, including the authenticity of official documents written in accordance with the program regulations and legislation, and;

- assurance that intended outcomes and program objectives are achieved.

Numerous documents were not available, thus we could not verify the aforementioned assertions.

For instance, a sample of thirty five guarantied projects -- five from each Regional Housing and Urban Development Office (RHUDO) -- revealed that a high percentage of contracts and agreements were missing in the Office of Housing and the Loan Management Division. A synopsis of missing documents is provided on the following page:

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Guaranty Authorizations	14%
Contract of Guaranty	3%
Host Country Guaranties	26%
Letter Agreement	3%
Implementation Agreements	31%
Paying & Transfer Agent Agreements	6%
Escrow Agreements	46%
Action Memos	46%
Action Memos for Disbursement from Escrow	37%

In addition, Escrow Account Reports, telexes from the Paying and Transfer Agent (i.e. copies of bills sent to borrowers), wire transfers (i.e. repayments and fees received from borrowers), and lender Selection Approvals are not consistently maintained in the files.

Further, documentation required to monitor the progress of the program participants and administrators was insufficient. Files maintained in the Office of Housing were missing numerous documents, such as RHUDO monitoring plans, on-site review reports (trip reports), initial visit memorandums, program reviews, and project implementation letters.

Cause:

Responsibility for maintenance of documents has not been formally established in Washington. Checklists have not been developed to facilitate the completeness of files, space is very limited, and state-of-the-art filing systems have not been provided.

Effect:

Most notably, A.I.D. may not be able to provide the necessary documents should a legal dispute occur. Further, the assertions in the financial statements cannot be supported and compliance with applicable laws and regulations cannot be assured. Also, analysis of program performance cannot be conducted through review of reports, and trends and discrepancies will go undetected. Moreover, redundancy occurs when different divisions are attempting to file and maintain the same documentation.

Recommendation:

A.I.D. should define custodial responsibility over all original documents and maintain them in a secured area. A central filing system similar to that implemented in Central Accounting and Reporting should be adopted where checklists are devised to ensure file completeness, information flowing to and from separate divisions (i.e. RHUDO, PRE/H, and Loan Management) should be tracked, and possession of files should be monitored and followed up. In addition, the authorization process should include a final distribution policy to ensure that all parties requiring documents receive the completed authorized documents rather than copies which have been partially processed and which do not evidence all necessary authorizations.

A.I.D. has no established and documented billing, delinquency notification, collections, write-off, and documentation procedures (collectively known as due diligence procedures) to follow when attempting to collect outstanding claims receivable.

Condition:

Documented due diligence procedures are essential to the effective collection of outstanding receivables. Documented due diligence procedures allow for standardization and accountability, and the use of performance standards to monitor effectiveness. Without documented due diligence procedures in place, staff responsibilities and duties cannot be properly designated. In addition, management is left without the tools necessary for effective decision-making.

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Loan Management's current due diligence procedures are informal and consist of billing the Ministry of Finance or similar body in host countries with outstanding claims receivable when the borrower's next regular payment is due. Billing only in the months when regular payments are due poses a problem for several reasons. Many of the loans which Loan Management guarantees use repayment plans which only require one or two payments per year. Loan Management's practice of sending bills in months when regular payments are due allows only one or two billings per year in which to collect outstanding receivables. This does not represent effective due diligence. In fact, it even allows for the possibility of a country falling under sanctions of Section 620(q) of the Foreign Assistance Act without even receiving so much as a single bill. The practice of one or two billings per year is ineffective for another reason. If a borrower only makes one payment per year on a loan, this payment is, understandably, quite large and financially straining. To ask a borrower or guarantor to make two complete payments at once may be a futile effort. Repayment is much more likely during months in which no large Housing Guaranty Program payments are due.

In addition to the billings, telephone calls are placed to the host countries by various A.I.D. personnel located at the Mission/RHUDO in attempts to collect monies due. A policy defining responsibility, frequency, and results reporting has not been formally established and documented. Therefore, this collection process is applied inconsistently.

Cause:

It appears that A.I.D. management has not made collection of outstanding claims receivable a high priority. Political and logistical aspects of contacting the debtor, which is often the Host Country Government, contributes to a cumbersome and time-consuming process conducted from Washington. Additionally, since formal policies and procedures have not been implemented, and A.I.D.'s analysis of the Debt Collection Act led management to believe that, for the most part, it is not applicable to foreign assistance programs, management is unaware of the collection approaches required.

Effect:

A.I.D. may be incurring losses on a significant amount of its claims receivable portfolio because it is not applying adequate due diligence procedures.

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Recommendation:

A.I.D. management should resolve with General Counsel and the Office of Management and Budget what Debt Collection Act provisions and other regulatory guidelines are applicable to the collection of foreign debt by Loan Management and the Office of Housing.

A.I.D. should establish and document formal due diligence procedures to be performed and documented each month for all outstanding accounts. All due diligence procedures implemented should include standardized procedures, as well as methods of documenting and analyzing performance. Sample procedures to include are:

- send bills each month for all outstanding claims receivable;
- contact the host country guarantor twice per month by telephone in attempts to collect outstanding claims receivable;
- mail letters to the host country on a monthly basis; the tone of these letters should stiffen progressively as the claim becomes more delinquent.

Consideration should be given to having the RHUDOs contact Host Countries regarding delinquent claim payments on a routine basis. This would be facilitated through an aged claims receivable report forwarded by Loan Management on a monthly basis. The RHUDO would be required to document collection efforts and report to Loan Management and the Office of Housing.

Loan Management has no documented formal guidelines or system to identify loans for which claim payments will be necessary, or to minimize the late fees and penalties paid on behalf of the borrower.

Condition:

Loan Management's current procedures of identifying loans for which claims payments will be necessary are rather informal. In general, the process performed for each claim is similar; however, the time periods in which the process is performed appear to vary widely.

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Currently, Loan Management identifies loans for claim payment by reviewing monthly payment schedules, lender reports, Paying and Transfer Agent's telex notifications to the borrowers, and letters from the lenders. The individual borrower's prior payment patterns are analyzed judgmentally to determine when Loan Management should initiate the claims process. Telephone attempts to contact the borrower are made to determine if the claim payment will be necessary. Loan Management attempts to pay all claims by the fifteenth day after the payment due date. Although this procedure is performed similarly for all claim payments, lack of standardization could potentially be very costly to the agency since A.I.D. will be liable to the lenders for late fees and interest penalties.

A.I.D., in the Letter Agreements and Guaranty Authorizations, guarantees to pay the lender all principal and interest owed the lender in the event of borrower default. The host country, in turn, agrees to indemnify A.I.D. for all claims paid on behalf of the borrower.

A.I.D., in its claim payments for host country guarantied loans, pays, in addition to principal and interest, late fees and interest penalties billed by the lender to the borrower. When a claim is made against the Housing Guaranty Program, the lender or PTA often includes in the claim billing interest penalties incurred through previous late payments. The bills are not accompanied by documentation which supports the additional fees. The Housing Guaranty Program pays the late fees as part of the claim, then includes the fees in the claims receivable from the host country guarantor.

Cause:

A lack of formalized procedures and accountability exists. Additionally, management does not have adequate reports on which to base decisions. Further, it appears that Loan Management has not made accurate, timely recognition of claims payable a high priority since the disbursements made by A.I.D. are then recorded as receivables from the Host Country. However, since the default rate is significant the program is still losing money unnecessarily.

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Effect:

Unnecessary losses are incurred by A.I.D. when untimely or inaccurate identification of claims occurs. These losses include late fees and unnecessary payments. A.I.D. paid more than $98,000 in late fees during fiscal year 1991. Many of these costs can be directly linked to Loan Management's lack of standard claim monitoring procedures.

Recommendation:

A.I.D. should develop a computerized tracking system, perhaps through the Housing Guaranty Portfolio Management System (HGPMS), for Loan Management to compare items such as payment due dates, claim initiation dates, and actual claim disbursement dates. This system should generate monthly management reports showing compliance with Loan Management imposed performance standards and late fees/interest penalties incurred by Loan Management on claim payments.

In addition, Loan Management should determine if it is liable to pay late fees and interest penalties on behalf of the borrower. If A.I.D. has no obligation to pay late fees and interest penalties on behalf of the borrower, the agency should cease the practice at once and re-write the standard guaranty authorization to outline A.I.D.'s responsibilities more specifically.

If A.I.D. does have an obligation to the lender to pay late fees and interest penalties on behalf of the borrower, Loan Management should require from the lenders documentation to support any late fees or interest penalties billed to A.I.D. by the lender.

Loan Management should establish and document formal procedures for identifying when claim payments are necessary. Compliance with these procedures should be tracked through the use of standard performance measures on a regular basis and reported to management.

Appendix V

Not all A.I.D. funds are under the U.S. Treasury custody.

Condition:

Generally accepted accounting principles require that all assets in the possession and control of an entity be reflected on the balance sheet.

The original cash in the Central Reserve Bank Account with Riggs National Bank was contributed by borrowers as a reserve against future defaults. This cash belonged to the borrowers and any interest earned on the account also belonged to the borrowers. The Housing Guaranty Program intended to use the cash in this account to pay lenders in the event that these borrowers defaulted. Once loans were repaid in full, any monies in the account which had not been used on the borrowers' behalf were to be returned to the borrowers.

Because the account was designed to operate in this manner, Loan Management did not recognize this cash in its financial statements as a Housing Guaranty Program asset. In addition, although federal law requires agencies to keep all cash in the U.S. Treasury, Loan Management believed that the cash did not belong to Housing Guaranty Program; thus, the money did not belong under the U.S. Treasury custody.

However, a recent study of the CRBA, initiated by Loan Management, revealed that nearly all of the borrowers who contributed to the CRBA have either defaulted on their loans, or experienced foreign exchange devaluation. These conditions resulted in the need for A.I.D. to make claim payments to lenders in amounts greater than borrowers' contributions to the CRBA plus any interest earnings. Thus, essentially all cash in the CRBA is a result of A.I.D. contributions to replenish the account. Accordingly, the money in the CRBA belongs to A.I.D., not the borrowers, and therefore, should be reported on the face of the balance sheet and maintained in a U.S. Treasury account.

Cause:

The causes of this problem are two-fold. First, the nature of the CRBA has changed over the years as the original borrower contributions have been depleted. Second, since sufficient records were not maintained on transactions

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in the CRBA, it was not determinable until a recent reconstruction of the account was performed, that the funds indeed belonged to A.I.D. Thus, the necessity to maintain the funds with the U.S. Treasury or to report them as assets of A.I.D. was not apparent.

Effect:

Because the amounts held by Riggs National Bank are public funds to be utilized by Housing, GAO Title 7 requires these funds to be held by the U.S. Treasury. Thus, Housing Guaranty is not in compliance with GAO Title 7.

Recommendation:

Currently, Loan Management has three options to comply with GAO's Title 7:

1) Close the Central Reserve Bank Account and transfer all funds to the U.S. Treasury;
2) Cease replenishing the account and allow it to deplete; or,
3) Obtain a waiver from the U.S. Treasury to continue the Central Reserve Bank Account with adequate control and supervision.

In all cases, the funds, which are A.I.D.'s, must be reflected on the balance sheet and reported to the U.S. Treasury as funds which are available to A.I.D. for operating its Housing Guaranty Program.

Appendix V

REPORTABLE CONDITION

Loan Management is not deobligating funds in a timely manner. There are outstanding obligated amounts which should have been deobligated because the goods or services already delivered cost less than the obligation or because the goods or services will not be received.

Condition:

Loan Management should review outstanding obligations on a regular basis and deobligate any monies for which obligations are no longer necessary in order to properly account for operating expenses and accrued liabilities.

Loan Management reviews outstanding obligations each July and deobligates any that management believes are no longer necessary. Loan Management performs this process again after the close of the fiscal year.

Loan Management is precluded from deobligating any funds related to multi-funded contracts unless the contract is complete. Loan Management cannot deobligate these funds even if no additional services are scheduled to be provided to Loan Management. Loan Management deobligates these funds only after receiving permission to do so from the Contracting Officer. Consequently, funds which could be made available to other programs within the agency remain restricted for use in the Housing Guaranty Program even though it is probable that the funds will not be utilized.

Cause:

Loan Management is hesitant to deobligate funds because an agency-wide suspense account has not been reconciled as of September 30, 1991. However, the reconciliation process is well underway, and as this process ensues, disbursements are posted against unliquidated Loan Management obligations from prior years.

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Effect:

Monies which were not deobligated are not made available for other uses and monies which are never deobligated create opportunities for fund misappropriation.

Recommendation:

First, A.I.D. should complete the reconciliation of the Unapplied Account as soon as possible. Second, a review of outstanding obligation status should be performed on a quarterly basis, especially for those funds which are no longer impacted by the suspense account problem (i.e. current year obligations). This can be accomplished with a FACS Support generated report, "Unliquidated Obligations". For any obligations in the report which have been outstanding for more than ninety days, management should investigate and deobligate any funds which are no longer deemed necessary.

****

Certain of the internal control weaknesses presented in this report were identified during the prior year audit of the Housing and Other Credit Guaranty Programs. Included among the previously identified deficiencies are: (1) inadequate financial systems; (2) A.I.D. funds maintained outside of the U.S. Treasury; (3) insufficient reconciliations of ledgers, trial balance, and financial statements; (4) inadequate controls over congressional authorization limits; (5) insufficient plans to repay borrowings; and (6) untimely deobligation of funds. These control weaknesses remain as reportable conditions which have not yet been rectified since the fiscal year 1990 financial audit of the Housing and Other Credit Guaranty Programs.

We also noted other matters involving the internal control structure and its operations that we are reporting to the management of the Housing Guaranty Program of A.I.D. in a separate letter.

Appendix V

This report is intended for the information of the Congress, the A.I.D. Office of the Inspector General, and the management of the Agency for International Development. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Price Waterhouse

Washington, D.C.
July 17, 1992

Office of Government Services
1801 K Street, N W
Washington, DC 20006.
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Price Waterhouse

Appendix VI

To the Administrator
and the Inspector General
of the Agency for International Development

Report of Independent Accountants on Compliance with Laws and Regulations

We were engaged to audit the financial statements of the Housing and Other Credit Guaranty Programs of the Agency for International Development (A.I.D.) for the year ended September 30, 1991 and have issued our report thereon dated July 17, 1992.

Compliance with laws and regulations applicable to the Housing and Other Credit Guaranty Programs is the responsibility of A.I.D.'s management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we tested compliance with laws and regulations that may directly affect the financial statements and certain other laws and regulations designated by Office of Management and Budget and A.I.D. Applicable laws included: Title III of the Foreign Assistance Act of 1961, as amended; the Chief Financial Officers Act of 1990; the Budget and Accounting Procedures Act of 1950; the Debt Collection Act of 1982; and the Prompt Payment Act. We reviewed management's process for evaluating and reporting on internal control and accounting systems as required by the Federal Managers' Financial Integrity Act (FMFIA) and compared A.I.D.'s most recent FMFIA reports with the evaluation we conducted of the Housing and Other Credit Guaranty Programs' internal control system. We also reviewed the programs' policies, procedures, and systems for documenting and supporting financial, statistical, and other information presented in the overview of the reporting entity, entitled "Program Overview". It was not our objective to provide an opinion on overall compliance with such provisions.

Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in laws or regulations that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements or the sensitivity of the matter would cause it to be perceived as significant by others. The results of our tests of compliance disclosed the following instances of material noncompliance.

A.I.D. management has not complied with certain provisions of the Debt Collection Act of 1982 which are applicable to the Housing and Other Credit Guaranty Programs with respect to the billing and collection of claims receivable. Inadequate due diligence policies and procedures coupled with a lack of accurate data in the recently implemented Housing Guaranty Portfolio Management System have contributed to management's noncompliance with the Act.

The Budget and Accounting Procedures Act of 1950 requires that the Housing and Other Credit Guaranty Programs' systems conform to the accounting principles, standards, and related requirements prescribed by the Comptroller General of the United States. In GAO's Policy and Procedures Manual for Guidance of Federal Agencies, Title VII, Fiscal Procedures, the Comptroller General requires that, except where the Congress may have legislated specifically to the contrary, all public funds shall be deposited in accounts maintained by the U.S. Treasury. However, program funds were maintained at a commercial bank in the United States and were not reported in the programs' financial reports to the U.S. Treasury.

A.I.D. management has not ensured compliance with the requirements of the Federal Manager's Financial Integrity Act of 1982 to establish internal administrative and accounting controls for the Housing and Other Credit Guaranty Programs in accordance with standards established by the Comptroller General. Thus, management cannot provide reasonable assurance that: obligations and costs are in compliance with applicable laws; funds, property and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports in accordance with applicable accounting standards; and to maintain accountability over assets.

Further, our review of management's process for evaluating and reporting on internal control and accounting systems as required by the Federal Managers' Financial Integrity Act (FMFIA) revealed that A.I.D.'s most recent FMFIA reports did not reflect material weaknesses of the Housing and Other Credit Guaranty Programs' internal control structure. These weaknesses significantly impair the fulfillment of the Housing and Other Credit Guaranty Programs' mission, violate statutory requirements of the Debt Collection Act and the Budget and Accounting Procedures Act and significantly weaken safeguards against loss of funds. Therefore, the material weaknesses should have been disclosed in the Agency's FMFIA report.

We considered these material instances of noncompliance in our decision to disclaim an opinion on the financial statements of the Housing and Other Credit Guaranty Programs as of September 30, 1991.

Appendix VI

Our review of the information presented in the "Program Overview" revealed that management of the Housing and Other Credit Guaranty Programs had not formulated performance indicators for use in measuring and reporting achievement with program objectives. Further, as disclosed by management in the Annual Financial Statement, the financial and performance information that was presented in the "Program Overview" was not derived from adequate systems which document and support the information presented. The Agency has initiatives underway to design an integrated financial management system intended to provide for the timely and uniform preparation of financial information and systematic measurement of performance and, accordingly, is complying with the provisions of the Chief Financial Officers Act regarding the development of systems to support performance measures.

As discussed in our report on the financial statements dated July 17, 1992, the scope of our work was not sufficient to enable us to express an opinion on the financial statements for the year ended September 30, 1991. Because the scope of our testing was limited as a result of the Housing and Other Credit Guaranty Programs' lack of adequate accounting records and automated systems, we are unable to determine whether all transactions complied in all material respects with the provisions referred to in the second paragraph of this report. Consequently, we are unable to determine, and thus give no assurance that, the Housing and Other Credit Guaranty Programs complied in all material respects with those provisions.

This report is intended for the information of the Congress, the A.I.D. Office of the Inspector General, and the management of the Agency for International Development. This is not intended to limit distribution of this report, which is a matter of public record.

Price Waterhouse

Washington, D.C.
July 17, 1992

USAID

U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

JUL 24 1992

MEMORANDUM

TO: AIG/A, John P. Competello

FROM: AA/FA, Richard A. Ames RAA
A-AA/PRE, John L. Wilkinson JLW

SUBJECT: Response to Draft Audit Report on Housing Guaranty

A.I.D. under the Housing Guaranty program has guaranteed $2.3 billion of loans carried out or in progress in over 40 countries. The program has consistently been evaluated as achieving high development impact. The program has demonstrated that a guaranty program can deliver the same developmental impact as other A.I.D. programs and leverage private funding for the foreign assistance program.

The HG program has felt the financial impact of the LDC debt crisis as have all international lenders, including the U.S. Export Import Bank (EXIM). As of the end of the fiscal year 1991 the program paid out $268 million in claims to U.S. investors, including $57 million in FY 1991. Most of these claims are the result of the rescheduling of LDC debt by the Paris Club, where the U.S. and other donors have agreed to accept less than the full amount of the official debt due. When this happens, A.I.D. must make up the difference due to the U.S. lender. Through FY 1991, A.I.D. has covered these costs by borrowing from the U.S. Treasury pursuant to authorities reviewed annually in authorizing and appropriation legislation. It is important to understand that these costs are not a reflection of the condition of the housing sector of the loan recipients, but reflect the overall debt of the borrower nations.

The Audit Report states that the HG program is intended to be self-supporting and should therefore revise its fee structure upward. However, with the onset in the 1980's of the LDC debt crisis other approaches to deal with claim payments were established for U.S. Government international credit programs. As discussed in the Program Overview of the audit in the section

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entitled "Financial Performance", we explain the evolution from the reliance on fee income to cover operating expenses and also losses on foreign exchange to the receipt of limited appropriations and then Treasury borrowing authority.

The Federal Credit Reform Act has put all credit programs "on-budget" or on a pay-as-you-go basis" whereby appropriated funds sufficient to cover the estimated credit risk over the life of these loans are made available upon authorization of any new loan guaranty. Under this system, in fiscal years 1992 and 1993, the HG program will require a subsidy appropriation of about 15 cents for every dollar of new loan guaranties.

The financial information and data available to program managers is more than adequate to make program decisions. The current audit and the prior year audit point out a number of significant accounting and program management problems regarding automation, procedures and documentation. Real progress was made in resolving these accounting issues in the past year and more will be accomplished next year. We agree that greater attention to resolving these issues is necessary.

Program management appreciates the audit report recommendations on adopting additional program performance measures and we expect to improve our capability in this area for the fiscal year 1992 audit.

The audit comments on the Housing Guaranty Program can be covered under three general classifications.

1. Lack of automated and integrated accounting systems:

   A servicing system (HGPMS) has been developed for Housing and is now being tested for the Private Sector Investment Program. In addition, staff have initiated work on the General Ledger, including credit reform requirements.

2. Lack of written policies and procedures for accounting operations:

   Accounting performance will continue to be borderline until this task is done. The process is on-going in the Loan

Management Division. There is no deadline established for completion of this task.

3. <u>A need for a review and documentation of program management policy</u>:

   This task must be undertaken in view of the many changes that are necessary to implement appropriate credit management policies and meet the needs of credit reform in the Agency. Discussions have not been initiated on either when this could be accomplished or the resources that can be made available.

We are in general agreement with the recommendations included in the draft audit report. Resolutions of the problems will require substantial effort by the Agency and action may be delayed in the Agency, since resources are limited. A plan to address the issues raised and plans to resolve them will be included in the Chief Financial Officer's five-year plan due to OMB by the end of August.

We appreciate the efforts of your staff and that of Price Waterhouse in provision of this audit of the Housing Guaranty Program.

Status of Prior Year Recommendations

The current status of the recommendations resulting from the fiscal year 1990 financial statement audit of the Housing and Other Credit Guaranty Programs is as follows:

Rec. No.	Status	Summary of Recommendations
1	Open	Maintain financial records which properly account for and record transactions affecting the Central Reserve Bank Account.
2	Resolved	Develop accounting records to support furniture and equipment balances recorded in the general ledger.
3	Resolved	Establish and document a methodology to compute the allowances for doubtful receivable accounts and losses on outstanding guaranties.
4	Resolved	Revise accounting and internal controls to ensure that Housing and Other Credit Guaranty Program non-salary administrative disbursements are charged to the appropriate program.
5	Resolved	Perform an analysis of accrual balances to ensure the validity of the recorded liabilities and to deobligate funds accordingly.
6	Resolved	Conduct an analysis of the agency support cost allocation process, and develop a more accurate method to allocate payroll and other costs to the appropriate program account.
7	Resolved	Automate the Housing and Other Credit Guaranty Programs related to accounting functions.
8	Resolved	Evaluate mitigating controls to financial accounting and control system during the implementation phase of the replacement system.

Status of Prior Year Recommendations

Rec. No.	Status	Summary of Recommendations
9	Resolved	Enhance Washington's controls over regional accounting station transactions recorded in the general ledger.
10	Closed	Perform reconciliations between the general ledger, summary records, and source documentation to ensure accuracy of data compiled.
11	Closed	Compare projects to Congressional Authorization Limits prior to guaranty authorization.
12	Resolved	Devise a payment plan to repay borrowings.
13	Closed	Devise a plan to liquidate investments associated with the Productive Credit Guaranty Program.
14	Resolved	Pursue travel advance collections, and implement collection efforts in accordance with existing policies and procedures.

Financial Management/Loan Management has indicated that they will provide us evidence shortly which, in their opinion, will result in closure of most of these recommendations by September 30, 1992.

Appendix IX

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