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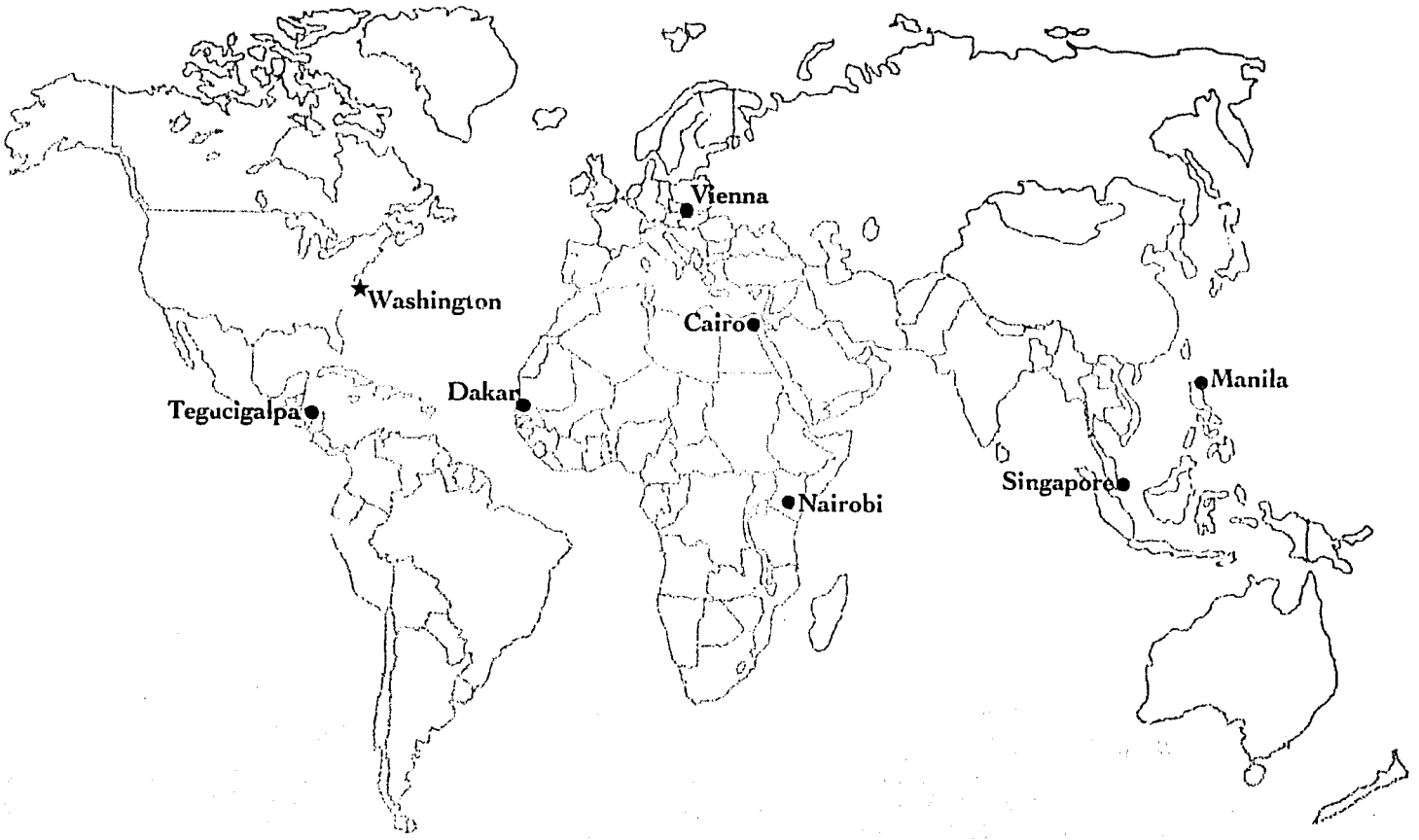
Regional Inspector General for Audit
Singapore

AUDIT OF USAID/PHILIPPINES' MANAGEMENT OF CASH ADVANCES TO RECIPIENT ORGANIZATIONS

Audit Report No. 5-492-94-017
August 31, 1994



INSPECTOR GENERAL
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

August 31, 1994

MEMORANDUM

TO: Thomas W. Stukel Jr., Mission Director, USAID/Philippines

FROM: Richard C. Thabet, RIG/A/Singapore

SUBJECT: Audit of USAID/Philippines' Management of Cash Advances to Recipient Organizations (Audit Report No. 5-492-94-017)

Enclosed are five copies of the subject audit report. Our audit work and the written representations made by your office confirmed that USAID/Philippines' management of cash advances has been effective in many ways. Nevertheless, further efforts were needed to limit cash advances to the immediate cash needs of the recipients.

In addition, our audit showed that USAID/Philippines generally required the recipients to maintain cash advances in interest-bearing accounts. However, the Mission did not ensure that all interest earned by recipients was promptly remitted to USAID.

Your comments to the draft report were very responsive. These comments are summarized after each finding and presented in their entirety in Appendix II. Based on your comments and supporting documentation, Recommendation No. 1.1 is resolved and can be closed when the planned action is completed. The remaining recommendations are unresolved and can be resolved when USAID/Philippines proposes an appropriate course of action.

Please provide us information within 30 days documenting actions taken to implement and resolve the open recommendations. I sincerely appreciate the cooperation and courtesies extended to my staff during the audit.

Attachments: a/s

EXECUTIVE SUMMARY

Federal agencies are required to administer their financial activities in a cost-effective manner so that the U.S. Treasury will have the maximum amount of cash available for investment and to avoid unnecessary borrowing. USAID/Philippines was responsible for administering outstanding cash advances—excluding advances made with operating expense funds—of about $25.7 million as of October 1992. By December 31, 1993, the total outstanding advances had decreased to $19.5 million (Page 1).

U.S. Army Corp of Engineers received cash advances from USAID/Philippines to study the effects of the Mount Pinatubo eruptions. Photo: Courtesy of U.S. Army Corp of Engineers

The Office of the Regional Inspector General for Audit, Singapore audited USAID/Philippines' management of cash advances to recipient organizations to determine whether the Mission: (1) limited cash advances

to the immediate cash needs of recipients, and (2) ensured that recipients maintained cash advances in interest-bearing accounts and remitted the interest earned to USAID. We made the audit from February 14, 1994 to March 4, 1994 (Page 2 and Appendix I).

With respect to the first audit objective, we found that USAID/Philippines' management of cash advances has been effective in many ways. Nevertheless, further efforts were needed to limit cash advances to the immediate cash needs of the recipients (Page 3).

With respect to the second audit objective, our audit showed that USAID/Philippines generally required the recipients to maintain cash advances in interest-bearing accounts. However, the Mission did not ensure that all interest earned by recipients was promptly remitted to USAID (Page 11).

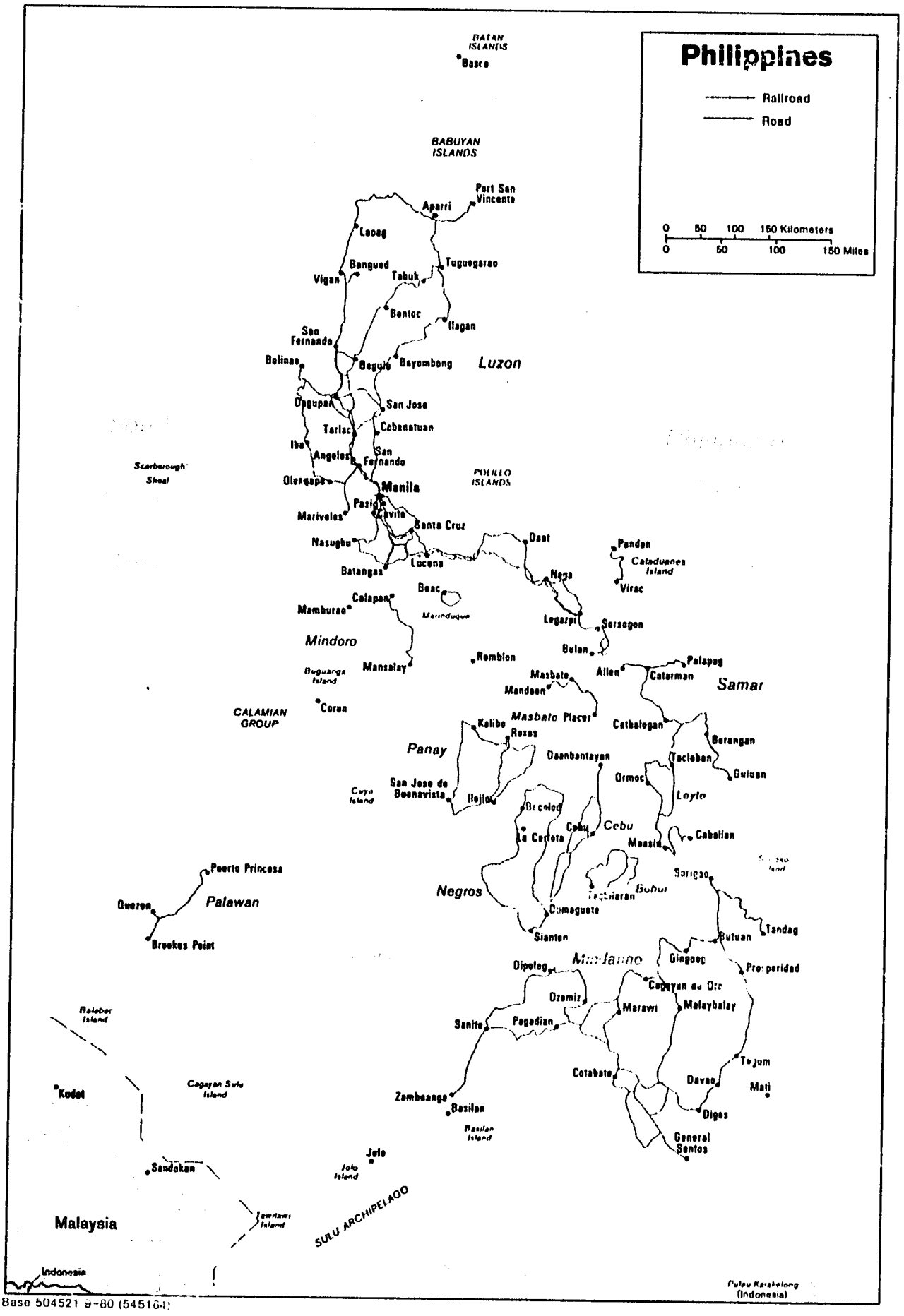
We made two recommendations to correct the problems identified by our audit. They include recommendations to better ensure that:

- cash advances are limited to the immediate cash needs of the recipients (Page 6); and
- all interest earned on advances is remitted at least quarterly to USAID (Page 13).

In responding to a draft of this report, USAID/Philippines officials generally agreed with the report's findings, but did not always agree with our recommendations to correct the problems identified. We carefully considered their comments in preparing this final report and made several revisions to our recommendations. The Mission's comments and our evaluations are summarized under each finding. The complete text of the Mission comments to our draft report is provided in Appendix II.

Office of the Inspector General

Office of the Inspector General
August 31, 1994



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INTRODUCTION

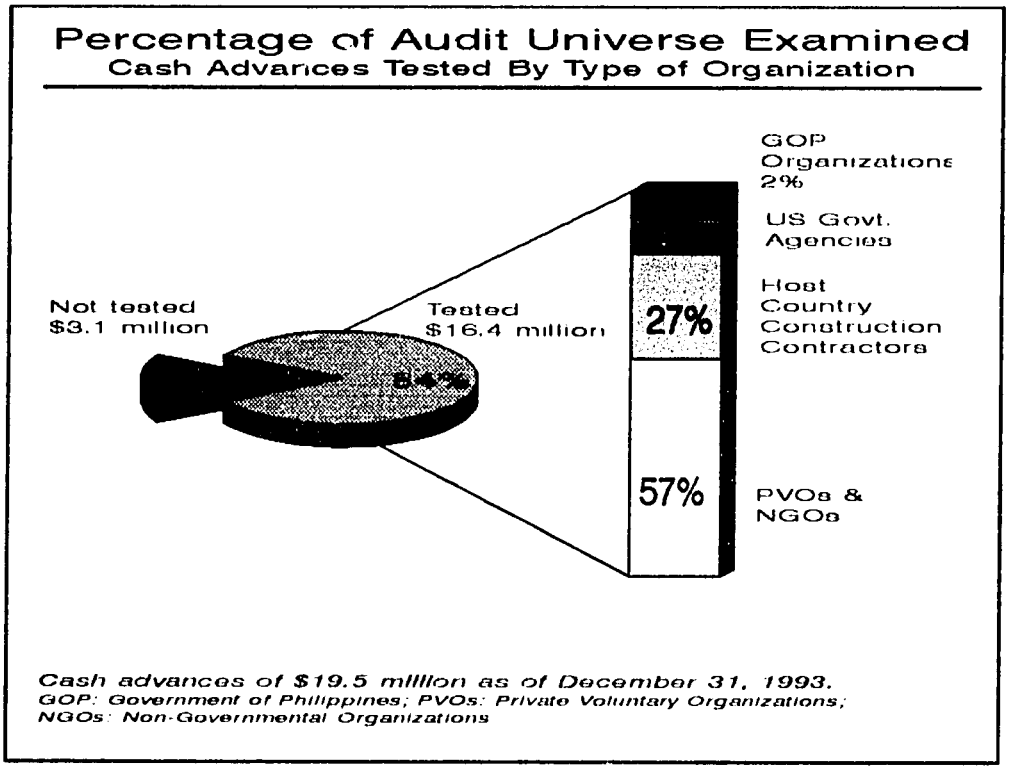
Background

Federal agencies are required to administer their financial activities in a cost-effective manner so that the U.S Treasury will have the maximum amount of cash available for investment and to avoid unnecessary borrowing.

Federal policy endorses advancing cash in reasonable amounts to nonprofit, educational or research institutions for experimental, developmental or research work. The U.S. Agency for International Development (USAID) extends this policy to all nonprofit organizations, including international private voluntary organizations and international research institutions. The policy ensures that the organizations will not have to use their own money to pay for work done under USAID agreements.

The U.S. Treasury requires federal agencies to monitor the cash management practices of recipients to ensure that advances of federal funds are limited to the minimum amounts necessary for immediate disbursement needs. If these advances exceed the minimum necessary, these agencies are required to take remedial action.

According to USAID/Philippines' records, the Mission was responsible for administering outstanding cash advances (excluding advances made with operating expense funds) of about $25.7 million as of October 31, 1992. By December 31, 1993, the total outstanding advances had decreased to $19.5 million. The following chart shows the types of organizations which received these advances.



Audit Objectives

The Office of the Regional Inspector General for Audit, Singapore audited USAID/Philippines' management of cash advances to recipient organizations. The audit was made to answer the following objectives:

- **Did USAID/Philippines limit cash advances to the immediate cash needs of recipients in accordance with USAID policy and U.S. Treasury regulations?**

- **Did USAID/Philippines ensure that recipients maintained cash advances in interest-bearing accounts and remitted the interest earned to USAID in accordance with Agency policy and Office of Management and Budget Circular Number A-110 requirements?**

REPORT OF AUDIT FINDINGS

Did USAID/Philippines Limit Cash Advances to the Immediate Cash Needs of Recipients in Accordance with USAID Policy and U.S. Treasury Regulations?

USAID/Philippines has not limited cash advances to the immediate needs of recipients in accordance with USAID policy and U.S. Treasury regulations.

Even so, USAID/Philippines' management of cash advances has been effective in many ways. For example, the Mission:

- Revised its procedures on advances in April 1993 to include U.S. Treasury and USAID Handbook provisions on restricting advances to amounts which meet the immediate disbursing needs of recipients. These revised procedures modified documentary requirements for the request of advances, reports of sub-grantee advances, and interest income from advances.

- Held in-house and external financial management seminars for various officials from the Mission, private voluntary organizations, and other recipients of advances. These officials were briefed on the Mission's revised procedures for providing cash advances. The issues discussed and explained included the U.S. Treasury and USAID Handbook requirements on cash advances. A total of 47 Mission officials and 69 employees of recipient organizations attended these seminars.

- Audited recipients through the non-Federal Audit Program and the Recipient-Contracted Audit Program. Two non-Federal audit reports and 27 recipient-contracted audit reports were issued from January 1993 through February 1994. These audits included coverage on advances made to

recipients and their compliance with USAID Handbook provisions and U.S. Treasury regulations.

- Made financial reviews or contracted with an external firm to review recipients' financial and other records. These reviews covered advances made to recipients and the corresponding liquidations made against those advances.

- Properly made $7.9 million in mobilization and other material advances under host-country construction contracts in accordance with the terms of the contracts. With the exception of $3.5 million related to mobilization advances to a construction contractor, the remaining $4.4 million were liquidated in accordance with the contracts' provisions, and were based on certifications from the surveyors and construction consultants employed.

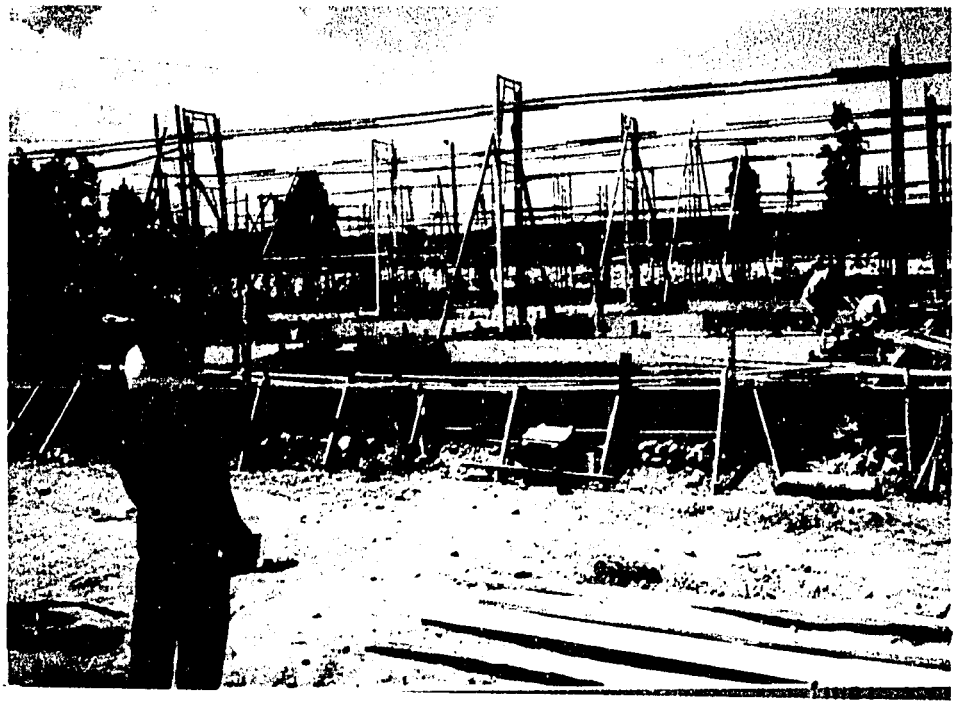
- Required recipients to submit requests for cash advances and the necessary cash flow analysis on the standard forms required by USAID policies and procedures. The forms were properly prepared and approved.

- Processed these requests for cash advances in a timely manner and properly obtained the administrative approvals from Project Officers for most of the 124 advances tested.

- Occasionally did not approve cash advances to recipients when their undisbursed cash balances were sufficient to meet immediate cash needs.

- Recently withheld a check for approximately $113,000 to another federal agency pending the liquidation of cash advance balances which were long outstanding.

- Commenced recouping excess undisbursed cash advances when processing new requests from recipients. As a result, outstanding advances decreased by $3.6 million or 15 percent from April 1993 to December 1993.



Olongapo City General Hospital - The construction for this hospital was financed by USAID/Philippines.
Photo: Courtesy of USAID/Philippines

However, USAID/Philippines did not limit cash advances to the immediate cash needs of recipients.

USAID/Philippines Needs to Further Improve Its Management of Cash Advances to Recipients

USAID/Philippines did not always limit advances to the immediate disbursing needs—30 days—of recipients as required by U. S. Treasury and USAID regulations. Mission officials believed that the allowed period of 30 days was inadequate to cover the cash needs of recipients and that this limit would be inefficient and impractical to apply. Furthermore, low priority was accorded to properly analyzing or monitoring the cash needs of recipients. The excess cash withdrawn from the U.S. Treasury cost the federal government an estimated $66,000 in additional interest costs between October 1992 and December 1993.

<u>Recommendation No. 1:</u> We recommend that USAID/Philippines:

1.1 Document justifications in writing when providing advances for more than 30 days cash needs; and

1.2 Document its review of the cash flow analyses of recipients to ensure that the amount of advances requested does not exceed immediate requirements.

U.S. Treasury regulations limit cash advances to amounts necessary to meet the immediate disbursement needs of the organization. Section 2025 of Chapter 2000 of the Treasury Financial Manual requires that:

> *"Advances to a recipient organization will be limited to the minimum amounts necessary for immediate disbursement needs and will be timed to be in accord only with the immediate cash requirements of the recipient organization in carrying out the purpose of an approved program or project. The timing and amount of cash advances will be as close as is administratively feasible to the actual disbursements by the recipient organization for direct program costs and the proportionate share of any allowable indirect costs."*

USAID Handbook 19, Appendix 1-B, on Cash Management further expands on these regulations. The Handbook stipulates that:

> *"Advances under Treasury Check methods...may be assumed to be cash requirements for as much as 30 days from the date the recipient receives the advance until it is expended. As an exception to the rule, the period of an advance...may extend for as long as 90 days when the Bureau AA, USAID Director or Office head has determined in writing that implementation will be seriously interrupted or impeded by applying the 30 day rule."*

These minimum amounts vary depending on the financing method used, the type of recipient, and whether written justification exists extending the period of the advance. Generally, U.S. Treasury check recipients receive advances for up to 30 days' needs. The rules and principles limiting cash advances to USAID recipients are contained in USAID Handbooks 1, 13 and 19, the USAID Financial Management Bulletin Part II, and in Volume 1 of the Treasury Financial Manual.

These rules and principles were also incorporated into USAID/Philippines' procedures for cash advances in April 1993 because of a 1993 Office of the Inspector General audit report recommendation. The procedures also require cash flow statements which detail projected cash requirements for immediate disbursement. Also, the procedures require the Mission to continually make trend analyses of the recipients' projected cash requirements against actual disbursements over several quarters. From the results of these analyses, the Controller and the Project Officer are to, if necessary, warn the recipients by letter and reduce the advances requested by the amount of the overstatement.

USAID/Philippines, however, made advances for 90-days cash needs without the required written justification. The grant agreements included provisions for advancing cash to recipients for 90-days needs. To illustrate, a grant agreement dated June 28, 1993 stipulates that:

> *"...the Grantee may request an initial advance of funds equivalent to the amount required for the first ninety (90) days of Grant activities."*

Accordingly, advances were routinely made for 90-day cash needs without documenting the justification for departing from the Agency's 30-day rule. We reviewed advances made to 26 recipients, representing $9.3 million (84 percent) of the $11 million outstanding advances to recipients under grants and cooperative agreements with nonprofit organizations as of December 31, 1993. These 26 recipients received $25.6 million (67 percent) of approximately $38.2 million in 90-day U.S. Treasury check advances made during the 15-month period from October 1, 1992 through December 31, 1993. None of these 90-day advances were supported with the required written justification.

According to USAID/Philippines' officials, it was not practical and efficient to restrict advances to the cash needs of recipients for 30 days, given the number of advances made. Processing and liquidating them would significantly increase Mission workload on a staff which is continually being reduced due to cuts in operating expense funding. Also, the 30-day rule is generally difficult to implement in an overseas mission environment as USAID takes time to process the advance, request the check from the disbursing officer in Bangkok, receive the check and send it to the recipient, sometimes located in a remote part of the country.

Furthermore, USAID/Philippines officials were of the view that the recipients needed advances for 90-day cash requirements. These recipients did not have the money or access to other sources of cash to

meet their working capital requirements in implementing the grant activities. Although the 90-day rule was not formally documented, Mission officials noted that the Mission Director was well aware of the reasons for making 90-day advances and approved this rule.

Even if USAID/Philippines had prepared written justification for all the 90-day advances, the advances still would not always have been limited to the immediate disbursing needs of recipients. For example, in July 1993, the Mission prepared a trend analysis on the projected cash requirements of recipients. It showed the following:

- 27 percent consistently spent less than 50 percent of what they had projected.
- 52 percent consistently spent less than 75 percent of what they had projected.
- 14 percent consistently spent less than 50 percent of the amount advanced.
- 41 percent consistently spent less than 75 percent of the amount advanced.

Although the results of the above analysis were explained at a USAID financial management seminar attended by Project Officers and recipient officials, these recipients still continued to overstate their projected needs for cash advances. USAID/Philippines' records showed a total of $19.5 million in unliquidated cash advances to approximately 115 recipient organizations as of December 31, 1993. For 38 organizations selected, $13.1 million (or 34 percent) of the $38.2 million advanced from October 1, 1992 through December 3, 1993 exceeded their immediate disbursement needs. On the average, these organizations took 179 days to liquidate the advances.

Commencing in April 1993, USAID/Philippines adopted an approach of rolling over the undisbursed balance from prior advances instead of reducing the next request for an advance. This approach did not have the intended effect of reducing the recipients' overstated cash projections submitted for that quarter.

For example, an advance of $51,452 was made to a grantee for the quarter ended September 30, 1993. In November 1993, $29,106 was reported as disbursed, and a new advance of $60,598 for the following quarter was requested. USAID/Philippines reduced the amount requested to $40,814 by rolling over $19,501 undisbursed from previous advances and $283 from interest earnings. As a result, the recipient still had $60,598 as an advance outstanding. Instead of reviewing the advance request to determine if the projected disbursements were excessive, the Mission merely rolled over the undisbursed balance into the October advance. Therefore, the Mission did not properly apply the principles established in its April 1993 procedures to reduce the amounts advanced to recipients.

USAID/Philippines gave low priority to analyzing and monitoring the recipients' immediate cash requirements and comparing the projects for the cash required to actual disbursements for the projects. Although the Mission planned to analyze the recipients' history of advances and liquidations for the six months following the April 1993 revised procedures, this analysis had not been made as of March 1994.

If advances were restricted to the needs of recipients for 30 days, the outstanding balance would have been reduced by about $8.9 million for the 15-month period covered in this audit. Since USAID/Philippines did not make proper determinations to justify the 90-day advances, there is insufficient assurance that the Mission efficiently managed the $38.2 million in advances by ensuring that they were made only in amounts necessary to meet the immediate disbursement needs, thus minimizing overdue balances.

By not reviewing the requests from recipients for advances to ensure that they were only for immediate cash disbursement needs, the $13.1 million in excess cash advances identified above cost the federal government potential interest earnings. We estimate that, in addition to the $189,000 total interest earned and reported for the 15-month period under review, $66,000 in savings could have been realized if advances were limited to 30 days' needs instead of 90 days.

USAID/Philippines needs to determine the immediate cash needs of the recipients and only make sufficient advances for reasonable periods. Any exceptions to the 30-day rule need to be justified, documented in writing, and approved. If advances are extended for periods longer than 30 days, the reasons should be explained. The Mission should only accept these reasons if they are significant enough to impede project implementation

if the advance is not made. Also, USAID/Philippines should ensure that the recipients' projected cash needs are reviewed, analyzed, and documented.

Management Comments and Our Evaluation

USAID/Philippines concurred with Recommendation No. 1.1, but did not agree with Recommendation No. 1.2. The Mission contends that it is already doing what the recommendation requires. Mission officials said that each recipient's outstanding cash advances and projected cash needs are carefully considered in processing new requests for cash advances. Furthermore, the voucher examiner compares actual against projected expenditures. Also, the Mission asserts that any unexpended balance from a previous cash advance which is not substantiated by the grantee's budget is deducted from the subsequent advance. These unexpended balances are not merely rolled over, and the grantees are required to justify their need to retain these unexpended advances.

We agree that the Mission tracks each recipient's cash advances and liquidations on a spreadsheet and requires the submission of liquidation reports for outstanding advances before new advances are made to the recipient. However, we found no evidence that the voucher examiners did any trend analysis of the recipients' actual cash needs based on their history of amounts advanced versus actually expended, as required by Mission procedures. Furthermore, only occasionally did the Mission not approve cash advances to recipients when their undisbursed cash balances were sufficient to meet immediate cash needs. We gave an example of such an excess advance to a grantee on page 9. Lastly, the July 1993 trend analysis prepared by the Mission (see page 8) disclosed that actual expenditures were consistently less than the amount requested and advanced by USAID. Since a recent trend analysis has not been prepared, the Mission is unaware of whether it still consistently provides advances in excess of the recipients' actual cash needs.

Based on USAID/Philippines' comments, Recommendation No. 1.1 is resolved and will be closed upon receipt of documentation showing that the planned corrective action has been completed. We have modified Recommendation No. 1.2, which is considered unresolved. The recommendation will be resolved when USAID/Philippines proposes an action plan to ensure that the recipients' projected cash needs are reviewed, analyzed, and documented.

Did USAID/Philippines Ensure that Recipients Maintained Cash Advances in Interest-Bearing Accounts and Remitted the Interest Earned to USAID in Accordance with Agency Policy and Office of Management and Budget Circular Number A-110 Requirements?

USAID/Philippines generally encouraged recipients to maintain cash advances in interest-bearing accounts in accordance with Agency policy and Office of Management and Budget Circular Number A-110 requirements. However, the Mission did not ensure that all interest earned by recipients was promptly remitted to USAID.

USAID/Philippines relied on the following internal control procedures to ensure that recipients maintained cash advances in interest-bearing accounts and remitted the interest earned.

(1) The Project Officers discuss these requirements with the recipients and hold seminars for private voluntary organizations.

(2) Recipient-contracted audits and non-Federal audits are made.

(3) The Mission's Controller's Office makes financial reviews of the recipients.

(4) The Mission's Office of Voluntary Cooperation contracted with a private firm to make financial reviews. This office handles grants and cooperative agreements with private voluntary organizations. A majority of the recipients fall into this category.

(5) The Mission implemented the use of "PVO Form 1B" in April 1993. The recipients use this form to request cash advances. The form requires the recipient to include the amount of interest earned which would then be deducted from the actual amount of cash transferred.

The photo below shows a project seminar which was financed by USAID/Philippines.

Seminar on Working Capital Management held at Batu-Bato Mountain Resort in Calamba, Laguna.
Photo: Courtesy of USAID/Philippines

Of the 38 recipients reviewed, all but two deposited advances into interest-bearing accounts when required. Twenty advances from 13 recipients were traced to bank statements without exception.

Nevertheless, USAID/Philippines does not have reasonable assurance that all interest earned was promptly remitted to USAID.

USAID/Philippines Needs to Better Monitor Recipients' Interest Earnings on Federal Funds

Contrary to federal regulations and Agency policies, USAID/Philippines did not ensure that interest earned by recipients on cash advances was promptly remitted to USAID. This occurred because Mission officials believed that they had sufficient internal controls to ensure that interest would be remitted. These controls were not fully assessed. Also, inconsistencies in USAID Handbook guidance contributed to this problem. As a result, an estimated $70,000 in interest was not remitted to USAID between October 1, 1992 and December 31, 1993.

<u>Recommendation No. 2:</u> We recommend that USAID/Philippines ensure that all interest earned is remitted to USAID on a quarterly basis by:

2.1 Requiring the recipient to report the period for which the interest is derived;

2.2 Reviewing the interest reported during the normal voucher review process, and following up with the recipient when the interest for the relevant periods has not been remitted; and

2.3 Requiring recipients to deposit USAID advances in interest-bearing accounts where appropriate.

Office of Management and Budget Circular Number A-110 requires recipients to maintain advances of federal funds in interest-bearing accounts and to remit the interest earned to the federal agency providing the funds. USAID Handbook 13, Chapter 4, extends this policy to all nonprofit organizations, including U.S. or international private voluntary organizations.

USAID Handbook 19 requires responsible Agency officials to monitor the cash management practices of recipients "to ensure that...except where contrary to law, interest earned on federal funds by recipient organizations is promptly paid over to the Treasury." According to USAID Handbook 13, Chapter 1, Section 10.3.e.:

> *"Recipients and subrecipients shall maintain advances of funds from AID in interest bearing accounts and shall remit to AID, at least quarterly, the interest earned on such advances. Interest amounts up to $100 per year may be retained by the recipient and subrecipient for administrative expense."*

Contrary to the Handbook 13 requirement above, USAID/Philippines did not adequately monitor the interest earnings of recipients to ensure that the interest was fully remitted quarterly. According to Mission records from October 1, 1992 through December 31, 1993, interest earned on advances to recipients and reported to USAID was $189,000. However, this amount did not reflect the total amount which should have been earned and remitted to USAID during this period. A review of 26 Mission files on recipients who were required to maintain interest-bearing

accounts disclosed that only 3 recipients remitted interest for the entire period.

The remaining 23 recipients either did not report any interest for this period or remitted some interest which could not be matched to the period earned. In three instances, the files disclosed that no interest was remitted. When the Project Officer asked one recipient why the interest was not remitted, the latter responded that it did not know the interest had to be remitted, but would do so in the future. For the other 20 recipients, some interest was reported. However, the interest remitted covered only one or two quarters, not the full period of five quarters. Furthermore, all 20 recipients did not identify the period for which the interest was earned. Some of the recipients who did not report or partially reported interest income are shown below:

Recipients	Interest Reported	Estimate of Interest Lost/ Not Reported
Philippine Business for Social Progress	$3,014 (two quarters)	$4,521
Economic Development Foundation	$16,188 (two quarters)	$24,282
Philippine Statistical Association	$0	$3,855
Philippine Center for Population and Development	$434	$1,732
Total	$19,636	$34,390

USAID/Philippines relied primarily on the existing internal control procedures listed on page 11. However, the Controller's Office does not have procedures to track the interest earnings of recipients from USAID advances. The voucher examiners were not required to track the interest reported or the interest not reported.

Even when the recipients reported the interest, they did not identify the period during which the interest was earned. Consequently, USAID/Philippines had difficulty in ascertaining whether the interest reported represented the complete amount earned.

Inconsistencies in the USAID Handbook guidance also contributed to the problem of advances not being placed in interest-bearing accounts. Specifically, Handbook 13, Appendix 4D, which pertains to non-U.S., non-governmental recipients, stipulates:

> *"AID funds shall not be commingled...The grantee shall deposit all AID cash advances in a separate bank account and shall make all disbursements...from this account."*

This section does not mention whether the recipients must deposit the advances in an interest-bearing account. However, Chapter 1 in Handbook 13 requires recipients to maintain USAID advances in interest-bearing accounts and to remit the interest earned.

Consequently, USAID/Philippines included the following clause in most of its agreements:

> *"If interest is earned with respective advances, the amount in excess of $100 or Pesos 2,400 per year shall promptly be paid to USAID at least quarterly."*

This clause did not require the recipients to deposit advances in interest-bearing accounts.

As a result, USAID/Philippines had insufficient assurance that the $189,000 of interest reported from October 1992 through December 1993 was the total for that period. Also, the Mission did not know which recipients were not reporting interest earned from USAID advances For those recipients who were required to place the advances in interest-bearing accounts, we estimated that the total interest to be received by the Mission for the period from October 1992 through December 1993 should be in the range of $235,000 to $282,000, or an average of about $259,000. Therefore, approximately $70,000[1] in interest was not remitted to the Mission for the period reviewed.

Interest earned by recipients on advances of federal funds are federal earnings. Remitting these earnings to the U.S. Treasury in accordance with applicable requirements helps to offset the borrowing costs incurred in making the advances. USAID/Philippines should therefore ensure that all interest earned is remitted to USAID by requiring the recipient-contracted auditor to: (a) determine the amount of interest earned on

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[1] Our estimate of $259,000 less $189,000 actually received by USAID/Philippines.

USAID funds for the period under review and (b) reconcile the amount derived against the amount reported or actually remitted to USAID. Also, the Mission needs to ensure that recipients place USAID advances into interest-bearing accounts where appropriate, and remit the interest earned at least quarterly.

Management Comments and Our Evaluation

USAID/Philippines generally agreed that the interest earned by recipients should be better monitored. However, the Mission disagreed with Recommendations No. 2.1 and 2.2 as presented in the draft report. The Mission believed that the recommendations would increase its workload without compensating benefits derived from the extra efforts. USAID/Philippines suggested that the recipients require their auditors to determine the amount of interest earned on USAID funds and reconcile the amount derived with the amount reported and remitted to USAID. The Mission has informed the recipients that these procedures will be incorporated in the scope of work for recipient contracted audits, and has provided us with copies of letters to recipients informing them of the additional procedures.

We agree with the Mission's suggestion to require the auditors to review and verify interest earned on USAID funds in general, but we disagree that the Mission should entirely transfer the responsibility of monitoring interest earned to the auditors. Recommendation No. 2.1 deals with correcting a reporting deficiency by requiring recipients to disclose the period for which the interest is derived in their reports. Recommendation No. 2.2 deals with following up with the recipients when interest is not remitted. The recipients are responsible to "determine the amount of interest earned" and properly report the same to USAID. As part of its normal voucher review process, the Mission will then be able to properly (and efficiently) review interest earned for the various periods and ensure completeness of the reported interest without increasing its workload. Therefore, based on Mission comments, we have modified Recommendation No. 2.2.

USAID/Philippines disagreed with Recommendation No. 2.3. Mission officials contend that neither the USAID Handbook nor Agency policy specifically stipulate that non-U.S. grantees must deposit USAID funds into interest-bearing accounts. Although USAID/Philippines believes that the Handbook guidance does not mandate interest-bearing accounts, the Mission does encourage the use of such accounts.

Although the USAID Handbook is not consistent in requiring that advances to indigenous recipients be deposited in interest-bearing accounts, Handbook 13, Chapter 1, Section 10.3.e., which applies to all nonprofit organizations, stipulates that organizations receiving advances of funds from USAID shall maintain these advances in interest-bearing accounts. While we understand that inconsistencies in the Handbook contributed to several advances not being placed in interest-bearing accounts, we believe the intention of the Handbook provision is that these advances should earn interest where appropriate. In some countries, the use of interest-bearing accounts is not always possible or legal. In the Philippines, however, these accounts are readily available. Furthermore, USAID/Philippines already encourages such accounts. Accordingly, based on Mission comments, Recommendation No. 2.3 has been amended to require recipients to maintain advances in interest-bearing accounts, where appropriate.

Based on USAID/Philippines' comments, Recommendation Nos. 2.1, 2.2, and 2.3 are unresolved. They will be resolved when the Mission proposes an appropriate course of action.

SCOPE AND METHODOLOGY

Scope

We audited USAID/Philippines' management of cash advances to recipient organizations in accordance with generally accepted government auditing standards. We made the audit from February 14 through March 4, 1994 at USAID/Philippines and reviewed the office's management of cash advances from October 1, 1992 through December 31, 1993.

We obtained computer-generated lists from USAID/Philippines showing the outstanding cash advances (excluding advances made with Operating Expense Funds) as of December 31, 1993, which totaled $19.5 million. We did not verify the overall reliability of this data. However, we verified the accuracy of the account balances and related data for the 38 recipients selected for detailed review.

We grouped the outstanding advances into five categories: (1) those under $100,000; (2) those which were at least $100,000 but less than $500,000; (3) those which were at least $500,000 but less than $1,000,000; (4) those which were at least $1,000,000 but less than $5,000,000; and (5) those which were $5,000,000 or more. We selected 100 percent of advances greater than $50,000 totalling $16.4 million or 84 percent for detailed review.[2] We then reviewed all the cash advances which were made from October 1, 1992 through December 31, 1993 to the 38 recipients identified in accordance with this methodology. These advances totaled $38 million. The $38 million included $7.9 million in mobilization advances to nine construction contractors and $4.6 million in other advances to another federal agency and Government of Philippines agencies.

[2] This amount includes advances to another federal agency and mobilization advances to nine host-country construction contractors.

We started with four audit objectives but deleted two because they were not applicable for USAID/Philippines. The objectives deleted were:

- Did USAID/Philippines use letters-of-credit to finance recipients in lieu of cash advances in accordance with USAID policy and U.S. Treasury regulations?

- Did USAID/Philippines program the local currency generated through its programs to provide cash advances to project recipients in lieu of using appropriated dollars to buy local currency?

The first objective was deleted because letters-of-credit are handled primarily in USAID/Washington, which is beyond the scope of this audit.

The second objective was deleted because USAID/Philippines did not have any programs which generated local currency during the audit period.

Methodology

The methodology for each audit objective follows.

Audit Objective One

This audit objective was to determine if USAID/Philippines limited cash advances to the immediate cash needs of recipients in accordance with Agency policy and U.S. Treasury regulations. To accomplish this objective, we reviewed the Mission accounting records on cash advances and liquidations for each selected recipient from October 1, 1992 through December 31, 1993 and calculated the number of days it took to liquidate the advances. We then reviewed this data to determine each recipient's unliquidated cash advance balances through December 31, 1993. When we found recipients with excess cash balances, we interviewed USAID personnel to determine the reasons. We discussed whether the personnel monitored the recipients' financial reports, analyzed recipients' immediate cash needs, and asked the recipients to return excess cash promptly. We also estimated the interest cost to the U.S. Treasury for the excess advances.

Audit Objective Two

This audit objective was to determine if USAID/Philippines ensured that recipients maintained cash advances in interest-bearing accounts and remitted the interest earned to USAID in accordance with Agency policy and Office of Management and Budget Circular Number A-110 requirements. To accomplish this objective, we reviewed recipients' agreements with the Mission to see if it required the recipients to deposit cash advances in interest-bearing accounts and to remit interest earnings to USAID. We also determined if the Mission had records showing the recipients' earnings. For 13 recipients, judgmentally selected, we obtained bank statements to confirm how they handled advances and the disposition of any earnings. We interviewed Mission personnel to determine how they tracked recipients' interest earnings and discussed the reasons why recipients did not remit the earnings to USAID. For the selected recipients who were required to maintain interest-bearing accounts, we estimated the amount of interest they ought to have earned and remitted to USAID for the audit period. Also, we estimated the total interest they should have earned but did not report to the Mission.

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

USAID / Philippines
APO AP 96440

Fax No.: 632 - 521 - 4811
Tel. No.: 632 - 522 - 4411

JUL 27 1994

MEMORANDUM

TO: Mr. Richard C. Thabet
RIG/A/Singapore

FROM: Thomas W. Stukel TWS
Director, USAID/Philippines

SUBJECT: Audit of USAID/Philippines Management of Cash Advances to Recipient Organizations

REFERENCE: Thabet/Stukel Memo dated May 24, 1994

As requested, we reviewed the draft report on subject audit. Please find below our response to the findings and recommendations. We hope that our response will be fully considered in finalizing the report. We are also enclosing a final representation letter for inclusion in the report.

Mission Response to Findings and Recommendations

First Objective: Did USAID/Philippines limit cash advances to the immediate cash needs of recipients in accordance with USAID policy and U.S. Treasury Regulations?

Finding No. 1: Advances were routinely made for 90-day cash needs without documenting the justification for departing from the Agency's 30-day rule.

Recommendation No. 1.1: Document justifications in writing when providing cash advances for more than 30 days cash needs.

Mission Response: The Mission concurs that a written justification is required. Accordingly, the Mission will put in writing the rationale for giving recipient organizations cash advances which exceed their 30-day cash needs. The Mission feels that to do otherwise will hinder recipients' performance and inhibit the development program. It also may not be in the best interest of the U.S. Government to limit advances to 30-day cash needs given the increased manpower requirements, and paperwork this would entail.

Finding No. 2: USAID/Philippines gave low priority to analyzing the recipients' immediate cash requirements and comparing the projections for the cash required to actual disbursements.

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USAID/Philippines adopted an approach of rolling over the undisbursed balance from prior advances instead of reducing the next request for an advance. This did not have the intended effect of reducing the recipients' overstated cash projections submitted for that quarter.

Recommendation No. 1.2: Review the cash flow analyses of recipients to ensure that the amount of advances requested does not exceed immediate requirements, and reduce future advances to recipients who consistently overstate projected cash requirements.

Mission Response: The Mission does not agree with the statement that low priority was accorded to the analysis of the recipient's cash requirements. Although a "formal" trend analysis comparing actual against projected expenditures was not done, this analysis is being carried out by each voucher examiner for each grantee when each cash advance voucher is processed. In addition, the cognizant project office reviews the related implementation plan and cash flow projections to determine the reasonableness of the grantees' projected cash requirements.

The Mission is already doing what the recommendation requires. Procedures to track cash advance requests and liquidations were initiated before the audit was conducted. The cash position and the cash flow projections submitted by the recipients are carefully considered in processing new cash advance requests. Any unexpended balance from a previous cash advance which is not substantiated by the grantee's budget, is deducted from the subsequent advance. Unexpended balances are not merely rolled over -- grantees are required to justify the need for that amount. Furthermore, new cash advance requests are not processed unless liquidation reports for previous advances are submitted.

Second Objective: Did USAID/Philippines ensure that recipients maintained cash advances in interest-bearing accounts and remitted the interest earned to USAID in accordance with Agency policy and Office of Management and Budget Circular No. A-110 requirements?

Finding: USAID/Philippines did not ensure that interest earned by recipients on cash advances were promptly remitted to USAID. The Controller's Office does not have procedures to track the interest earnings of recipients from USAID advances. Even when the recipients reported the interest, they did not identify the

period during which the interest was earned. Inconsistencies in the USAID handbook guidance also contributed to the problem of advances not being placed in interest-bearing accounts.

Recommendations:

2.1 Require the recipient to report the period for which the interest is derived;

2.2 Track the interest earned and follow up with the recipient when the interest has not been remitted; and

2.3 Incorporate mandatory terms for recipients to deposit USAID advances in interest-bearing accounts in all agreements.

Mission Response: The Mission does not agree with recommendations 2.1 and 2.2. We believe that implementing these recommendations will result in greatly increased workload without compensating benefits derived from the extra efforts. To address these issues, the Mission has incorporated additional audit steps in the RCA scope of work. These steps require the auditor to: (a) determine the amount of interest earned on USAID funds for the period under review; and (2) reconcile the amount derived against the amount reported and/or actually remitted to USAID. Any shortfall will be reported as a questioned cost. The Mission has requested recipients to implement these new procedures in all future RCA's. Shown in Attachment 1 are sample letters to recipients. We believe that the RCA approach is a more cost effective method that fully addresses the issue.

The Mission also does not agree with Recommendation No. 2.3. Appendix 4D of A.I.D. Handbook 13 details Standard Provisions for Non-U.S., Nongovernmental Grantees which are to be included in grants to foreign PVO's. Provision No. 1: Payment - Periodic Advance (June 1993) states requirements for grantees' handling of USAID funds. These are that "A.I.D. funds shall not be commingled..." and shall be deposited "...in a separate bank account." Neither the Handbook or Agency policy stipulates that non-U.S. grantees must deposit USAID funds into interest bearing accounts. The Mission encourages the use of interest-bearing accounts, but does not mandate such accounts given the Handbook guidance. USAID/Philippines believes that the Mission has complied with Agency requirements in this respect.

Attachment: Copy of letters to recipient organizations

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

USAID / Philippines
APO AP 96440

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JUL 27 1994

REPRESENTATION LETTER

AUDIT OF USAID/PHILIPPINES MANAGEMENT OF CASH ADVANCES TO RECIPIENT ORGANIZATIONS

Mr. Richard C. Thabet
Regional Inspector General for Audit/Singapore
U.S. Agency for International Development
APO AP 96534

Dear Mr. Thabet:

You have asked that USAID/Philippines provide a Representation Letter in connection with your audit of USAID/Philippines management of cash advances to recipient organizations. Your staff informed us that the audit covered advances to 38 recipients to whom advances were given during the period October 1, 1992 to December 31, 1993. These advances totalled $38 million, of which $7.9 million were mobilization advances to construction contractors and $4.6 million were advances to another federal agency (the U.S. Army Corps of Engineers) and some Philippine government agencies.

The audit was intended to answer the following audit objectives:

- Did USAID/Philippines limit cash advances to the immediate cash needs of recipients in accordance with USAID policy and U.S. Treasury regulations?

- Did USAID/Philippines ensure that recipients maintained cash advances in interest-bearing accounts and remitted the interest earned to USAID in accordance with Agency policy and Office of Management and Budget Circular Number A-110 requirements?

I have asked the offices concerned with the audit, particularly the Office of Financial Management, the Office of Regional Procurement, and the technical offices involved in managing the projects under which the cash advances were given (the Office of Voluntary Cooperation, the Office of Capital Projects, the Office of Population, Health and Nutrition, and the Office of Natural Resources, Agriculture and Decentralization), to make available to your staff all records in our possession for the purpose of the audit.

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They have assured me that all records in our possession have been made available.

In making the representations contained herein, we rely extensively on the audit reports of contracted private independent audit firms and USAID's Office of the Inspector General as a primary element of internal control to determine the compliance with applicable laws and regulations, and to ensure the accuracy of accounting and management information.

Based upon this reliance on audit, the representations made to me by my staff and their concurrence with the representations made herein, and in reliance on your office which has not informed me of any difficulty in obtaining records or information, or of any difficulty in obtaining the full cooperation of the various offices and staff involved, I confirm, as a layman and not as a lawyer, the following representations with respect to the audit of the Mission's management of cash advances to recipient organizations:

1. USAID/Philippines is responsible for: (a) the Mission's internal control system relating thereto; (b) the Mission's compliance with applicable U.S. laws, regulations, and the project agreements relating thereto; and (c) the fairness and accuracy of the Mission's accounting and management information relating thereto.

2. To the best of my knowledge and belief, USAID/Philippines has made available to RIG/A/S auditors all Mission record(s) related to the activities audited.

3. To the best of my knowledge and belief, Mission records relating to the activities audited are accurate and complete and give a fair representation as to the status of the activities audited.

4. To the best of my knowledge and belief, as a layman and not as a lawyer, USAID/Philippines is not aware of any known material instances where financial or management information directly relating to this audit has not been properly and accurately recorded, other than the findings in the draft report.

5. To the best of my knowledge and belief, as a layman and not as a lawyer, USAID/Philippines has made available information regarding any known material irregularities

related to the management of cash advances to recipients which we consider substantive, involving Mission employees with internal control responsibilities for the matter under audit or other organizations responsible for management of cash advances. For purposes of this representation, "irregularities" means the intentional noncompliance with applicable laws or regulations and/or intentional misstatements, omissions or failure to disclose.

6. To the best of my knowledge and belief, as a layman and not as a lawyer, USAID/Philippines is not aware of any known instance (other than what has been included in the draft audit report or reported by the Mission during the course of the audit) in which, in the Mission's judgment, there has been a material noncompliance by the Mission with USAID policies and procedures or violation of U.S. law or regulation, which would substantially impact upon the matter under audit.

7. To the best of my knowledge and belief, as a layman and not as a lawyer, USAID/Philippines is not aware of any known instance (other than what has been included in the draft audit report or reported by the Mission during the course of the audit) in which, in the Mission's judgment, there has been a material noncompliance by the Mission with the terms of the project agreement relating to the activities audited, which would substantially impact upon the matter under audit.

8. Following our review of your draft audit report and further consultation with my staff, I know of no other facts as of the date of this letter (other than those expressed in our enclosed Management Comments to the draft report) which, to the best of my knowledge and belief, would materially alter the conclusions reached in the draft report.

I request that this Representation Letter be included as part of the official management comments on the draft report and that it be published herewith as an Annex to the report.

Sincerely,

Thomas W. Stukel

Thomas W. Stukel
Director

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