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AUDIT OF
CASH ADVANCES TO PRIVATE VOLUNTARY
ORGANIZATIONS UNDER LETTERS OF CREDIT

AUDIT REPORT NO. 9-000-87-4

MARCH 25, 1987

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

Deputy
Inspector General

March 25, 1987

MEMORANDUM FOR AA/M, R. T. Rollis, Jr.

FROM: D/IG, James B. Durnil

SUBJECT: Audit of Cash Advances to Private Voluntary Organizations Under Letters of Credit

This report represents the results of audit of cash advances to Private Voluntary Organizations (PVOs) Under Letters of Credit. The audit objectives were to evaluate whether PVOs were maintaining cash advances in excess of immediate needs, and whether the PVOs' periodic reports required by OMB Circular A-110 conformed with Agency requirements and were supported by the PVOs' independently certified financial records. This subject matter had previously been covered in A.I.D. IG Report 82-73, May 25, 1982, "Excessive Cash Advances Are Costing the U.S. Government Over $2.5 Million In Interest Annually."

Audit results showed that the Office of Financial Management had made significant procedural improvements since the previous report. However, our audit found that the Agency still did not exercise effective control over letters of credit. There still existed large excess advances, control and accountability was inadequate, and two of five PVOs examined had diverted cash advances for unauthorized purposes. One of these two failed in December 1986 after its letter of credit was suspended, with a potential loss to the Agency of up to $1 million.

We have made three recommendations involving notifying all letter of credit recipients that they must fully comply with Agency requirements, enforcing full compliance after notification, and taking specific actions for improvement concerning two of the letters of credit.

Bureau for Management, Office of Financial Management comments were incorporated into this report and are included in full as Appendix A. Based on corrective action taken, all three recommendations will be considered closed on report issuance. I appreciate the cooperation and courtesy extended to my staff during the audit.

EXECUTIVE SUMMARY

The Department of the Treasury required that A.I.D. monitor its cash management practices to ensure that Agency cash was not being retained in excess of immediate disbursement needs. The Agency used letters of credit (LOC) to facilitate making cash available to nonprofit and educational organizations to finance Agency work. These organizations used LOCs to finance annual expenses of about $570 million. Of a total 240 organizations that use LOCs, eighty-five were private voluntary organizations (PVOs). The 85 PVOs reported they had $23.4 million in cash advances as of July 31, 1986.

The objectives of this financial and compliance audit were to evaluate whether PVOs were maintaining cash balances in excess of immediate needs, and to determine whether the PVOs periodic reports required by OMB Circular A-110 conformed with Agency requirements and were supported by the PVOs' independently certified financial records. The audit disclosed that:

PVOs were maintaining cash balances in excess of immediate needs. PVOs were permitted to report and carry excessive cash without effective intervention by the Office of Financial Management.

Ten PVOs reported cash balances of $19.7 million as of July 31, 1986, of which at least $6 million to $7 million represented excess cash on hand. About $2.9 million of the excess was returned in October 1986.

Periodic reporting by PVOs did not conform to requirements, thereby causing a serious breach in internal controls, as the Agency was unable to determine whether recipients were holding excessive cash. This factor contributed to two of the five PVOs examined diverting the funds for unauthorized purposes. These two PVOs were in financial difficulty as of November 30, 1986. In December 1986, one of these PVOs failed, with a potential loss to the Agency of up to $1 million.

Significant differences existed for two of five PVOs between the amount of cash outstanding as reported to A.I.D. and the liability for this debt as recorded in their financial records. Both PVOs reported to A.I.D. that they owed several hundred thousand dollars less than reported in their financial records.

In recognition of the importance of strong controls over LOCs, the Agency's Office of Financial Management (OFM)

Bureau for Management, made significant procedural improvements in its management of LOCs over the past several years. OFM had introduced a computerized management system to provide up-to-date information and analysis concerning each recipient's use of the LOC. OFM was also monitoring each requested cash drawdown, and temporarily denying many requests when periodic reports were not submitted timely or where other problems existed. Despite these changes, however, OFM still needed to make significant improvements in the management of the LOC system.

The A.I.D. Handbook requires that Federal cash advances not exceed amounts required for immediate disbursement needs related to Agency business and that LOC recipients periodically report on the status of cash advances. Our audit disclosed, however, that some LOC recipients were abusing the LOCs and not providing current and accurate financial information to A.I.D. As a result, (i) excess cash of at least $6 million to $7 million was maintained by A.I.D.'s PVO recipients, at an average loss of interest to the U.S. Government of about $0.5 million to $0.6 million annually; (ii) control and accountability was lost as PVOs were able to draw excessive balances and OFM was unable to determine when a problem existed; and (iii) two PVOs may be unable to return all of their advances that totaled about $1.7 million as of July 31, 1986, and other PVOs may also be in financial difficulty.

These results occurred because OFM had not required that periodic reports from recipients fully explain obvious excessive cash balances and had not taken aggressive action to collect excessive advances or to correct other apparent problems.

This report recommends that all LOC recipients be notified that they must fully comply with Agency requirements to (1) maintain minimum cash balances, (2) report disbursements on a timely basis, and (3) explain why excessive balances existed and cite actions underway to reduce such excesses. Also, appropriate action should be taken by Agency management to enforce full compliance by recipients of Agency requirements concerning LOCs and to make some specific corrective actions with regard to two LOCs.

Office of the Inspector General

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PART I - INTRODUCTION

A. Background

U. S. Government policy endorses making cash advances to nonprofit organizations so the organizations do not have to provide their own funds to finance U. S. Government work. About 240 nonprofit or educational organizations draw cash through commercial banks under Letters of Credit (LOC) to be reimbursed for expenses that totaled about $570 million during fiscal year 1985. Of the 240 LOC recipients, 85 are private voluntary organizations (PVOs). As of July 31, 1986, PVOs reported that $23.4 million in cash advances had been drawn under their LOCs.

A.I.D. policy requires that cash management practices of LOC recipients be monitored to ensure that Federal cash is not maintained in excess of immediate needs. Agency policy and grant agreements and contracts required recipients to draw cash only when actually needed to cover recent or anticipated disbursements. Further, drawing cash in excess of immediate needs may be cause for suspension or revocation of the LOC.

The A.I.D. Inspector General has issued three audit reports during the past five years that identified significant problems concerning Agency management over cash advances.

Prior Report Concerning Use of LOCs - Audit Report No. 82-73, "Excessive Cash Advances Are Costing the U.S. Government Over $2.5 Million In Interest Annually," May 25, 1982, stated that most A.I.D. LOC recipients were maintaining excess cash, thereby costing the U.S. Government about $2.5 million in interest annually. The report stated further that (1) interest was being earned on LOC cash advances, but not reported to A.I.D., (2) advances were used for non-A.I.D. business, (3) reporting of advance balance and utilization was untimely and inaccurate and (4) A.I.D.'s internal control over the LOC process was inadequate.

Prior Report Concerning Advances by Check - Audit Report 82-68, "Controls Over Cash Advances to Grantees and Contractors Are Lax," April 30, 1982, concerned cash advances made by check. The report stated that excess cash advances of as much as $5.3 million existed as of May 31, 1981, and that the Agency was not maintaining sufficient records to minimize such advances.

Prior Reports Concerning Advances by Missions - Audit Report 84-15, "Management of Cash Advances by A.I.D. Overseas Missions Needs Improvement," December 12, 1983, stated that as much as $73 million in excess advances could have been provided by overseas missions as of September 30, 1982, resulting in losses of up to $10.2 million in interest annually.

A.I.D.'s Office of Financial Management is responsible for monitoring and managing cash flowing to grantees under LOCs. The Office also is responsible for ensuring that U.S. Treasury funds drawn by grantees are the minimum needed to cover their operational needs.

The President's Council on Integrity and Efficiency has selected cash drawdowns by nonprofit organizations under LOCs for government-wide audit. This report summarizes A.I.D.'s part of that government-wide audit.

B. Audit Objectives and Scope

A financial and compliance audit was made of A.I.D.'s control over the use of LOCs by PVOs. The objectives of the audit were to evaluate whether PVOs were maintaining cash balances in excess of immediate needs, and whether the PVOs' financial reports required by OMB Circular A-110 conformed with Agency requirements and were supported by the PVOs' independently certified financial records.

The audit was made at the A.I.D. Bureau for Management and at five PVOs: American Institute for Free Labor Development, Catholic Relief Services, Cooperative League of the USA, Partnership for Productivity, and Volunteers in Technical Assistance. The five PVOs had $14.9 million of the $23.4 million reported outstanding by the 85 PVOs as of July 31, 1986. The first four named PVOs were selected because they reported large advances under the LOC. Volunteers in Technical Assistance was included because problems with its LOC discovered during a previous A.I.D. Inspector General audit were similar to some of the conditions encountered at the other four PVOs.

The audit reviewed administrative and financial records that concerned cash advances under letters of credit, as maintained by the Bureau for Management and by the PVOs. We examined recipient PVOs' cash drawdowns and reports for the current and prior fiscal periods, placing emphasis on the control and accountability over cash. Records reviewed covered the period January 1, 1985 through August 31, 1986.

The audit was limited to individual letters of credit. We did not examine records concerning the aggregate payments made by the Department of the Treasury to the Agency's LOC recipients, nor the records maintained by the Office of Financial Management to account for and control such aggregate payments. Further, the audit neither included a detailed review of the Agency's internal controls system concerning LOCs, nor relied on these systems in establishing the audit's scope. For the PVOs visited, we did confirm that the Office of Financial Management's records of LOC payments agreed with the PVOs' records of LOC receipts.

The audit fieldwork was made during the period August through October 1986 and the audit was made in accordance with generally accepted government auditing standards.

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PART II - RESULTS OF AUDIT

Management of cash and expenditures under Letters of Credit (LOC) did not adequately safeguard the Agency's interests. As reported in three prior audits and in this audit, the Agency had not exercised effective control over LOCs and was unable to determine when recipients draw cash excessive to their needs or divert cash for unauthorized purposes. Private voluntary organizations (PVOs) were permitted to draw, report and hold excessive cash over long periods of time without the Office of Financial Management (OFM) identifying and requiring either the return of excess cash or a change in procedures to report more accurate balances. As a result, ten PVOs reported cash advances as of July 31, 1986 of $19.7 million, far more than was needed to satisfy immediate disbursement needs. At least $6 million to $7 million of the $19.7 million represented excess cash on hand. About $2.9 million of the excess had already been returned by one of the PVOs; however, two PVOs are in financial difficulty and may be unable to return all of the cash. Savings of about $0.5 million to $0.6 million in interest annually could be achieved by requiring PVOs to report expenditures timely and taking aggressive action - including denying cash drawdowns and temporarily suspending letters of credit, as appropriate - if PVOs draw excessive cash balances. These actions would also prevent PVOs from having excess cash available that could be vulnerable to misuse, and thereby, reduce the government's risk of advancing cash that might not be available for return.

In addition, significant differences existed at two PVOs between the amount of cash advanced as reported to A.I.D. and the liability for this debt as recorded in the PVO's financial records. In both cases, the PVOs reported to A.I.D. the amount of cash advances was several hundred thousand dollars less than the amount recorded in the PVO's accounting records. When our auditors brought the discrepancy to one PVO's attention, the PVO acknowledged the discrepancy, revised the monthly reports to A.I.D. to reflect the correct amount owed, and stated it would repay the difference of about $217,000. When the IG auditors brought a similar discrepancy to the attention of another PVO, the PVO stated that its accounting records - although audited and certified by a certified public accounting firm - were erroneous and it actually owed a lesser amount than reported to A.I.D. (a difference of $321,794). An independent audit is required of the transactions concerning the latter PVO's letter of credit to ascertain the correct amount owed the U.S. Government.

The problems noted above appeared to involve relatively few of the 85 PVOs that used the letters of credit. Ten PVOs had reported about 84 percent of the total $23.4 million reported outstanding as of July 31, 1986. According to OFM records, 51 of the 85 PVOs cash advances represented less than five days of cash needs and 19 had 6 to 20 days needs. Thirty-six of the 51 with less than five days of cash used LOCs to reimburse themselves only after their own funds had been disbursed. The 36 PVOs expended about $6 million of their own cash as of July 31, 1986, for which they were due reimbursement.

Although the problems reported by A.I.D. IG Report 82-73 (page 2) still existed, OFM had made significant procedural improvements in its management of LOCs since 1982. OFM had introduced a computerized management system that provided it current information and analysis concerning the status of each recipient's LOC. The Office also monitored each cash draw requested by recipients - temporarily denying many of them - thereby providing it with a means of enforcing timely and accurate reporting. In reviewing OFM's procedures and controls, we concluded that more intense management over a small number of the LOCs reporting large cash advances would prevent most of the problems discussed herein.

This report recommends that all LOC recipients be notified that they must (1) fully comply with Agency cash advance requirements, (2) report disbursements on a timely basis and (3) explain why excessive balances existed and cite actions underway to reduce such excesses. Also, appropriate action must be taken by Agency management to enforce full compliance by recipients of Agency requirements concerning LOCs and to make some specific corrective action with regard to two LOCs.

A. Finding and Recommendations

Improper Use of Letters of Credit Resulted in Excessive Cash Drawdowns and Monetary Losses

The A.I.D. Handbook requires that Federal cash advances not exceed amounts required for immediate disbursement needs for Agency business and LOC recipients periodically report on the status of cash advances. Our audit disclosed, however, that some LOC recipients were abusing the LOCs and not providing current and accurate financial information to A.I.D. As a result, (i) excess cash of at least $6 million to $7 million was maintained by A.I.D.'s PVO recipients, at an average loss of interest to the U.S. Government of about $0.5 million to $0.6 million annually; (ii) control and accountability was lost as PVOs were able to draw excessive balances and OFM was unable to determine when a problem existed; and (iii) two PVOs may be unable to return all of their advances that totaled about $1.7 million as of July 31, 1986, and other PVOs may also be in financial difficulty. These deficiencies occurred because OFM had neither required that recipients fully explain apparent excessive cash balances in their periodic financial reports nor taken aggressive action to collect excessive advances.

Recommendation No. 1

We recommend that the Assistant Administrator, Bureau for Management, inform all A.I.D. recipients receiving advances under letters of credit, that they must immediately comply with the Agency's requirements concerning letters of credit. Specifically, OFM should inform recipients to:

a. Draw sufficient cash only to support immediate disbursement needs.

b. Report disbursements on a timely basis to permit accurate reporting of cash advances.

c. Provide detailed explanations for cash draws that exceed three days requirements for domestic uses and 30 days requirements for overseas expenditures. Such explanations should include information on the amount of average daily domestic and overseas disbursements, and

d. Provide a narrative explanation of actions to reduce excess balances of cash.

Recommendation No. 2

We recommend that the Assistant Administrator, Bureau for Management refuse advances or suspend or revoke letters of credit when recipients fail to draw, report and maintain cash balances sufficient to support only immediate disbursement needs.

Recommendation No. 3

We recommend that the Assistant Administrator, Bureau for Management, take the following additional specific actions with regard to the private voluntary organizations included in this review:

- Catholic Relief Services and the Cooperative League of the U.S.A. should be required to present a specific plan on how they will reduce the amounts of excess cash held.

- The Cooperative League of the U.S.A. should arrange for an audit that specifically addresses the difference between the amounts it owed A.I.D. as reported and as recorded in its internal financial records. The audit should include a written, independently certified opinion on the amount of the correct liability.

Discussion

The Department of the Treasury requires A.I.D. to monitor cash management practices to ensure organizations do not maintain cash in excess of their immediate disbursement needs. A.I.D. Handbook 19 requires that recipients make drawdowns as close as possible to the time of disbursement and maintain procedures that minimize the time elapsing between the transfer of funds and their disbursement.

The Agency used Standard Form (SF) 272, "Report of Federal Cash Transactions," to monitor cash advances and disbursements. Recipients used the form to report (1) cash on hand at the beginning of the period, (2) cash drawn from the Treasury and disbursed by the recipient during the period, and (3) cash on hand at the end of the period. According to A.I.D. Handbook 13, recipients were to explain advances in excess of three days' requirements in the hands of sub-recipients and the amount of cash advances in excess of 30 days' requirements for overseas sub-recipients. Recipients were also required to provide short narrative explanations of actions taken to reduce excess cash.

Grants and contracts between A.I.D. and PVOs require that recipient organizations commit themselves to drawing cash only when actually needed for disbursements and for timely reporting of cash used and balances on hand. Further, the agreements state that failure of recipients to adhere to these provisions may be cause for suspension on revocation of LOC.

OFM was responsible for managing the use of LOCs within the Agency. This office received the SF 272s and maintained a computerized system to record:

- Total drawdowns authorized by approved grants;

- Cumulative drawdowns against total authorized; and

- Net cash available for drawdown.

The system also computed the total number of days on hand as of any given date, based upon actual cash drawdown and expended according to recent SF 272s. A computer generated report was periodically prepared entitled Indication of Excess Cash.

The Department of the Treasury reports to A.I.D. all requests from LOC recipients for cash advances. OFM could deny requests by informing Treasury by 2 P.M. the following day that the advance should not be made. The cash drawdown is automatically approved unless specifically denied. OFM stated that it often refused advances in order to enforce timely reporting or when recipients requested excessive cash.

Indicators of Excess Cash - Both the SF 272 Reports and OFM's Indication of Excess Cash suggested there were problems with the Agency's LOC system. Ten PVOs reported advances as of July 31, 1986, of $19.7 million (Exhibit 1). In addition, OFM's indicator of excess cash balances - the number of days of cash on hand - also showed that PVOs maintained excessive advances. The following table reflects organizations having the following number of days of cash advances.

Number of Days of Cash Advances Maintained by A.I.D. PVOs Under Letters of Credit

Days Of Cash	Number of PVOs	Cash Reported as of 7/31/86
100 or more	8	$15.7 million
51 to 100	7	1.8 million
21 to 50	11	2.7 million
11 to 20	8	1.8 million
6 to 10	5	0.2 million
5 or less	46	1.2 million
	85	$23.4 million

The table shows that 30 to 40 percent of PVOs had excessive cash balances, or required careful monitoring to prevent their cash from becoming excessive. Twenty-six PVOs with more than 20 days on hand and 34 PVOs with more than 10 days had 86 percent and 94 percent, respectively, of the cash.

We selected four PVOs for detailed review based primarily on their large advances. The four had reported advances of $14.9 million (the correct figure was subsequently shown to be $15.3 million), and all had more than 100 days of cash outstanding. In addition to the four PVOs, we also reported on a fifth PVO's use of its LOC, based upon information obtained during another audit.

Apparent Problems Permitted to Exist - OFM permitted PVOs to report large cash balances without determining whether a significant problem existed. All five PVOs had reported large advances over an extensive period of time. Although OFM had queried the PVOs concerning the large balances, neither were written explanations obtained nor action taken to temporarily suspend or revoke LOCs even when evidence existed of significant problems. The following paragraphs discuss audit results at the five PVOs.

The Partnership for Productivity (PfP)

Despite evidence of problems, OFM did not take action to suspend PfP's use of the LOC. PfP cash advances almost doubled from April 1, 1985 to March 31, 1986. Upon query by OFM, PfP explained that much of the $932,432 advance as of March 31, 1986, was to pay for overhead costs spent in excess of the rate approved by A.I.D. The unauthorized funds were spent without indication from A.I.D. that the higher overhead rate would be approved and despite the fact that drawing cash for overhead that exceeded the approved rate was prohibited by the terms of PfP's grants.

OFM noted the increase in cash advances but efforts to control the LOC were ineffective. On April 25, 1986, OFM requested in writing the return of $378,157.

PfP did not return the excess funds. On the contrary, it dramatically increased its advance to $1,456,727 as of August 31, 1986, and withdrew an additional $870,000 in September and October, 1986. OFM took no action to prevent the additional drawdowns until early November 1986, when preliminary results of this audit were reported.

A.I.D. has had evidence for several years that PfP has had serious financial problems. A.I.D. Inspector General Audit Report 84-21, "Partnership for Productivity, International, Incorporated," February 22, 1984, reported that PfP was likely insolvent at December 31, 1983. PfP's own certified financial statements showed that it was insolvent on March 31, 1985. Our audit showed that, except for a gift of Zimbabwe dollars usable only in Zimbabwe, PfP remained insolvent as of August 31, 1986.

PfP's existence was perpetuated only because A.I.D. continuously advanced funds that PfP used for working capital, while never repaying the advance. Such use did not comply with the A.I.D. Handbook, which required that cash advances be used only to reimburse recipients for their immediate disbursement needs. Although cash drawdowns by PfP were suspended in early November 1986, after we reported preliminary results of the audit, OFM had not taken aggressive action to curtail continuously increasing cash advances to PfP.

Catholic Relief Services (CRS)

OFM permitted CRS to improperly draw very large cash advances. CRS' cash advance increased from $3,359,970 as of September 1, 1985, to $10,409,883 as of July 31, 1986. The audit showed that about $5.2 million of the cash was excess to CRS' needs (Exhibit 2). CRS returned $2.9 million of the excess in October 1986 as the result of our audit and agreed to reduce its future cash requests to eliminate the remaining excess balance.

OFM had evidence of the impropriety of CRS' large advances. The OFM indicator of excess cash (number of days of cash on hand) showed that CRS had 93 days of cash as of July 31, 1986 and 206 days as of September 10, 1986. Except for one month of exceptionally high expenditures, CRS was spending an average of about $1.3 million monthly, far less than the amount of cash being carried.

CRS had also previously improperly maintained large amounts of excess cash. A.I.D. Inspector General Report 82-73, May 25, 1982, in discussing CRS' LOC, stated:

> ". . . this organization is maintaining excessive FRLC cash on hand that amounts to $4 to $4.5 million dollars. These large cash balances in the U.S. and overseas represent several months of disbursements."

Despite clear evidence that CRS had excessive cash, OFM did not take action to halt continuing cash advances. OFM needed to more closely monitor CRS' drawdowns under its LOC, and take action to prohibit excessive balances.

Cooperative League of the U.S.A. (CLUSA)

A number of problems existed with CLUSA's use of the LOC.

- CLUSA reported large cash balances and understated on the SF-272 the actual amount outstanding.

- CLUSA's financial reports to A.I.D. on the status of cash advances differed significantly from the amount recorded in its financial records.

- About $246,000 of CLUSA's cash advances were excess to its needs (Exhibit 3).

- CLUSA was earning interest on some of this excess cash but not returning it to the U.S. Government.

CLUSA's monthly cash reports significantly understated cash advances. CLUSA reported only those advances that it had provided its employees and overseas offices, and neglected amounts that pertained to general operating funds maintained in Washington. The under-reporting caused significant distortions, as follows:

Month Ending	Amount Reported to A.I.D.	Amount That Should Have Been Reported	Amount Under-Reported
July 31, 1986	$1,005,854	$1,439,226	$433,372
August 31, 1986	743,253	1,419,183	675,930
September 30, 1986	856,718	1,256,443	399,725

Although CLUSA's quarterly reports reflected actual amounts outstanding at the end of each quarter, the distorted, incomplete interim reports seriously limited OFM's ability to monitor CLUSA's use of its LOC. OFM knew of the reporting deficiency, but did not require CLUSA to report correctly.

There was also a difference between CLUSA's record of the liability as reported to A.I.D. and the amount reflected in its accounting records, as shown by the following:

Month Ending	Amount Reportable to A.I.D.	Liability Per CLUSA's Internal Records	Amount of Advance Under-Reported
December 31, 1985	$ 273,856	$ 595,150	$321,294
July 31, 1986	1,439,326	1,816,070	376,744

The liability as of December 31, 1985, represents the amount as audited by CLUSA's independent auditors who, in the annual financial statements as of that date, stated that the liability as recorded represented fairly CLUSA's financial position.

CLUSA's auditors certified the accuracy of accounting records showing CLUSA owed $595,150, nevertheless, CLUSA's personnel stated that its records were incorrect and that the $273,856 as reported to A.I.D. was accurate. A certified audit of CLUSA's books and financial reports to A.I.D. is needed to reconcile these documents and ensure that CLUSA doesn't owe A.I.D. $321,294 more than reported.

About $246,000 of CLUSA's advance represents excess funds (Exhibit 3) that should be returned or used before additional drawdowns are made. In addition, CLUSA had deposited some of the advances in interest-bearing money market accounts without reporting the interest earned. A total of $700,000 of the $4,050,000 drawn for the seven months ending July 31, 1986, was deposited initially into the money-market account. Although the funds were not retained there long and the interest earned was not significant, CLUSA's activities were improper. CLUSA should return the interest previously earned and report future interest earned to A.I.D.

American Institute for Free Labor Development (AIFLD)

AIFLD has consistently reported very large cash balances when in fact there was little or no cash on hand. AIFLD was paying expenses on a current basis, but not recording them for several months. Although AIFLD had paid the bills and no longer had the cash, it was unwilling to report the expenditures to A.I.D. until it had ensured that all expenditures were appropriate.

As a result, AIFLD's reports vastly overstated available cash. Its reports showed that it routinely had cash advances from $2 million to $4 million when, in fact, AIFLD was advancing its own funds to support A.I.D. grants.

AIFLD reporting procedures meant that OFM could not effectively monitor AIFLD's LOC. OFM's files showed that in March 1986 it had refused a drawdown request by AIFLD because reports showed it already had large cash advances. OFM resumed the drawdowns when AIFLD explained that it didn't have the funds. Although AIFLD in fact did not have the funds, OFM resumed cash drawdowns without first confirming that AIFLD's statement was accurate.

A.I.D. Handbook 19 requires timely submission of SF 272 to provide a basis for determining whether recipients have drawn excess cash. According to Handbook 19, frequent reporting inaccuracies are grounds for suspension of the LOC. AIFLD's reports, however, violated both the timeliness and accuracy reporting requirements of Handbook 19. AIFLD should change its accounting procedures to permit timely and accurate reporting, or be subject to suspension of its LOC.

Volunteers in Technical Assistance (VITA)

Two significant problems existed in VITA's use of the LOC. Vita made errors in its monthly reports that resulted in its improperly reducing the amount of its debt by about $217,000. Secondly, VITA used the excess funds drawn from A.I.D. to support its other business operations. The diversion was the result of other donors not providing matching funds and a deteriorating financial condition that encouraged the use of funds for purposes not related to A.I.D. grants and contracts.

Impact of Reporting Excess Balances - The above five PVOs all reported excessive cash balances. Four PVOs actually had too much cash; however, two of the four had utilized the cash for purposes other than intended, and were now required to return the excess. In summary, the audit results showed that (i) the Agency's PVOs had excess cash of at least $6 million to $7 million, (ii) there was a serious breach in internal controls as OFM had lost control over the LOC cash advances and (iii) A.I.D. may lose funds as two PVOs were having financial difficulty and may be unable to return all of the cash to the U.S. Government.

Excess Cash. Two of the five PVOs had excess cash totaling $5.4 million of the total $14.9 million that the five reported to A.I.D. as of July 31, 1986 (Exhibits 2 and 3). Based upon these results, we projected excess cash for the Agency to be at least $6 million to $7 million. Based upon a current interest rate of eight percent, the excess cash of $6 million to $7 million resulted in loss of interest to the U.S. Government of $500,000 to $600,000 million annually.

Loss of Control. A serious breach in internal control occurred, as the Agency had effectively lost control over cash advances drawn by PVOs under their LOCs. PVOs could maintain large advances and use for inappropriate purposes because OFM did not require that recipients accurately report and maintain minimum amounts of cash. OFM's lax monitoring of the LOCs thereby contributed to two of the five PVOs visited using cash advances inappropriately.

- PfP had used the cash to provide a cushion of working capital that permitted it to avoid bankruptcy. It also used the cash to finance an overhead rate that was 46 percent higher than approved by A.I.D. and for work that had not been approved by A.I.D.

- VITA had also diverted cash drawn under the LOC to provide working capital that it used to finance other business interests.

Both cases illustrate a significant internal control deficiency that permitted recipients to draw cash even when excessive amounts were reported.

Inability to Return Advances. PfP did not have sufficient funds to reimburse A.I.D. for the excessive advances. In November 1986 OFM suspended PfP's LOC in order to protect the U. S. Government from further potential loss. At a meeting between Agency and PfP on November 20, 1986, PfP stated that approximately one week of operating cash existed and Agency forbearance was required to avoid imminent failure. On December 16, 1986, the Agency terminated its cooperative agreement with PfP, and on December 23, 1986, the Cooperative for American Relief Everywhere (CARE) agreed to take over PfP's overseas program and repay up to $500,000 of PfP's liability owed A.I.D.

VITA was also unable to immediately repay excess cash overdrawn and was operating under an agreement to repay the overdrawn funds. On September 17, 1986, the Agency formally agreed to continue VITA's funding, subject to its repayment of the $328,286 advance outstanding at the end of July 1986. VITA was to pay its own expenses under the grant until the outstanding advance had been liquidated. As of November 30, 1986, VITA appeared to have improved its financial management and was optimistic that it could repay the advance.

Reasons for Cash Management Problems - Cash management problems occurred because periodic reports by LOC recipients to OFM did not accurately reflect their cash position and requirements, and because OFM was not sufficiently aggressive in getting accurate information or in collecting excessive advances.

A.I.D. Handbook 13 requires that SF 272 be used to provide information to monitor cash advances. Among other information, the SF 272 should report the amount of cash advances in excess of targeted needs and state actions underway to reduce excessive balances. LOCs may be suspended for frequent reporting inaccuracies.

OFM has not required that the above procedures be followed. None of the hundreds of Form 272s that we examined either report the amount of cash advances in excess of requirements or included a narrative explanation of actions underway to reduce excessive advances.

Moreover, the audit showed that the reports were often inaccurate. For example:

- The disbursement information reported by AIFLD significantly underestimated disbursements to date.

- Except on interim reports, CLUSA did not accurately report either cash advance balances or monthly disbursements.

- VITA lost accountability over $217,000 through inaccurate reporting.

As a result, OFM could not rely on the reports to determine whether recipients were drawing excess cash. OFM could neither determine how much cash the recipients actually had nor how much was needed. Improved reporting is a prerequisite to provide the basis for OFM to ensure that recipients maintain advances commensurate with their needs.

The second cause for the problems was that OFM was not taking sufficient action to ensure that recipients complied with requirements, even when it knew a problem existed. OFM did not require that recipients improve their reporting or return excessive cash. For example:

-- OFM knew for at least six months that PfP was drawing cash inappropriately but did nothing to suspend drawdowns until interim results from this audit were available.

-- Over a period of a year, OFM permitted CRS to increase its advances to over $10 million without demanding an explanation.

-- OFM was aware that AIFLD was submitting reports that effectively prevented OFM from monitoring the LOC, yet took no action to require current information.

OFM has not fully carried out its responsibilities to ensure that funds drawn by grantees are the minimum needed to cover recipients' immediate operational requirements. OFM had not enforced full reporting of periodic information it needed to monitor the LOCs and has allowed some recipients to report large cash balances, thereby contributing to serious misuse of the LOCs. Significant improvements could be made by (i) informing recipients that continued use of LOCs were dependent upon complete and accurate reporting, and (ii) by requiring recipients to report cash balances that did not exceed a few days' requirements, and demanding explanations or return of cash that exceeded a few days' requirements.

Management Comments

The Bureau for Management concurs with Recommendation No. 1, and are sending letters to each LOC recipient reminding them of the Agency's cash management and reporting requirements.

Office of Inspector General Comments

The action taken by the Bureau for Management is responsive to the recommendation.

Management Comments

The Bureau for Management concurs with Recommendation No. 2, and promises to take more aggressive action to enforce recipients' compliance with Agency requirements when warranted.

Office of Inspector General Comments

The action taken by the Bureau for Management is responsive to our recommendations.

Management Comments

The Bureau for Management concurs with Recommendation No. 3, and promises to initiate the necessary steps to implement it.

Office of Inspector General Comments

The action taken by the Bureau for Management is responsive to the recommendation.

B. Compliance and Internal Control

As discussed in Section A, there existed a serious internal control deficiency in that the Agency had effectively lost control over cash advances drawn by PVOs under the LOCs (see page 14).

AUDIT OF
CASH ADVANCES TO PRIVATE VOLUNTARY
ORGANIZATIONS UNDER LETTERS OF CREDIT

PART III - EXHIBITS AND APPENDICES

EXHIBIT 1

Private Voluntary Organizations
Reporting Large Cash Advances
(As of July 31, 1986)

Private Voluntary Organization	Cash Reported on Hand as of July 31, 1986
Catholic Relief Services	$10,409,883
American Institute for Free Labor Development	2,064,266
Partnership for Producrivity	1,422,030
Planned Parenthood Foundation of America	1,388,060
International Planned Parenthood Foundation West	1,012,323
Cooperative League of the U.S.A	1,005,854
Cooperative Housing Foundation	686,097
Mercy Corps International	593,514
Save the Children Foundation	554,483
Credit Union National Association	531,364
	$19,667,874

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Excess Cash - Catholic Relief Services (CRS)

Introduction. CRS financed 53 A.I.D. grants under its LOC. Cash advances for the grants were based upon requests from personnel responsible for implementing the individual grants. CRS headquarters in New York accumulated requests for cash for several grants and then requested a single LOC drawdown that combined the individual requests. Once the funds were received, CRS headquarters deposited them in dollar and/or local currency accounts set up for each grant.

Amount of Excess Cash. CRS held about $5.2 million of excess U.S. Government cash as of December 31, 1985, and this amount probably increased since then. Twenty CRS grants represented $9.8 million of the total $10.4 million of cash outstanding as of July 31, 1986. These amounts are overstated by an unknown amount, as expenses had been paid but had not yet been extended into the accounting records. The same 20 grants had $5.1 million of the total $5.6 million outstanding as of December 31, 1985, at which time all expenses had been posted to the appropriate accounts.

Amounts of cash on hand often greatly exceeded monthly disbursements. The following shows the months of cash on hand and the amount of excess cash for the grants having the largest advances as of December 31, 1985.

Grants	U.S. Government Cash as of 12/31/85	Months of Cash*	Amount of Excess U.S. Government Cash
4152 Ethiopia	$1,815,611	2.5	$1,815,611
2017 Italy	405,654	7.8	350,000
3009 Italy	298,920	13.2	275,000
4098 Ethiopia	429,754	16.6	350,000
5123 Jerusalem	369,400	4.4	280,000
4114 Haiti	357,658	17.1	357,658
5068 Ethiopia	257,234	1045.7	250,000
3164 Latin America	254,766	3.1	240,000
4204 Tanzania	245,949	5.7	245,949
3151 Tanzania	235,617	5.9	235,617
5043 Haiti	108,897	3.0	70,000
0270 Togo	105,349	5.4	105,349
Total	$5,147,065		$4,775,184

*Based upon average 1985 monthly expenses

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Excess Cash - Catholic Relief Services (CRS) Cont'd

The table shows that advances as of December 31, 1985 were several times average monthly disbursements experienced during 1985. Further, the number of months of cash generally increased during 1986 as cash advances increased from $5.6 million to $10.4 million.

Due to the large ratio of cash advances to monthly disbursements, we examined cash advances for several grants to determine whether the balances carried as of December 31, 1985 were excessive. For the 20 grants examined, we determined that about $4,775,184 of the $5,147,065 (92.8 percent) on hand as of December 31, 1985, was excess to CRS' needs, and should have been returned. Based upon this experience, we estimated that CRS had additional excesses of about $415,857 for the grants not examined 1/ for total excesses of $5,191,104, or $5.2 million. Summaries of our analyses for each grant follow:

Ethiopia Grant 4152. Funding requirements for this grant were overestimated and $1,815,611 remained unexpended when the grant expired on December 31, 198_. Accounting adjustments between Ethiopia Grant 4152 and Ethiopia Grant 5701 after December 31, 1985 resulted in the on-hand balance for Grant 4152 being increased to $3,077,323 as of July 31, 1986. CRS had not returned the funds for this grant because it believed that the grant would be renegotiated and the funds applied to the new grant. As a result, CRS maintained between $1.8 million and $3.1 million that should have been returned when the grants expired.

Italian Grant 2017. CRS has maintained excessive balances for this grant. The balances as of December 31, 1985 and July 31, 1986 was $811,307 and $380,194, respectively, of which half belonged to A.I.D. and half to CRS. Large balances built up because the CRS director in Italy requested large, intermittent withdrawals of cash. For example, $453,379 was advanced in late July 1985, after which no subsequent advances were made until November 1985. Drawdown requests for advances were supported by very general statements that did not consider cash already available.

1/ $5,595,107 total on hand as of 12/31/85, less $5,147,065 on hand for the 20 grants examined = $448,122 x .928 (percent of funds excess) = $415,857.

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Excess Cash - Catholic Relief Services (CRS) Cont'd

Monthly disbursements for this grant averaged only $103,054 during 1985. Therefore, allowing 30 days of cash as of December 31, 1985, CRS had on hand about $700,000 of excess cash for this grant, of which $350,000 belonged to A.I.D.

Italian Grant 3009. CRS maintained excessive balances for this grant. Monthly expenditures averaged $45,274 and $25,781 during 1985 and 1986, respectively, compared with a total A.I.D. and CRS cash balance as of December 31, 1985 and July 31, 1986 of $597,840 and $742,372. Based upon the 1985 rate of expenditure, about $550,000 of the December 31, 1985 balance was excessive, of which $275,000 belonged to A.I.D.

Italian Grant 2020. This grant was similar to the preceding two Italian grants. The balance as of December 31, 1986 of $524,513 compared with average monthly 1985 disbursements of $120,209, was excessive by at least $400,000. Of the $400,000, half belonged to A.I.D.

Ethiopian Grant 4098. Disbursements averaged $25,795 monthly during 1985 compared with an advance of $429,754 at the end of the year, of which at least $350,000 was excessive.

Jerusalem Grant 5123. This grant built up excessively large advances beginning in August 1985. Drawdowns totaling $702,436 were made between the middle of August 1985 and the end of December 1985, when the cash advance was $369,400. No further drawdowns were made for this grant until August 1986. Disbursements averaged only $83,258 per month during 1985; therefore, at least $280,000 of the above cash advance was excessive.

Haiti Grant 4114 and Mauritania Grant 3151. The total amount of these two advances as of December 31, 1985, $357,658 and $235,617, respectively, was excessive, as the grants expired on that date. Although the grants were subsequently extended to March 30, 1986, additional disbursements were minor. Further, amounts available as of December 31, 1985, should all have been returned until the amount needed to support immediate disbursement needs was determined.

Excess Cash - Catholic Relief Services (CRS) Cont'd

Ethiopia Grant 5068. About $250,000 of the total advance of $257,234 was excess. This grant averaged monthly disbursements during 1985 and 1986, respectively, of only $246 and $10,504.

Tanzania 4204. The entire balance as of December 31, 1985 was excess. The balance of $245,949 existed because CRS' Director in Tanzania wanted to spend all amounts available before the grant expired. He cabled CRS headquarters on September 22, 1985, and requested deposit of all remaining funds under the grant in Tanzania's dollar account, before the grant expired on September 30, 1985. The planned last-minute purchases were never made and the funds remained virtually intact for over a year until our visit in October 1986.

Haiti 5043. At least $70,000 was excess. The December 31, 1985 balance of $108,897 was three times the 1985 average disbursements of $36,686.

Togo 0270. The entire balance as of December 31, 1985, when the grant expired was excess. Funds remaining under the grant were reserved for a construction project. However, the funds were not required until the summer of 1986. The remaining funds should have been returned to A.I.D. until needed.

Excess Cash - Cooperative League of the U.S.A. (CLUSA)

Introduction

CLUSA had cash on hand to support requirements in Guatemala, India, Rwanda, Indonesia, Equatorial Guinea, Niger and Haiti. CLUSA maintained both a dollar account in Washington and local currency accounts in each of these countries. The Washington accounts were used primarily to replenish the local currency accounts.

Amount of Excess Cash. CLUSA held about $246,000 of excess U.S. Government cash as of December 31, 1985.

As of December 31, 1985, the balances in accounts used to support CLUSA overseas operations were:

Country	Local Currency Account	Washington Account	Total
Haiti	Unknown	$ 9,000	$ 9,000
India	47,669	19,314	66,983
Indonesia	42,314	7,513	49,827
Rwanda	(19,523)	84,937	65,414
Niger	52,373	21,424	73,797
Equatorial Guinea	63,911	(17,762)	81,673
	$186,744	$159,950	$346,694

Analysis of CLUSA's 1986 transactions through July 31, 1986, shows that the amounts carried in these accounts were far more than needed. Average monthly disbursements for CLUSA's operations in the above five countries averaged $157,421 monthly. The Washington accounts, which could be replenished with drawdowns under the LOC within two days, alone averaged about $169,000 on hand throughout 1986. These Washington accounts should be reduced to a maximum balance of about a three days cash, or about $16,000. Therefore, about $153,000 of the amount carried throughout 1986 in CLUSA's Washington accounts for its overseas offices was excess.

Excess Cash - Cooperative League of the U.S.A. (CLUSA) Cont'd

Some of the local currency accounts also appeared to carry excessive balances. All the accounts except Rwanda and Equatorial Guinea appeared to be carrying several times the monthly disbursements experienced in these countries. At least half, or about $93,000, on hand in the overseas accounts as of December 31, 1985, was excess.

Combining the amounts as estimated in the above two paragraphs, we estimated that at least $246,000 of the accounts carried by CLUSA in support of its overseas operations was excess and should be returned.

AGENCY FOR INTERNATIONAL DEVELOPMENT

WASHINGTON, D.C 20523

ASSISTANT TO THE ADMINISTRATOR
FOR MANAGEMENT

17 FEB 1987

MEMORANDUM FOR IG/PSA, William C. Montoney

FROM: AA/M, R. T. Rollis, Jr.

SUBJECT: Audit of Cash Advances to Private Voluntary Organizations Under Letters of Credit

REFERENCE: Your Memorandum Dated January 27, 1987

Thank you for the opportunity to comment on the subject draft report. We have reviewed the three recommendations made in the report and agree to take the recommended actions. Specifically, M/FM/PAFD will send a letter to each Letter of Credit (LOC) recipient reminding them of the Agency's cash management and reporting requirements (Recommendation No. 1). M/FM/PAFD will begin to take more aggressive action to enforce compliance with these requirements when warranted (Recommendation No. 2). M/FM/PAFD will initiate the steps required to implement the specific actions in Recommendation No. 3 related to Catholic Relief Services and the Cooperative League of the USA. Based on the preceding we request that you close all three recommendations.

While we agree that implementation of the report's recommendations should result in improved management of the funds advanced to PVOs under the LOC method of financing, we do not agree that there has been a serious breach in internal controls or that M/FM has lost control over LOC advances as stated in the report on pages ii, 10, 24 and 30. As noted on page 8 of the report, the problems identified involve relatively few of the 85 PVOs using the LOC. On the same page you concluded that "more intense management over a small number of the LOCs reporting large cash advances would prevent most of the problems." To expand on these statements, the 85 PVOs covered by this report drew almost $290 million from their LOCs in FY 1986. Given excess cash on hand by 10 of the PVOs of $6 to $7 million, then less than 2.5% of the total drawn in FY 1986 is considered as excess. We do not believe that excess cash advances of only 2.5% results in a serious breach in internal control or in the loss of control over LOC cash advances, especially when dealing with organizations with overseas offices and the difficulties in getting timely reporting of overseas expenditures. We suggest that you modify the report to more accurately describe the materiality of the findings.

We appreciate the credit given M/FM for the improvements made in the management of the LOCs since 1982. Given the limited staff resources we have available to perform these functions, we believe that we have made significant improvements. With the implementation of the recommendations in this report and changes we are planning for our automated systems we hope to continue to improve our management of this important activity.

We will provide you with copies of our correspondence related to the implementation of Recommendations 1 and 3. Please call Elmer Owens on 632-0066 if you have any questions about our comments.

LIST OF RECOMMENDATIONS

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Recommendation No. 1 6

We recommend that the Assistant Administrator, Bureau for Management, inform all A.I.D. recipients receiving advances under letters of credit, that they must immediately comply with the Agency's requirements concerning letters of credit. Specifically, OFM should inform recipients to:

a. Draw sufficient cash only to support immediate disbursement needs.

b. Report disbursements on a timely basis to permit accurate reporting of cash advances.

c. Provide detailed explanations for cash draws that exceed three days requirements for domestic uses and 30 days requirements for overseas expenditures. Such explanations should include information on the amount of average daily domestic and overseas disbursements, and

d. Provide a narrative explanation of actions to reduce excess balances of cash.

Recommendation No. 2 7

We recommend that the Assistant Administrator, Bureau for Management refuse advances or suspend or revoke letters of credit when recipients fail to draw, report and maintain cash balances sufficient to support only immediate disbursement needs.

LIST OF RECOMMENDATIONS

Page

Recommendation No. 3 7

We recommend that the Assistant Administrator, Bureau for Management, take the following additional specific actions with regard to the private voluntary organizations included in this review:

- Catholic Relief Services and the Cooperative League of the U.S.A. should be required to present a specific plan on how they will reduce the amounts of excess cash held.

- The Cooperative League of the U.S.A. should arrange for an audit that specifically addresses the difference between the amounts it owed A.I.D. as reported and as recorded in its internal financial records. The audit should include a written, independently certified opinion on the amount of the correct liability.

APPENDIX C

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