

AUDIT OF
USAID/INDONESIA'S
POLICY AND PROCEDURES FOR
REVIEWING UNLIQUIDATED OBLIGATIONS

Audit Report No. 2-497-89-04
November 10, 1988

UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT
REGIONAL INSPECTOR GENERAL/AUDIT
MANILA

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MANILA, PHILIPPINES

November 10, 1988
RIG/EA-89-47

MEMORANDUM

TO: David N. Merrill
Director USAID/Indonesia

FROM: *William C. Montoney*
William C. Montoney, RIG/A/M

SUBJECT: Audit of USAID/Indonesia's Policy and Procedures
for Reviewing Unliquidated Obligations
Audit Report No. 2-497-89-04

This report presents the results of audit of USAID/Indonesia's policy and procedures for reviewing unliquidated obligations. The draft report was submitted to you for formal comment. Your comments were considered in finalizing this report and are attached. The report contains one audit recommendation which requires your action. Please advise us within 30 days of the actions planned or taken to close the recommendation.

I appreciate the cooperation and courtesy extended to my staff during the audit.

Background

The Inspector General's Office of Programs & Systems Audits (IG/PSA) conducted a Centrally Directed Audit to determine the adequacy of A.I.D.'s policy and procedures for reviewing unliquidated obligations. The audit was a comprehensive review of the Agency's policy and procedures for applying Section 1311 of the Supplemental Appropriations Act of 1955 (31 U.S.C. 1501) which requires agencies to certify that unliquidated obligation balances are needed at the end of each fiscal year.

IG/PSA requested that each Regional Inspector General (RIG) audit one Mission in its respective region to determine the adequacy of the policy and procedures for reviewing

unliquidated obligations and issue a report--whether the results were positive or negative--to the Mission audited. IG/PSA was to prepare a capping report based on the reports issued by the RIG's.

RIG/A/Manila selected USAID/Indonesia for the review as this Mission had one of the most active programs in the region. The Missions program objective was to develop a foundation which would provide for a significant expansion of the Indonesia Government's capacity to use its own financial resources, and those of foreign donors, in meeting the basic needs of the rural population relating to the areas of employment, food, health, family planning, energy, and education. To support this objective, the USAID/Indonesia Mission had a staff of approximately 42 U.S. direct hire employees and about 140 foreign service national direct hires and contract personnel. The annual operating expense budget was approximately \$4.8 million with a development assistance pipeline of approximately \$280 million consisting of 58 active and inactive projects. In addition, the Mission was responsible for a local currency trust fund equivalent to about \$650 thousand.

Audit Objectives and Scope

The objective of this financial and compliance audit was to evaluate the adequacy of USAID/Indonesia's policy and procedures for applying Section 1311 of the Supplemental Appropriations Act. More specifically, the audit was to determine whether the Mission had adequate internal controls to prevent the Mission from: (1) preparing inaccurate and incomplete reports on unliquidated obligations, (2) failing to deobligate funds promptly, (3) reprogramming funds without proper review and authorization, (4) failing to comply with applicable laws and regulations, and (5) exposing Agency funds to fraud, waste or abuse. The audit was limited to review of the obligation accounting controls and did not include a review of disbursement accounting controls.

A sample was taken of USAID/Indonesia's unliquidated obligations and the related supporting documents were examined to determine if the Agency's policy and procedures were being implemented, to evaluate the effectiveness of these controls, and to assess the need for the unliquidated balances. The sample was drawn from each of the two categories of obligations: operating expenses and project assistance. The sample size was determined by identifying total unliquidated obligations in each category as of September 30, 1987 and selecting a judgmental sample of each category. For operating expense, total unliquidated obligations were about \$486,000. The sample included 39 or

15% of the 257 unliquidated balances. For project accounts, total unliquidated obligations were about \$280 million for 58 active and inactive projects. This sample included 32 of these projects.

All work was performed at USAID/Indonesia during July 1988. Interviews and discussions were held with the Mission Director, Deputy Mission Director, Controller personnel, Program Office personnel, and Project Officers. The audit was made in accordance with generally accepted government auditing standards for financial and compliance audits.

Results of Audit

USAID/Indonesia's policy and procedures for reviewing unliquidated obligations were generally adequate; however, management controls were not in place to assure that the staff followed the Mission's policy and procedures. USAID/Indonesia did not accurately report its unliquidated obligations at fiscal year end 1987. About \$1.9 million in unliquidated obligations, which could have been deobligated, were certified as needed by the USAID. USAID/Indonesia did not take prompt action to deobligate unliquidated obligations which were no longer needed for the original purpose. Nothing came to our attention during the audit of internal controls that would indicate that USAID/Indonesia was not in compliance with other applicable laws and regulations or it was vulnerable to loss of Agency funds.

In March 1988, USAID/Indonesia performed an intensive review of the unliquidated obligations in its projects and reviewed the policy and procedures for reviewing unliquidated obligations. The Mission initiated actions to assure that most of the existing policy and procedures were followed. However, additional actions were needed to assure more accurate reporting of obligations and more timely deobligation of unneeded funds.

1. Certain Obligations Were Not Reported Accurately - As of September 30, 1987, 29 of the 32 project accounts reviewed had unliquidated obligations totaling \$1.9 million which could have been deobligated. USAID/Indonesia had reported and certified these obligations as needed as of that date. Therefore, the report was not in compliance with Section 1311 of the Supplemental Appropriations Act. This occurred because the USAID lacked management controls to assure full implementation of Agency procedures for conducting fiscal year-end reviews of unliquidated obligations. Consequently, these funds were not made available for other purposes or returned to the U.S. Treasury in a timely manner.

Discussion - Section 1311 of the Supplemental Appropriations Act of 1955 (31 U.S.C. 1501) is the legal requirement for reporting and retaining documentary evidence of United States Government obligations. It provides the following:

"An amount shall be recorded as an obligation of the United States Government only when supported by documentary evidence of a binding agreement ... that is in writing, in a way and form, and for a purpose authorized by law; and executed before the end of the period of availability for obligation of the appropriation or fund used for specific goods to be delivered, ... or service to be provided ...".

A.I.D. Handbook 19, Financial Management, provided guidance on how the USAID was to comply with this law. It stated that each mission should have unliquidated obligation balances under continuous review. A special intensive review should be conducted at each mid-fiscal year of all unliquidated obligations. The timing of this review was cited as especially important to the A.I.D. planning process since resulting deobligations of prior-year funds could be reported to permit timely reallocation and orderly reobligations prior to the fiscal year end. A final review of unliquidated obligations was to be made at each fiscal year end to assure that recorded obligations were needed for the Agency Controller certification under the provisions of Section 1311 (31 U.S.C. 1501). The reports and certifications were to be supported by records maintained at each Mission in a manner which facilitates audit and reconciliation.

Handbook 19 also states that each obligating document having an unliquidated balance, along with the related supporting documents, should be examined to determine the need for the unliquidated balance. When all the goods, services, or training under the obligating document has been received, any unliquidated balance in excess of the amount required to provide for the goods delivered and services performed for which payment had not been made should be deobligated. For project assistance, the Project Assistance Completion Date (PACD) provided a positive reference point for concluding A.I.D. assistance. The PACD establishes a date whereby A.I.D. will not issue or approve documentation which authorized services to be performed or goods to be furnished after this date. Amounts obligated which were not needed to pay for goods and services delivered by the final PACD were to be considered unneeded.

Twenty-nine of the 32 projects reviewed were found to have unneeded unliquidated obligations that could have been deobligated or reprogrammed. Twenty-five of these accounts

were for terminated projects. The oldest of these accounts had a PACD of December 30, 1980; the most recent account had a PACD of August 31, 1987. The unneeded amounts ranged from \$1 to \$298,000 (See Exhibit 1). Of the seven active projects, six had unneeded funds ranging from about \$1,500 to about \$170,000.

The Mission Controller had certified and reported as needed about \$280 million in project obligations at fiscal year end 1987 on the U-101 report (Summary of BPC Ledger Transactions and Reconciliation with Disbursing Officer's Account). However, this report included the \$1.9 million of unneeded obligations which could have been deobligated. Thus, as of September 30, 1987, the Mission submitted an inaccurate report on unliquidated obligations because existing policy and procedures were not being fully implemented.

The Mission's controller staff advised us that the 1987 fiscal year-end Section 1311 review for project assistance was not conducted. The staff said that they generally relied on the Program Office to review the pipeline and to inform them of amounts that should be deobligated. However, a discussion with Program Office personnel disclosed that they only reviewed large amounts, \$50,000 or more, which would be worthwhile for reobligating. Responsibility for determining which funds were unneeded and for deobligating these funds was not clear to USAID/Indonesia personnel.

The Mission's Program Office personnel stated that the Office of Management Budget's requirement to deobligate unneeded obligations and to reobligate them within the same fiscal year was another reason for not properly reporting and not promptly deobligating and reobligating (deob/reob) unneeded obligations. Since the deob/reob process takes several months for approval, there often was not enough time left in the fiscal year to deobligate and obtain the approval to reobligate these funds. Thus, there was a tendency to wait until the start of the next fiscal year before initiating deobligation action. Mission personnel believed that the removal of this requirement to deobligate and reobligate within the same fiscal year would avoid inaccurate reporting of obligations in some cases.

In November 1987, the Mission took steps to improve implementation of its fund controls by establishing a Pipeline Reduction Task Force. One of its specific tasks was to identify project assistance funds available for deobligation. On March 31, 1988, an intensive review of all projects in the Mission portfolio was completed. Approximately \$8.2 million of obligations were identified for possible deobligation.

USAID/Indonesia officials agreed that clarification of responsibilities between the Program Office and the Controller's Office was needed and would be addressed in a USAID Mission Order. These officials pointed out that the problems occurring in fiscal year 1987 have been corrected. Therefore, the following recommendation is considered resolved and will be closed after review of the proposed Mission Order dealing with review of unliquidated obligations.

Recommendation No. 1

We recommend that USAID/Indonesia issue a Mission Order that assigns responsibility for performing reviews of unliquidated obligations, identifying funds for deobligation and/or reobligation, and reporting the results of these actions as required.

USAID/Indonesia agreed with the recommendation and will issue a Mission Order that assigns responsibility for performing reviews of unliquidated obligations. The Office of the Inspector General considers the recommendation resolved and it will be closed after review of this Order.

2. Potential Deobligations Were Not Acted on Promptly -
When the unliquidated balances exceeded the funds required for an activity, USAID had not promptly deobligated these funds. Because of factors outside the Mission's control, only \$479,300 of the \$8.2 million in Development Assistance (DA) identified for possible deobligation had been deobligated as of July 1988. As a result, unneeded funds were not deobligated and/or made available for other purposes in a timely manner.

Discussion - A.I.D. Handbook 19 - Financial Management, states that when it is determined that the unliquidated balance exceeds the funds required, prompt deobligation action should be taken. The Asia and Near East (ANE) Bureau in AID/W provided guidelines for the fiscal year 1988 deob/reob process in December 1987. In March 1988, the ANE Missions were advised to proceed with deobligation of no-year funds. Also, in May 1988 the Bureau advised the Missions to hold off on deobligating all funds except no-year funds. The Missions were advised that the deob/reob ceiling was \$12.5 million for DA funds and \$12.5 million for Economic Support Funds for the entire Agency. As a result, USAID/Indonesia slowed down its planned deobligations.

In May 1988, the ANE Bureau advised the USAID program officer by telephone that the Mission should not create a paper trail of excess funds. In June 1988, the Bureau advised all Missions that the ceiling on deob/reob would

take several weeks to resolve. Finally, on July 18 the Bureau advised the Missions that it was 98 percent sure that the ceiling would be lifted and asked the Missions to submit candidates for deobligation. USAID/Indonesia had dropped about \$6 million from its reporting to the Bureau during this period. While USAID/Indonesia admitted that it would deobligate this amount, it was not willing to do so until the Bureau advised that the funds could be reprogrammed.

There was a conflict of guidance. On one hand, the Mission was required by Agency policy to deobligate promptly; but on the other hand, the Mission was instructed by the Bureau to wait. Subsequently, USAID/Indonesia was advised to proceed with its planned deobligations. The USAID has reported the \$8.2 million in deobligations to AID/W. Of this, \$2.2 million was planned to be reobligated for Indonesia and the remaining \$6.0 million was to be made available for other programs.

USAID/Indonesia officials stated that they were taking action as directed by AID/W and believed that they had obtained the necessary clarification on the issues. Since USAID/Indonesia has reported its candidates for deobligation, we are making no recommendation.

In formal comments on this report, the Mission stated that the planned \$8.2 million in deobligations was reduced to \$6.4 million. The \$6.4 million in deobligations was completed in September 1988. The Mission explained that for the remaining \$1.8 million, about \$1.0 million was no-year grant funds which must be reviewed by the Office of Management and Budget before the Congressional Notification can be submitted, thus insufficient time was available to complete the action. About \$800,000 was held to meet reassessed project needs.

Projects Selected for Review with
Unliquidated Obligations
as of 9/30/87

<u>Project Description</u>	<u>Fund Type</u>	<u>Grant(G) Loan (L) Project Number</u>	<u>PACD</u>	<u>Total Unliquidated Obligations</u>	<u>Unneeded Unliquidated Obligations</u>
<u>Terminated Projects</u>					
Surakarta Potable Water	L	497-0262	1/24/83	\$ 3,831	\$ 3,831
Science & Technology	G	497-0266	4/12/84	\$ 57,312	\$ 57,312
	L	497-0266	4/12/84	\$ 68,863	\$ 68,863
Rural Electrification	G	497-0267	12/31/84	\$ 32,291	\$ 32,291
	L	497-0267	12/31/84	\$ 120,563	\$ 120,563
Energy Manpower & Trng.	G	497-0300	9/30/84	\$ 84,865	\$ 84,865
Assistance to Environmental Ctr.	G	497-0314	1/31/85	\$ 2,236	\$ 2,236
Energy Planning for Dev. II	L	497-0318	9/30/85	\$ 11,805	\$ 11,805
Rural Works II	L	497-0285	1/31/85	\$ 177,930	\$ 11,930
Local Gov't Trng. II	G	497-0308	3/31/86	\$ 42,401	\$ 16,667
	L	497-0308	3/31/86	\$ 160,758	\$ 91,411
Sumatra Agrc. Res.	L	497-0263	8/31/87	\$ 744,705	\$ 297,570
Agr. Dev. Plng. & Adm.	L	497-0265	9/30/84	\$ 25,020	\$ 25,020
Small Scale Fisheries	G	497-0286	9/30/86	\$ 375,051	\$ 169,934
Sederhana Irrig. & Land Dev. II	G	497-0252	12/31/85	\$ 151,944	\$ 122,694
	L	497-0252	12/31/85	\$ 53,697	\$ 53,697
Higher Educ. Dev. Trng.	L	497-0248	9/28/84	\$ 46,914	\$ 19,890
Prof. Resources Dev. I	L	497-0261	9/30/84	\$ 11,120	\$ 11,120
Prof. Resources Dev. II	L	497-0275	9/28/84	\$ 112,473	\$ 112,473

Self Inst. Learning System	G	497-0280	9/30/84	\$ 1	\$ 1
Eastern Islands Agr. Educ.	L	497-0293	09/30/84	\$ 42,307	\$ 9,982
Educ. Communication Dev.	G	497-0296	09/30/84	\$ 1,629	\$ 1,629
In-Country Mgt. Dev.	L	497-0317	09/01/86	\$ 16,585	\$ 4,585
Inv. Dev. & Pack-Micr. Lend. Fac. Ind.	G	940-0002.46	09/30/86	\$ 50,000	\$ 50,000
Agr. Dev. Planning	G	498-0265	12/31/80	\$ 301	\$ 301
Tissue Culture-Virus Free Potato	G	936-5542.97	06/30/87	\$ 154,632	\$ -
PVO Co-Fin.	G	497-0225	04/30/83	\$ 45,992	\$ 45,992
OPG-Community Dev.	G	497-0251	06/30/84	\$ 20,179	\$ 20,179
Int'l Disaster Assistance	G	497-0900	05/01/87	\$ <u>3,195</u>	\$ <u>-</u>
SUB-TOTAL				\$2,618,600	\$ <u>1,446,841</u>
<u>Active Projects</u>					
PD & S	G	398-0249.03	09/30/88	\$ 732,488	\$ 62,837
Inv. Dev. & Pack	G	940-2002.03	03/11/88	\$ 22,322	\$ -
PVO Co-Fin. II	G	497-0336	09/30/88	\$5,587,250	\$ 170,436
Provincial Area Dev. Progr.	G/L	497-0264	4/12/88	\$3,049,799	\$ 8,560
Family Planning Dev. Services I	G/L	497-0270	4/6/88	\$1,805,172	\$ 154,525
Private Sector Dev.	G/L	497-0329	9/1/88	\$5,860,096	\$ 1,487
Educ. Policy & Planning	G/L	497-0344	9/30/90	\$ <u>5,135,879</u>	\$ <u>12,223</u>
SUB-TOTAL				\$22,193,006	\$ <u>410,068</u>
TOTAL				\$ <u>24,811,606</u>	\$ <u>1,856,909</u>

memorandum

DATE: October 13, 1988

APPENDIX 1
Page 1 of 2REPLY TO
ATTN OF: David N. Merrill, Director, USAID/Indonesia *Jmm*SUBJECT: Mission Comments on Draft Memorandum Audit of Policy and Procedures for
Reviewing Unliquidated Obligations, dated September 7, 1988

TO: William Montoney, RIG/A/Manila

Mission appreciated chance to discuss draft report at exit conference with Messrs. Olsen and Woodard on August 16, 1988.

We agree in general with the findings in the report and especially appreciate the acknowledgment on pages 4, 7, and 8 that the Mission has taken action to strengthen our portfolio and pipeline reviews. In addition to the actions mentioned, the Mission Controller and the Mission Program Officer are both newly arrived and have agreed to continue strengthening the Mission efforts for reviewing unliquidated obligations. Issuance of a Mission Order to clearly assign responsibilities will be done shortly.

We suggest that the statements at the top of page 4 and near the middle of page 10 be clarified so the reader understands that only one fourth of the reprogrammed funds from terminated projects was reprogrammed to PD&S. We also suggest that the last paragraph on page 11 be expanded to indicate that the Mission and AID/W have notified Congress of the planned deobligation for reobligation to PD&S funds through a Congressional Notification. The 15-day waiting period for the CN has expired indicating that Congress has reviewed this action and raised no objection.

We also note that the report in a number of instances states that there were \$1.9 million in unneeded obligations as of September 30, 1987. Exhibit 1 shows that \$410,068 of this amount relates to projects which were still active as of September 30, 1987, and which had from six months to three years of project life remaining as of September 30, 1987. The determination that such projects had "unneeded" obligations as of September 30, 1987, was apparently made based on the Mission's conclusion almost six months later, as a result of an AID/W direction to review project portfolios and deobligate funds which were not immediately required so that they could be used elsewhere. We do not believe that it is appropriate, in hindsight, to now classify these funds as "unneeded" as of September 30, 1987 based on subsequent determinations made under different conditions and criteria than those which prevailed in September 1987. We recommend that the \$1.9 million figure be reduced to \$1.4 million in each place in the report that the former figure appears.

Our comments related to specific recommendations follow:

Recommendation No. 1

"We recommend that USAID/Indonesia issue a Mission Order that assigns responsibility for performing reviews of unliquidated obligations, identifying funds for deobligation and/or reobligation, and reporting the results of these actions as required."

Mission Comments:

We agree with the recommendation and will issue a Mission Order within the next 30 to 45 days.

Recommendation No. 2

"We recommend that USAID/Indonesia obtain clarification from AID/W on what steps it should take to process the \$8.2 million for deobligation and/or reobligation."

Mission Comments:

As indicated in your follow-on meeting with the Program and Project Support Office, the Mission did initiate deob/reob actions once AID/W provided procedural clarification and advised us in July of the formal lifting by OMB of restrictions on processing deobs/reobs. Specifically, the Mission was authorized to proceed with deobligations of grant funds from completed projects where TNs had expired. The Mission then deobligated \$470,360 in addition to \$479,312 deobligated prior to the hiatus. In late August AID/W notified Mission of TN expiration for the remaining deobligations. In September Mission completed the remaining deobligations of approximately \$5.4 million bringing total FY 88 deobligations to \$6.4 million. Reobligation by the Mission of approximately \$1.2 million was also completed before end of FY88.

Please note that our planned deobligations of \$8.2 million have been reduced by approximately \$1.8 million. \$1.0 million are no-year grant funds which, according to AID/W, have to be reviewed by OMB before submission of the CN, resulting in insufficient time to complete deob/reob this fiscal year. Approximately \$800,000 is required to meet reassessed project needs.

Summary: Originally planned for FY 88 deobs	\$8.2 million
Reduced from original plan	<u>1.8 million</u>
Total FY88 deobs completed	\$6.4 million

We appreciate your decision to close this recommendation upon issuance of this draft audit memorandum.

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