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A STUDY OF THE RISK AND VULNERABILITY OF THE S&T BUREAU'S PORTFOLIO AND GUIDELINES FOR MINIMIZING IT

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TABLE OF CONTENTS

I. EXECUTIVE SUMMARY

BACKGROUND:

S&T/PO requested Solloway & Associates, Inc. to "provide information and guidelines to establish Bureau policies and procedures to assure adequate financial review of the S&T portfolio." We were asked to determine what portion of the portfolio had been audited, identify areas not being adequately audited, establish guidelines for conducting financial reviews, and develop a project officer's guide on audits and financial reviews. Our review and analysis led to the following major conclusions and recommendations.

FINDINGS:

We found that the S&T Bureau dealt with more institutions (267 contractors, organizations, universities, etc.) than it thought, and that it had more awards (776 contracts, grants, cooperative agreements, etc.) than it expected. Also, it was common for one institution to have as many as four or five different awards, and there were several instances where institutions had as many as 15 to 20 different awards.

The number of awards and their cumulative obligated amount was very pronounced at both ends of a spectrum. Our analysis of the portfolio revealed that less than 20 percent of all awards represented over 80 percent of the cumulative obligated amount, and that 38 percent of all awards represented barely 2 percent of the cumulative obligated amount.

We were able to substantiate that audits or financial reviews were made of institutions having awards representing 68 percent of the portfolio's obligated amount. This figure would be increased to 83 percent if we included institutions that are required to be audited, and probably were, but which we were unable to substantiate. (For example, universities are required to have A-128 or A-133 audits, non-profit organizations are required to have A-133 audits at least biennially, and government agencies provide their own audit coverage.) These figures were much higher than what the Bureau expected. Unfortunately, this heavy audit coverage at the institutional level did not carry over to the individual award level. We were able to identify only 18 individual awards that had been audited or had financial reviews.

The Bureau had expressed definite concerns about the vulnerability of its portfolio in previous years' vulnerability assessments. Their initial efforts to address this problem was through financial reviews, and this contract was to help in that area. We quickly realized that this was too narrow of a focus, and we expanded our approach to a broader objective -- *i.e.*, to develop operating guidelines to minimize the Bureau's risk and vulnerability of its portfolio.

RECOMMENDATIONS:

1. Initially, the S&T Bureau should focus on financial reviews and audits of its largest dollar awards.

2. The Bureau should develop a plan for controlling and monitoring audit reports, financial reviews, etc.

3. The Bureau should adopt as regular Bureau policy, the "Guidelines for Minimizing Pisk and Vulnerability" or some variation thereof. (*See* Annex 2.)

II. INTRODUCTION

In the annual assessment of the S&T Bureau's internal controls, a concern was expressed that the Bureau's current level of financial audit coverage was not adequate. This led to S&T/PO (Program Office) requesting Solloway & Associates, Inc. to "provide information and guidelines to establish Bureau policy and procedures to assure adequate financial review of the S&T portfolio."

A large number of distinct individual tasks was requested; the most important one being to develop Bureau guidelines for when financial reviews should be conducted. However, we quickly realized that there was a broader, overall objective to develop guidelines to minimize the Bureau's risk and vulnerability. Consequently, throughout our research and analysis, we decided to focus on the broader objective, rather than just the narrower issues of financial reviews.

Even though a final report was provided, Solloway & Associates believed that the work was important enough to summarize and issue this abbreviated report.

Separately, a user's guide for project officers was written, and it included: an overview of financial reviews and audits, a generic scope of work and cost estimates for financial reviews, and guidelines for actions to be taken to minimize risk and vulnerability.

In order to develop guidelines for minimizing the S&T Bureau's risk and vulnerability, the first step was to categorize its portfolio by the following types of institutions.

- Colleges and Universities - domestic and international
- For Profit Companies - corporations and individuals
- Non-Profit Organizations - domestic, international and other

Within each category, we then identified the number of institutions and the related number and cumulative obligation amount of individual awards. The basic information was obtained from the Agency's Contract Information Management Systems (CIMS) data base, and where there were obvious errors, institutions and related awards were recategorized. The results are contained in the Annex 1 table, "Analysis and Audit Coverage of the S&T Bureau Portfolio".

With the use of RIG/A/W Quarterly Audit Status Reports and discussions with Bureau personnel, we identified the level of financial reviews and audits covering the institutions. Additionally, for each institutional category, we identified the number and dollar amount of awards which fell within the different levels of cumulative obligation amounts. This information provided significant insight into the composition of the portfolio, and it became an integral part in establishing the guidelines for minimizing risk and vulnerability. The guidelines provide three increasingly effective levels of action that can be taken to minimize risk and vulnerability.

The "Guidelines for Minimizing Risk and Vulnerability" can be found in Annex 2, and they were developed only for the most significant types of institutions.

Since many individuals are unfamiliar with financial reviews and audits, a series of short questions and answers on the subject is provided in Annex 3.

III. DISCUSSION

A. AN OVERVIEW OF THE S&T PORTFOLIO

The following section is a broad discussion of the composition of the S&T portfolio, and this data is presented in the Annex 1 table, "Analysis and Audit Coverage of the S&T Bureau Portfolio". An analysis was not done of audit reports performed overseas that may have covered programs in the S&T portfolio.

1. Findings

The S&T Bureau had 776 awards with 264 institutions totalling $1,597 million with 264 institutions. The majority of these institutions and awards were broken down as follows: 80 domestic colleges/universities received 203 awards totalling $351 million; 61 for-profit corporations received 245 awards totalling $251 million; and 44 domestic non-profit organizations received 179 awards totalling $703 million.

Further analysis identified that multiple awards were being made to the same institutions. It was not uncommon for an organization to have four or five awards, and still there were various institutions with as many as 15 to 20 awards. Also, between the domestic colleges/universities and the for-profit corporations, they had 153 awards of less than $100,000. This means that these 153 awards (20 percent of <u>all</u> awards) represent less than 1 percent of the obligated amount of the portfolio. So many different awards to the same institution and so many small awards can become overwhelming to the system -- both administratively as well as managerially.

2. Recommendation

The S&T Bureau should review its procedures for issuing awards to determine if awards can be consolidated, thereby streamlining the administrative process and reducing the number of awards requiring management oversight.

B. STATUS OF AUDITS AND FINANCIAL REVIEWS OF THE S&T PORTFOLIO

One of the objectives was to obtain a clearer idea of the extent of audit and financial review coverage. We found that there was much more coverage than was initially expected. However, it was heavily slanted toward institutional audits and reviews, rather than individually related S&T contracts, grants, cooperative agreements, etc.

1. Institutional Coverage

a. Findings. Audits or financial reviews were made of institutions having awards in the amount of $1,086 million (68% of the portfolio); and the unaudited amount was $511 million (32% of the portfolio). However, if the amount of unaudited domestic universities ($170 million), domestic non-profit organizations ($112 million), and government agencies ($63 million) was added to the audit amount, then approximately $1,331 million or 83% would have had some coverage. Also, if the $91.8 million pertaining to WHO ($91.6 million) and PAHO ($0.2 million) were included, then the figures for audit coverage increased to $1,423 million (89%). Since universities are required to have A-128 or A-133 audits, non-profit organizations are required to have A-133 audits at least biennially, and government agencies provide their own audit coverage; the incremental amount represents, at a minimum, that amount which probably was audited but was not substantiated. The above figures represented both organization-wide and contract specific audits, but the preponderance of the audits are in the former category.

It should be noted that about 63% ($107 million) of the universities with unsubstantiated audits came from Johns Hopkins ($50 million), the University of North Carolina ($22 million) and the State universities of Florida-Florida A&M, Florida State and the University of Florida ($35 million). However, the Department of Education performed an audit for FY 1989 for the State of Florida, and it could have included the three above-mentioned universities. Of the unaudited $112 million for domestic non-profit organizations, RIG/A/W was requested to provide S&T/PO the audit status on 14 non-profit organizations having awards totalling $108 million. Partnership for International Education and Training represented $104 million of that amount. Many of the international organizations were affiliated with the Consultative Group on International Agricultural Research and had financial audits and management reviews done at the institutional level. Copies were in the S&T/FA office.

In summary, the S&T Bureau's portfolio, by organization, has had substantial audit/financial review coverage, and its degree of risk and vulnerability is below average. However, certain actions must be taken to maintain and even improve on this position.

2. Individual Contract/Grant Coverage

a. Findings. As discussed above, there has been substantial audit/financial coverage at the institutional level. However, the substantiated level of audits and financial reviews of individual contract/grant awards is quite low. In this very limited analysis, it appears that only 18 individual awards had been audited or had financial reviews. We found recent financial reviews only of Clark University, the Ohio State Research Foundation and the University of Arkansas at Pine-Bluff. Unfortunately, because there is not a central control point within the S&T Bureau to control and provide oversight of the audit/financial review function, it is possible that other unidentified audits and financial reviews did occur. The following is an analysis of what was found.

(1) Domestic Universities and Colleges. There were 80 institutions receiving 203 awards totalling $351 million. There were three financial reviews covering four institutions, six audits identified as contract specific to the S&T portfolio, and another seven audits covering direct and indirect costs. Regarding the latter, without obtaining copies of the audit reports (and this was not done), there was no way to know if those audits related to contracts in the S&T portfolio. There were 42 institutions, representing 97 awards totalling $133 million, with no evidence of any financial review/audit coverage, and there was no record of any A-128 or A-133 audits on file for any of the institutions.

(2) For-Profit Corporations. There were 61 corporations receiving 245 awards totalling $251 million. The records indicate that there were: one pre-award review, five audits contract specific audits, and seven "other" (timekeeping practices, internal controls, and accounting systems) audits of the corporations. Of the direct and indirect cost audits which were performed, it was not possible to relate them to a specific contract without analyzing each audit report and that was not done. However, for the 26 corporations that did not have any financial review or audit coverage, they had received 76 awards worth $59 million.

(3) Domestic Non-Profit Organizations. The 44 non-profit organizations received 179 awards totalling $703

million. There were only four contract specific audits. Additionally, there was no evidence of an A-133 audit for 16 institutions with 23 awards exceeding $123 million.

(4) International Universities. No analysis was done in this area.

(5) Individual Awards. No analysis was done in this area.

(6) International Organizations. There were 25 institutions receiving 31 awards worth $161 million. Of the $161 million, $91.6 million pertained to WHO for which there had been no financial reviews or audits. International Research Centers associated with CGIAR represent the majority of the remaining awards, institutions and money. Most of the centers had CGIAR audits and/or external management reviews, but none of them were grant specific to S&T funds.

(7) Other Non-Profic Organizations. The majority of the 71 awards worth $128 million relate to other Government Agencies. These agencies have audit responsibility for the programs, but there was no evidence of any audit activity.

b. Discussion. In all areas of the portfolio, there has been a dearth of financial reviews and audits of specific contract/grant awards. The question that must be addressed is, "Should financial review/audit coverage focus on the number of awards or the dollar amount of the portfolio?" This question is quite significant since it directly affects the guidelines for when financial reviews and audits should occur.

The obvious answer is a balance between the number of awards and dollar amount, but it is not such an easy balancing act. That is because just less than 20 percent of the awards represents an exceptionally high (over 80%) dollar amount of the portfolio. Therefore, the incremental audit coverage (in dollars) is negligible in relation to each additional review. On the other hand, 38 percent of all awards represented barely 2 percent of the cumulative obligated amount. However, it is necessary that a meaningful number of individual awards are reviewed in each category. This relationship will be discussed in more specific detail in the next section.

c. <u>Recommendations</u>.

(1) S&T/PO should determine the audit and financial review coverage of its individual grants, cooperative agreements, contracts, etc., and increase the frequency of audits and financial reviews.

(2) As a starting point, it is recommended that the S&T Bureau focus its financial review/audit coverage on the few, largest dollar awards in each category. By doing this, the risk and vulnerability of the Bureau's portfolio, dollar-wise, can be minimized significantly.

(3) S&T/PO should establish a central control point for monitoring the status of audit reports, audit activity, *e.g.*, requesting non-federal audits, responding to open audit recommendations, monitoring financial reviews, etc.

(4) S&T/PO should consider establishing a "Vulnerability Data Bank" which would contain data on the financial and management coverage of the grants, contracts, cooperative agreements made to various institutions and organizations. The "Bank" would contain data on audits, financial reviews, management audits and reviews, etc., plus possibly evaluation information.

(5) S&T offices should be requested to systematically file any audits, financial reviews, etc. and advise the control point in S&T/PO of any audits that occur for updating of their vulnerability data bank.

C. STRATIFYING THE PORTFOLIO BY CUMULATIVE OBLIGATION AMOUNT

1. Findings

An in-depth analysis was made of the awards in the three major institutions comprising the Bureau's portfolio, and this analysis included stratifying the portfolio by type of recipient and the cumulative obligation amount of each award (contract/grant). Our analysis revealed that only 17 percent of the awards represented 67 percent of the cumulative obligated amount. At the other end, almost 33 percent of the awards represented less than 2 percent of the cumulative obligated amount. These figures are consistent with the Bureau's entire portfolio, as discussed in Section III.B.2.b.

The above information provided guidance in developing cost-effective guidelines for management oversight, and it resulted in becoming an integral element in establishing the guidelines for minimizing risk and vulnerability.

Following is an analysis by cumulative obligation amount of the three major institutions which comprise the portfolio.

a. Universities and Colleges - Domestic. The portfolio breaks down as follows:

	Awards	Cumulative Obligation Amount (millions)
Total Portfolio	203	$351
> $10.0 million	9 (4%)	182 (52%)
$1.0 - $10.0 million	36 (18%)	130 (37%)
$0.5 - $1.0 million	25 (12%)	18 (5%)
$0.1 - $0.5 million	80 (40%)	18 (5%)
< $100,000	53 (26%)	3 (1%)

At the top end of the spectrum, just 9 awards (4 percent) represent 52 percent of the dollar value of cumulative obligations. Obviously, financial reviews and/or audits of those nine grants/contracts would provide significant dollar coverage of the portfolio. However, at the bottom end of the dollar spectrum, 133 awards (66 percent) represent only $21 million, or just 6 percent of the portfolio. Consequently, by requiring financial reviews and/or audits for all awards exceeding $500,000, then coverage will be provided to 34 percent of the awards and 94 percent of the dollar value of awards to domestic universities and colleges.

b. Corporations. The portfolio breaks down as follows:

	Award	Cumulative Obligation Amount (millions)
Total Portfolio	245	$251
> $10.0 million	3 (1%)	64 (25%)
$1.0 - $10.0 million	45 (19%)	141 (57%)
$0.1 - $1.0 million	97 (39%)	34 (14%)
< $100,000	100 (41%)	12 (4%)

At the very top end of the spectrum, only three contracts represent 25 percent of the portfolio's dollar value. Financial reviews and/or audits of only 20 percent of the awards results in 82 percent of the portfolio's dollar value. Meanwhile, since 80 percent of all awards represents only 18 percent of the portfolio's dollar value, the demands diminish for financial reviews and/or audits of these lower valued awards.

c. Non-Profit Organizations - Domestic. The portfolio breaks down as follows:

	Award	Cumulative Obligation Amount (millions)
Total Portfolio	179	$703
> $50.0 million	4 (2%)	318 (45%)
$2.0 - $50.0 million	37 (21%)	329 (47%)
$1.0 - $2.0 million	19 (11%)	27 (3.8%)
$0.5 - $1.0 million	20 (11%)	13 (1.9%)
< $500,000	99 (55%)	16 (2.3%)

Again, just a few awards represent 45 percent of the portfolio's dollar amount. Reviewing and auditing all awards over $2.0 million would result in coverage of 92 percent of the portfolio (dollar-wise), but only 22 percent of the awards. At the bottom of the spectrum, 55 percent of the awards represent not even 3 percent of the portfolio. Once again, the dilemma is raised of balancing adequate coverage of both awards and dollar amounts.

2. Summary

An optimum situation would exist if a non-federal audit would be done for each award; however, it is not practical nor cost effective. Therefore, steps must be taken to assure that the greatest dollar amount of the portfolio is audited, but also that a meaningful number of awards are either audited or are subject to financial reviews.

D. GUIDELINES FOR MINIMIZING RISK AND VULNERABILITY

1. Background

Even though the initial task only required guidelines regarding financial reviews, further analysis of the portfolio indicated that the guidelines needed to be expanded to cover other actions that minimize risk and vulnerability. Consequently, the comprehensive matrices, Guidelines for Minimizing Risk and Vulnerability, were developed. (*See* Annex 2.) The guidelines are presented in a matrix format and cover domestic nonprofit organizations, domestic colleges and universities, and corporations. Depending upon the size of the contract/grant, the matrix provides guidelines as to what actions should be taken to provide different levels of coverage. The actions under each level represent what must be done to attain that level of risk and vulnerability coverage. Each ascending level represents a higher degree of risk and vulnerability coverage, *e.g.*, the higher the level, the lower the amount of risk and vulnerability.

2. Discussion

In evaluating what actions needed to be taken to minimize the risk and vulnerability of the S&T Bureau portfolio, it was decided to categorize the actions at three levels. The first level represents a routine level of effort which provides a minimum level of risk and vulnerability coverage. This first level is related to the basic actions and responsibilities of a project officer. The second and third levels relate to audits and financial reviews and the frequency of them. The second level, through financial reviews and audits, represents what can and should be done to provide average coverage and reduce the risk and vulnerability to an acceptable and satisfactory level. The third level represents the highest level of risk and vulnerability coverage, and it affords the greatest amount of protection to the portfolio. This is because of the frequency of the audits, the intensity of them, and the direct focus of the audits on specific grants/contracts.

By looking at these three levels collectively and by considering the number of awards in each dollar category, a plan should be developed to provide the Bureau with the maximum amount of coverage in the most cost-effective manner. That plan is outlined in the Guidelines for Minimizing Risk and Vulnerability.

4. <u>Recommendation</u>

We suggest that the Bureau adopt the Guidelines for Minimizing Risk and Vulnerability (*see* Annex 2) or some variation thereof.

ANALYSIS AND AUDIT COVERAGE OF THE S&T BUREAU PORTFOLIO

Type of Institution	# of Inst.	# of Awards	Dollar Amt (Millions)[a]	Audit (Millions)[b]	Unaudited (Millions)[c]	Comments
I. Colleges and Universities						
A. Domestic	80	203	351	$ 181	$ 170	#1
B. International	9	14	2	0	2	#2
Sub-total	89	217	353	181	172	
II. For Profit Corporations						
A. Corporations	61	245	251	193	58	#3
B. Individuals	26	33	1	0	1	#4
Sub-totals	87	278	252	193	59	
III. Non-Profit Organizations						
A. Domestic	44	179	703	591	112	#5
B. International	25	31	161	56	105	#6
C. Other (mostly Gov't.)	19	71	128	65	63	#7
Sub-totals	88	281	992	712	280	
Grand Totals	264	776	1,597	$ 1,086	$ 511	

[a] "Cumulative Obligated Amount" per the CIMS report as of 9/25/90.

[b] Indicates the substantiated dollar amount of audit, financial or management review that has been performed and documented on institutions and/or grants, contracts, etc.

[c] Indicates the unsubstantiated dollar amount of unaudited institutions and/or grants, contracts, etc.

COMMENTS:

1. All Universities are required to have either an A-128 or an A-133 audit.

2. All of the International Universities have received grants through the Office of the Science Advisor. There was no evidence of any financial or management reports being received.

3. The $58 million of unaudited awards represents about 20 companies, of which ABT Associates, Inc. has awards totalling approximately $19.5 million.

4. One individual has awards exceeding $100,000 and another has awards exceeding $300,000.

5. All of these domestic non-profit organizations should have an A-133 audit at least biennially. Of the unaudited $112 million, RIG/A/W was requested to provide the audit status on 14 non-profit organizations having awards totalling $108 million. Partnership for International Education and Training (PIET) represents $104 million of that amount.

6. Of the unaudited $105 million, $91.6 million pertains to WHO and $0.2 million to PAHO. The remaining $13.4 million pertains principally to international organizations affiliated with CGIAR (Consultative Group on International Agricultural Research).

7. Normally, when a Government Agency receives funds from another Government Agency, the recipient Agency has audit responsibility. Of the unaudited $63 million, $51.9 million represents USG Agencies and $9.9 million represents quasi-government (National Academy of Sciences, which has DCAA on site, and the Smithsonian), and Milwaukee County is $1.2 million.

GUIDELINES FOR MINIMIZING RISK AND VULNERABILITY

NON-PROFIT ORGANIZATIONS - DOMESTIC

Cumulative Obligated Amount per Award	>$2.0M	$1.0M- $2.0M	$0.5M- $1.0M	<$0.5M
FIRST LEVEL				
1. Normal Project Officer Oversight	1	1	1	1
2. A-133 Audits at Time of RFP	2	2	2	2
3. Pre-Award Survey	3a	3a	3a	3a
4. Provide Financial Management Workshop to New Recipients	3b	3b	3b	3b
5. Overhead Audit (Indirect Costs)	4	4	4	4
6. Contract/Grant Close-Out Audit	4	4	4	4
SECOND LEVEL				
1. A-133 Audit	8	8	8	8
2. Financial Review	11	5	6	7
THIRD LEVEL				
1. RIG/A Specific Contract/Grant Audit	4	4	4	4
2. Non-Federal Specific Contract/ Grant Audit (Bureau Funded)	9,10,11	9,10	9,10	9,10

NON-PROFIT ORGANIZATIONS - DOMESTIC

Criteria:

1. Required for all projects. See Project Officer's Guidebook.

2. Request copies of the two most recent A-133 audits.

3a. Required. Request survey from MS/OP if institution/organization is a first-time recipient of an AID contract/grant, or they do not have a significant track record.

3b. Required if institution/organization is a first-time recipient of an AID contract/grant.

4. Project Officer should obtain copies for review from RIG/A or MS/OP, if done separately from the A-133 audit.

5. Required approximately half-way through life of contract/grant.

6. Desired, but can be waived with a valid reason.

7. Not required, but can be done upon request.

8. Project Officer should obtain and review current (annual/biennial) A-133 audit once contract/grant has been awarded.

9. Required if recommended in second-level financial review.

10. Required in 4th year of contract/grant if part of a long-term project (10 to 15 years) where the award will be re-awarded, either competitively or sole-source.

11. Both a financial review and a non-federal audit are required during period of contract/grant. Project Officer should schedule them (financial review first) so that they build upon one another and are complementary. Under very special circumstances, the financial review may be waived if recommended by the program analyst and approved by S&T/PO. Just the same, consideration should be given to an annual financial review or audit.

GUIDELINES FOR MINIMIZING RISK AND VULNERABILITY

COLLEGES AND UNIVERSITIES - DOMESTIC

	Cumulative Obligated Amount per Award			
	>$1.0M	$0.5M- $1.0M	$0.1M- $0.5M	<$100,000
FIRST LEVEL				
1. Normal Project Officer Oversight	1	1	1	1
2. A-128 or A-133 Audits at Time of RFP	2	2	2	2
3. Financial Management Workshop for New Recipients	3	3	3	3
4. Overhead Audit (Indirect Costs)	4	4	4	4
5. Contract/Grant Close-Out Audit	4	4	4	4
SECOND LEVEL				
1. A-128 or A-133 Audit	8	8	8	8
2. Financial Review	11	5	6	7
THIRD LEVEL				
1. RIG/A or Other Government Agency Specific Contract/Grant Audit	4	4	4	4
2. Non-Federal Specific Contract/Grant Audit (Bureau Funded)	9,10,11	9,10	9,10	9,10

COLLEGES AND UNIVERSITIES - DOMESTIC

Criteria:

1. Required for all projects. See Project Officer's Guidebook.

2. Request copies of the two most recent A-128 or A-133 audits.

3. Required if institution/university is a first-time recipient of an AID contract/grant.

4. Project Officer should obtain copies for review from RIG/A or MS/OP.

5. Required approximately half-way through life of contract/grant.

6. Desired, but can be waived with a valid reason.

7. Not required, but can be done upon request.

8. Project Officer should obtain and review current (annual/biennial) A-128 or A-133 audit during life of contract/grant.

9. Required if recommended in second-level financial review.

10. Required in 4th year of contract/grant if part of a long-term project (10 to 15 years) where the award will be re-awarded, either competitively or sole-source.

11. Both a financial review and a non-federal audit are required during period of contract/grant. Project Officer should schedule them (financial review first) so that they build upon one another and are complementary. Under special circumstances, the financial review may be waived if recommended by the program analyst and approved by S&T/PO. Just the same, consideration should be given to an annual financial review or audit.

GUIDELINES FOR MINIMIZING RISK AND VULNERABILITY

CORPORATIONS

	Cumulative Obligated Amount per Award		
	>$1.0M	$0.1M-$1.0M	<$100,000
FIRST LEVEL			
1. Normal Project Officer Oversight	1	1	1
2. Copies of Audits at Time of RFP	2	2	2
3. Pre-Award Survey	3	3	3
4. Overhead Audit (Indirect Costs)	4	4	4
5. Contract Close-Out Audit	4	4	4
SECOND LEVEL			
1. Financial Review	9	5	6
THIRD LEVEL			
1. RIG/A Specific Contract/Grant Audit	4	4	4
2. Non-Federal Specific Contract/Grant Audit (Bureau Funded)	7,8,9	7,8	7,8

CORPORATIONS

Criteria:

1. Required for all projects. See Project Officer's Guidebook.

2. Request copies of the two most recent audits related to federal contracts (preferably one overhead and one direct cost and AID related).

3. Required. Request from MS/OP if contractor is a first-time recipient of an AID contract, or they do not have a significant track record.

4. Project Officer should obtain copies for review from RIG/A or MS/OP.

5. Required, but can be substituted with a RIG/A directed close-out audit.

6. Not required, but can be done upon request.

7. Required if recommended in second-level financial review.

8. Required in 4th year of contract/grant if part of a long-term project (10 to 15 years) where the award will be re-awarded, either competitively or sole-source.

9. Both a financial review and a non-federal audit are required during period of contract/grant. Project Officer should schedule them (financial review first) so that they build upon one another and are complementary. Under very special circumstances, the financial review may be waived if recommended by the program analyst and approved by S&T/PO. Just the same, consideration should be given to an annual financial review or audit.

QUESTIONS AND ANSWERS ON FINANCIAL REVIEWS AND AUDITS

It is felt that the best way to introduce individuals to the subject of financial reviews and audits is through the following series of short questions and answers.

What is a financial review?

A financial review is to be considered as another aspect of AID's project monitoring process. It is not intended to be as independent and official as an audit; but rather, a Bureau managed process that will provide financial scrutiny of a specific contract/grant on an interactive basis with the recipient.

The principal focus of a financial review is on contract/grant specific compliance and on individual accounting transactions associated with AID funds. It will also include oversight, when deemed necessary, of an organization's internal controls related to management of AID funds, *i.e.*, for a new organization, where a recent review of internal controls has not been done, or where there is an indication that internal controls are not adequate.

The purpose of the financial review is to provide reasonable assurance that AID funds are properly disbursed and accounted for in accordance with AID regulations. Within this context, limited testing and reviews will be made to insure that the organization has sound and adequate financial management and accounting systems, recordkeeping procedures, and internal controls. The financial review will not be an audit of the overhead rate.

How does a financial review differ from a non-federal audit?

The financial review is requested, funded and managed by the Bureau and the appropriate project officer. The resultant report is delivered to the project officer for subsequent dissemination and action. It is the responsibility of the project officer to coordinate the results of the review (*i.e.*, the final financial review report) with the MS/OP Grant/ Contract Officer and the grantee/contractor and determine what type of corrective action is required.

A non-federal audit is requested and funded by the Bureau, but it is managed by RIG/A/W. A non-federal audit is a more independent, comprehensive, formal and official process than a financial review. A copy of the scope of work will be sent to RIG/A/W, and they will oversee the issuance of the contract. Hence, the audit team is working under the direction and guidance of RIG/A/W and the auspices of that office, and the audit will be conducted in accordance with government auditing standards. The resultant audit report will be issued by RIG/A/W as a non-federal audit with an audit number, a red cover, and the normal and full dissemination that audit reports receive. The audit report normally will contain: an opinion on the statement of financial accountability, a report on internal controls, and a report on compliance of applicable laws and regulations. Additionally, RIG/A/W is to be notified of the actions taken to clear/resolve the audit recommendations, and they determine if that action is satisfactory.

Does a financial review negate or fulfill the need for a non-federal audit?

A financial review *per se* does not negate the need for a non-federal audit. Based upon the results of a financial review, in conjunction with A-133/A-128 audits, overhead audits, program audits or direct/indirect cost audits and other available information, it provides a basis for determining: (1) that a non-federal audit is needed immediately, or (2) that further audit work is not required at that time. However, some non-federal audit activity should occur in the context of random sampling or testing of the Bureau project portfolio.

What is the linkage between a financial review and a non-federal audit?

The first level of financial oversight should be accomplished when a Project Officer carries out his/her basic duties and responsibilities; *e.g.*, review of payment vouchers, etc. A financial review is the second level of AID's procedures regarding project monitoring and oversight. If a financial review identifies material weaknesses in either the internal controls, accounting systems or transactions, or compliance with AID regulations or contract provisions, then it would be incumbent upon the Project Officer to request an audit by RIG/A/W of the contract/grant. This represents the third and most significant level of project monitoring and oversight.