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Memorandum Report On The Overhead Audit Of Arkel-Talab Cargo Services, Ltd.

Audit Report No. 3-650-86-5
Dated February 18, 1986

MEMORANDUM

DATE: February 18, 1986

FROM: Mr. Richard C. Thabet, RIG/A/Nairobi

SUBJ: Memorandum Report On The Overhead Audit Of Arkel-Talab Cargo Services, Ltd. Audit Report No. 3-650-86-5

TO: Dr. William Brown, Director, USAID/Sudan

BACKGROUND

This report presents the results of the overhead audit of Arkel-Talab Cargo Services, Ltd. This organization is one of six interrelated companies. At the time of our review, these companies derived about 85 percent of their revenue from USAID/Sudan direct and host government contracts. In total, the companies had nine active contracts valued at about US $58.5 million. The primary purpose of these contracts was to provide for the transport of emergency food to drought-stricken areas of Sudan. Of the $58.5 million, USAID/Sudan financed six contracts directly, amounting to $10.6 million. In addition, PL 480 Title I sales and Commodity Import Program local currency generations were used to finance three other contracts valued at the equivalent of $47.9 million. These three contracts were administered by the Food Aid National Agency (FANA) of the Government of Sudan (GOS).

Arkel-Talab Cargo Services, Ltd. (A-T) was 50 percent owned by Arkel International, headquartered in Baton Rouge, Louisana. Arkel International was 50 percent owned by a Sudanese. The remaining 50 percent of A-T was owned by a Sudanese company, Talab Trading and Investment Co. Therefore, 75 percent of A-T is, theoretically, Sudanese owned.

The affiliate, Arkel Cargo Logistics Overseas (ACLO) was incorporated in the Cayman Islands in 1982 for the purpose of earning and transacting foreign exchange, mainly US dollars. In form, A-T and ACLO were separate entities. But, due to intercompany transactions and common management, we viewed this as a single operation in evaluating their proposed overhead rate. The latest available financial statements presented the status of the companies as of February 29, 1984. Efforts to obtain more current financial information were unsuccessful.

AUDIT OBJECTIVES AND SCOPE

In response to your request, we made an overhead audit of Arkel-Talab Cargo Services, Ltd. located in Khartoum, Sudan. The audit had the following objectives: (a) to assess the adequacy of the company's accounting system for recording, accumulating and reporting costs incurred under U.S. Government contracts; (b) to review the financial position and (c) to evaluate the proposed overhead rate based on costs incurred by Arkel-Talab Cargo Services, Ltd. for fiscal year ending February 28, 1985. Although our scope was limited, certain other information came to our attention during our fieldwork, and this information is included in this report. Audit work was accomplished during October and November, 1985. This audit was made in accordance with generally accepted government auditing standards.

The scope of our field work was limited because of the non availability of audited financial statements for the year ended February 28, 1985. Our requests for more current audited financial statements were not honored by the firm's independent auditors, despite their promises to provide them. We were unable to determine precisely why the auditors could not or would not supply these statements.

RESULTS OF AUDIT

We found the accounting system adequate to record and report U.S. Government costs with three exceptions. First, the accuracy of financial data was not determined. Second, the system should be fully automated to allow for the voluminous financial data to be more efficiently accumulated. Third, the system did not segregate entertainment expenses from travel expenses. Since entertainment is an unallowable cost under Federal Acquisition Regulations (FAR's), the company should maintain a separate accounting for all entertainment expenses incurred.

The accounting system was basically a manual system consisting of journals supported by vouchers detailing transactions. Transactions were summarized monthly and posted to the general ledger. The company had a chart of accounts and written procedures for cash disbursements and receipts, sales, payables and expatriate salary accruals. Disbursements were the only aspect of Arkel-Talab Cargo Services, Ltd. accounting system that were fully automated.

The high volume of contracts and nature of the transactions placed strains on the manual accounting system. We found that the postings to the general ledgers for Arkel-Talab Cargo Services, Ltd. and ACLO were in arrears. However, the company was in process of bringing the general ledger up to date. On November 13, 1985, we were informed that postings were current. However, complete automation of the accounting system was necessary to efficiently accumulate and segregate U.S. Government costs.

Audited financial statements are prepared by a local independent accounting firm at the end of each fiscal year. The fiscal year ends on the last day of February for Arkel-Talab Cargo Services, Ltd. and ACLO. As stated in our scope section, the latest financial statement available presented the companies status as of February 29, 1984. Efforts to obtain more current financial information were unsuccessful.

Our analysis of the financial statements showed that in 1984, A-T and ACLO had serious financial difficulties. They also had significant losses in fiscal years 1983 and 1984. The latest financial statement showed bank overdrafts, cash flow problems and a weak current ratio.

The 1984 financial statements were translated into U.S. dollars at the official exchange rate because the dollar was considered to be the functional currency. The opinions expressed on those financial statements were unqualified as of February 29, 1984, however, we noted serious financial weaknesses. Salient points were:

-- Current ratio of 0.70. The current ratio shows a company's ability to pay its current obligations from current assets. A ratio of less than 1.00 is a measure of the inability to pay current obligations from current assets.

-- A retained earnings account deficit of $485,610.

-- A working capital <u>deficit</u> (negative net current assets) of $1,294,548.

-- Long-term obligations totalling $857,946.

-- A net loss for the period of $654,468.

Arkel-Talab's financial manager attributed the firm's financial problems to the departure of the Chevron Corporation. Chevron was one of their primary customers before the start of the drought and famine relief programs.

The contractor had proposed an overhead rate of 22 percent which was based on costs incurred for the two primary related companies: Arkel-Talab Cargo Services, Ltd. and Arkel Cargo

Logistics Overseas. As a result of our review we recommend an overhead rate of 20 percent due to the existence of some costs included in the indirect account balances which are unallowable by FAR's. Those costs not accepted are identified in Exhibit A.

Finally, it is our opinion that USAID/Sudan needs to reassess its relationship with this contractor especially when awarding large contracts like the emergency food relief or road maintenance and repair programs. If USAID/Sudan is unable to find alternate sources to fulfill its requirements then, based on the financial information available, the USAID should take steps to protect the interest of the U.S. Government by reviewing future contracts with the Regional Legal Advisor prior to finalization.

EXHIBIT A1

Arkel-Talab Cargo Services, Ltd.
Schedule of Proposed Indirect Costs
as of FY ending 2-28-85

Indirect Cost	(1) A-T Proposed Pounds	(2) A-T Questioned Pounds	(3) A-T Accepted Pounds	(4) ACLO Proposed $U.S.	(5) ACLO Converted to Pounds	(6) ACLO Questioned Pounds	(7) ACLO Accepted Pounds	(Column 3&7) Total Costs Accepted Sudanese Pounds
Salaries	LS453556		LS453556	$456125	LS1140313		LS1140313	LS1593869
Payroll Burden	71911		71911	4550	11375		11375	83286
Subsistence Medical	16513		16513	16062	40155		40155	56668
Travel Expenses	94816	LS(49496) (a)	45320	58476	146190	LS(27475) (b)	118715	164035
Permits-Visas	12616		12616	181	452		452	13068
Staff Vehicle Expenses	418831	(154184) (c)	264647	15639	39097		39097	303744
Staff Housing Expenses	445418		445418					445418
Office Supplies	79100		79100	7118	17795		17795	96895
Printing-Stationery	19878		19878	204	510		510	20388
Telephone-Postage	180001		180001	20550	51375		51375	231376
Electricity-Water	66294		66294					66294
Rent-Office	87348		87348	3550	8875		8875	96223
Consumables-Office	6828		6828	4273	10682		10682	17510
Maintenance-Office	10674		10674					10674
Insurance	14278		14278	1026	2565		2565	16843
Legal Expenses	10171		10171	12539	31347		31347	41518
Audit Fees	92695		92695					92695
Service Charges	31728		31728	3764	9410		9410	41138
Taxes	94550		94550					94550
Depreciation	269417		269417					269417
Shop Tools	65433		65433					65433
Shop Consumables	51921		51921					51921
Shop Repairs & Maint.	120		120					120
Shop Security	9032		9032					9032
Freight	146621		146621	315	787		787	147408
Currency Exchange	(79449)		(79449)					(79449)
TOTALS	LS2670301	LS(203680)	LS2466621	$604372	LS1510928	LS(27475)	LS1483453	LS3950074

LS=Sudanese pounds. Translated at $1.00=LS 2.5 (Official exchange rate).
Indirect Costs/Direct Costs=O/H Rate (LS 3950074/ LS 20171639)= .1958 percent)
Based on our review of these costs submitted by Arkel-Talab, we recommend an O/H rate of 20 percent.
These informal statements were submitted to USAID/Sudan about June 1985. During our audit in November 1985, they had not been certified by an independent auditing firm.

Arkel-Talab Cargo Services, Ltd.
Schedule of Proposed Direct Costs
as of FY ending 2-28-85

Direct Cost	(1) A-T Proposed Pounds	(2) A-T Questioned Pounds	(3) A-T Accepted Pounds	(4) ACLO Proposed $U.S.	(5) ACLO Converted to Pounds	(6) ACLO Questioned Pounds	(7) ACLO Accepted Pounds	(Column 3&7) Total Costs Accepted Sudanese Pounds
External Hire	LS1362509		LS1362509					LS1362509
Clearing Expenses	559710	LS913000 (d)	1472710	$2650	LS6625		LS6625	1479335
Handling Expenses	28969		28969	1595	3987		3987	32956
Railway Expenses	193262	(50000) (e)	143262					143262
Warehousing Expenses	1925		1925					1925
Road Expenses	98749		98749					98749
Salaries	109618		109618	4050	10125		10125	119743
Subsistence & Medical	41282		41282					41282
Fuel & Lube	875318	28183 (f)	903501	4103	10257		10257	913758
Spare Parts	805677		805677	46503	116257		116257	921934
Tires	9359		9359					9359
Depreciation	1464328		1464328					1464328
Project West Expenses	13582129		13582129					13582129
USAID Project Expenses	370		370					370
TOTALS	LS19133205	LS891183	LS20024388	$58901	LS147251	LS-0-	L[illegible]47251	LS20171639

These informal statements were submitted to USAID/Sudan about June 1985. During our audit in November 1985, they had not been certified by an independent auditing firm.

Explanation of Questioned Costs

(a) Proposed costs were LS 94816. General ledger showed balance of LS 45320.
(b) Entertainment expenses of LS 27475 were commingled with travel expenses.
(c) Proposed costs were LS 418831. General ledger showed balance of LS 264647.
(d) Clearing expenses for Talab Clearing and Transport Company were omitted.
(e) Proposed costs were LS 193262. General ledger showed balance of LS 143262.
(f) Proposed costs were LS 875318. General Ledger showed balance of LS 903501.

APPENDIX A

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