



U.S. Department of Agriculture



Office of Inspector General  
Midwest Region

## **Audit Report**

### **Rural Business-Cooperative Service's Progress To Implement the Improper Payments Information Act of 2002**

Report No. 34601-0004-Ch  
February 2006

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UNITED STATES DEPARTMENT OF AGRICULTURE

OFFICE OF INSPECTOR GENERAL

Washington, DC 20250



DATE: February 8, 2006

REPLY TO

ATTN. OF: 34601-0004-Ch

TO: Jackie J. Gleason  
Acting Administrator  
Rural Business-Cooperative Service

THROUGH: John Dunsmuir  
Acting Director  
Financial Management Division

FROM: Robert W. Young /s/  
Assistant Inspector General  
for Audit

SUBJECT: Rural Business-Cooperative Service Progress To Implement the Improper Payments Information Act of 2002

This report presents the results of our audit of the Rural Business-Cooperative Service's (RBS) fiscal year (FY) 2005 efforts to implement the Improper Payments Information Act (IPIA) of 2002.<sup>1</sup> Our audit of RBS was conducted as part of a Department-wide effort to evaluate USDA's progress to implement the IPIA, focusing on the most recent guidance issued by the Office of the Chief Financial Officer (OCFO). Our review of the risk assessment for the Business and Industry (B&I) Guaranteed Loan Program—the only RBS program with an estimated program level of \$50 million or more—disclosed that RBS had not compiled sufficient information to support its conclusion that the program was at low risk for improper payments. As a result, we were unable to independently determine if the RBS' ranking was supportable.

## **BACKGROUND**

In November 2002, the President signed the IPIA, Public Law (P.L.) 107-300, which requires the head of each agency to annually review all programs and activities the agency administers to identify those that may be susceptible to significant improper payments. For each program or activity identified, the agency is required to estimate the annual amount of improper payments. If the estimate is over \$10 million, the agency must also report the estimate to Congress along with the actions the agency is taking to reduce those improper payments. In May 2003, the

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<sup>1</sup> Public Law (P.L.) 107-300, November 26, 2002.

Office of Management and Budget (OMB) issued guidance for estimating and reporting improper payments. As the lead agency for coordinating and reporting the Department's efforts to implement the IPIA, OCFO provided additional instructions to USDA agencies in August and October 2003.

In FY 2004, we performed audits of six agencies, including RBS,<sup>2</sup> to determine whether the agencies performed risk assessments in compliance with the OMB and OCFO guidance for implementing the IPIA. Our review disclosed that RBS did not develop risk factors specific to its programs; thus, the risk assessments RBS provided to OCFO did not accurately reflect the programs' risk of improper payments. We also performed an audit of OCFO<sup>3</sup> in FY 2004, to evaluate its actions to implement the IPIA—specifically, its efforts to assess the department's programs for the risk of improper payments. Based on the results of that audit and the conditions reported in the agency audit reports, we recommended that OCFO strengthen its guidance to agencies for performing risk assessments.

OCFO issued more prescriptive guidance in November and December 2004. The revised OCFO guidance included specific instructions for agencies to follow in order to meet IPIA requirements, focusing on those programs most likely to be at significant risk for improper payments. The guidance divided programs into six categories, ranging from programs with less than \$10 million in program outlays to programs exceeding \$400 million in program outlays. As part of the guidance, OCFO issued instructions for performing tests of transactions in each program to determine the effectiveness of internal controls in preventing improper payments. To support their conclusions regarding programs' susceptibility to improper payments, agencies were to include the results of these tests in each program's risk assessment. The guidance also included key milestones for agencies to submit information, allowing OCFO and OMB to assess the agencies' progress in completing all risk assessments by the established deadline of April 30, 2005.

## **OBJECTIVE**

The objective of the audit was to assess RBS' implementation of OCFO's revised guidance regarding improper payment reporting requirements, including (1) agency efforts to conduct risk assessments of selected programs and report results to OCFO, and (2) agency conclusions that programs were at low risk for improper payments.

## **SCOPE AND METHODOLOGY**

We performed an audit of RBS compliance with the IPIA at RBS Headquarters in Washington, D.C. We conducted our fieldwork from July through August 2005. The audit was performed in accordance with *Government Auditing Standards*.

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<sup>2</sup> Rural Development Compliance with the Improper Payments Information Act of 2002, Audit No. 04601-10-Ch, dated January 2005.

<sup>3</sup> USDA Compliance with the Improper Payments Information Act of 2002, Audit No. 50601-8-Ch, dated January, 2005.

Of the risk assessments submitted to OCFO as of April 30, 2005, we judgmentally selected the B&I Guaranteed Loan Program, with an estimated program level totaling \$600 million for FY 2005. We based our selection on our preliminary analysis of vulnerability criteria, outlay dollars or program level, and the extent and adequacy of the risk assessment documentation provided to OCFO. The B&I program was the only RBS program that fell into OCFO's top three categories for program outlays. To accomplish our audit objectives, we interviewed the appropriate officials and reviewed the following documents:

- the IPIA, OMB guidance, and OCFO directives,
- regulations, program procedures, and handbooks,
- Rural Development (RD) instructions and administrative notices,
- prior Government Accountability Office (GAO) and Office of Inspector General (OIG) audit reports,
- FY 2005 budget summary in comparison to agency information, and
- RBS' risk assessment.

## **FINDING**

### **RBS Did Not Collect and Analyze Sufficient Information To Determine the Extent of Improper Payments.**

Although RBS had improved its process for performing risk assessments by identifying major vulnerabilities (or risk factors) to improper payments, our review disclosed that the agency had not fully adhered to OCFO's guidance for conducting risk assessments. We attributed this to RBS not adequately conducting tests of transactions as required. The tests were inadequate because the agency did not include information relative to the scope and did not evaluate the test results to determine if they impacted improper payments. Controls were not adequate to ensure OCFO's requirements were met. In addition, RBS officials who prepared the risk assessments stated they were not clear on what to include in their tests of transactions section. It should be noted, however, that OCFO held frequent meetings with all agencies, to include RBS, and interacted directly with RBS officials to discuss the ongoing process. Further, once we provided them with our results, they agreed that they should have included more information to meet OCFO's requirements. As a result, RBS risk assessment officials could not support their conclusion that the B&I program was at low risk for improper payments.

According to OCFO guidance,<sup>4</sup> agencies must, as part of their program risk assessments, list the internal controls preventing improper payments for each of the vulnerabilities identified and test a judgmentally selected sample of transactions "to determine the effectiveness of program design and internal controls in the prevention of improper payments." The OCFO guidance<sup>5</sup> also states that agencies "may need to work with [their] program, financial, internal review, budget, and performance management staff to complete these risk assessments."

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<sup>4</sup> USDA FY 2005 Tests of Transactions Guidance, dated December 8, 2004.

<sup>5</sup> USDA FY 2005 Risk Assessment Guidance, dated November 10, 2004.

As tests of transactions for the B&I program, RBS cited its Management Control Reviews (MCR), which are performed at all levels of the organization, and its Business Program Assessment Reviews (BPAR), which are performed for all RBS programs in each State on a 5-year cycle. We reviewed the guides used for each type of review and found that relevant areas are included to identify improper payment issues. However, RBS provided no information on the universe and number of loans reviewed and test results of those file reviews (i.e., analyzing the number and dollar value of deficiencies noted), to support its conclusion that internal controls designed to prevent improper payments were working as designed. For example, RBS reported that the B&I program was the subject of an MCR in FY 2003, but it provided no information on the results of that review or their impact on improper payments. An MCR is performed on a program once every 5 years. Although RBS reported that BPARs were completed in 12 States in FY 2004 and in 6 States to date (of 10 States planned) in FY 2005, RBS did not provide the results of the reviews or their impact on improper payments. BPARs are performed in 10 States every year. RBS noted only that one State lost delegated authority in FY 2004; however, the agency did not explain whether improper loans or other payments were the reason.

The RBS division responsible for preparing and reviewing the documentation, the tests of transactions and preparing the risk assessment, did not include more detailed information because it relied on summary reports of the MCR and BPAR results. The Financial Management Division (FMD) receives copies of the MCR reports and supporting documentation from the program staffs that perform the reviews. FMD compiles the results and prepares a summary report for each type of review. The summary reports do not contain sufficient information to determine the effectiveness of program design and internal controls in the prevention of improper payments, as required by OCFO guidance. RBS officials performing the risk assessments stated that the detailed results of the MCR were maintained by FMD. Although OCFO guidance states that various agency staffs may have to work together to complete the risk assessment, these officials did not obtain the details from FMD. The agency also relied on summary reports of the BPAR for information on the review results. According to the BPAR Handbook, workpapers are to be prepared to support all conclusions contained in the reports; however, the officials did not obtain and review these workpapers to complete the tests of transactions section of the risk assessment. Risk assessment officials agreed that additional information was needed to fully explain the tests of transactions. They stated that they had not been aware of what was to be included in the explanation of the tests of transactions in the risk assessment but had not sought further guidance from OCFO.

## **RECOMMENDATION**

Strengthen controls over the risk assessment process to ensure sufficient information is collected and analyzed in the tests of transactions to support the agency's conclusion as to the adequacy of internal controls to deter improper payments. Seek additional guidance from OCFO.

**AGENCY POSITION**

RBS concurred with the recommendation in its response, dated December 20, 2005, (see exhibit A). RBS stated in its response that the FY 2005 risk assessment, which they plan to deliver to OMB by February 28, 2006, will thoroughly describe the tested transactions. They plan to include detailed results of the testing conducted on BPARs and MCRs. Also in the response, RBS stated that they will seek guidance from the OCFO, as necessary, and incorporate recommendations into future BPARs and MCRs.

**OIG POSITION**

We concur with management decision. For final action, RBS needs to follow its internal procedures and provide OCFO with the detailed results of the testing conducted on BPARs and MCRs.

Final action on management decision should be completed within 1 year of the date of management decision to preclude being listed in the Department's annual Performance and Accountability Report.

We appreciate the courtesies and cooperation extended to our staff during this review.

# Exhibit A – Agency Response

Exhibit A – Page 1 of 1



United States Department of Agriculture  
Rural Development

DEC 20 2005

SUBJECT: Business and Cooperative Programs  
Progress to Implement the Improper  
Payments Information Act of 2002  
(Audit No. 34601-004-CH)

TO: John M. Purcell  
Director  
Financial Management Division

This is in response to the recommendation made in subject audit that the Agency strengthen controls over the risk assessment process to ensure sufficient information is collected and analyzed in the test of transactions to support the Agency's conclusion as to the adequacy of the internal controls to deter improper payments, and to seek additional guidance from Office of the Chief Financial Officer (OCFO).

The Agency agrees with the conclusion that the risk assessment for the Business and Industry (B&I) Guaranteed Loan Program did not sufficiently describe the tests of transactions used to determine the effectiveness of the internal controls in preventing improper payments. The fiscal year (FY) 2005 B&I Risk Assessment will thoroughly describe the tested transactions. This will include detailed results of the testing conducted on Business Programs Assessment Reviews (BPAR) and Management Control Reviews (MCR). The FY 2005 risk assessment for the B&I program will be delivered to the Office of Management and Budget by the February 28, 2006, deadline established by the Department.

We will continue to monitor controls over improper payments through the BPAR and MCR processes. The Agency will seek guidance from the OCFO, as necessary, and incorporate recommendations into future BPARs and MCRs.

We request management decision and final action on this recommendation.

If you have any questions, please contact Rick Bonnet, Special Projects/Programs Oversight Division at 202-720-1804 or [rick.bonnet@wdc.usda.gov](mailto:rick.bonnet@wdc.usda.gov).

A handwritten signature in black ink, appearing to read "Peter J. Thomas".

PETER J. THOMAS  
Administrator  
Business and Cooperative Programs

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Informational copies of this report have been distributed to:

Administrator, Rural Business-Cooperative Service Through: Director, Financial Management Division Operations and Management	4
U.S. Government Accountability Office	1
Office of the Chief Financial Officer Director, Planning and Accountability Division	1
Office of Management and Budget	1