

## **NGO FINANCIAL NEWSLETTER**

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**FY 2013 FOREIGN AID BUDGET NOT EXPECTED TO INCREASE, BUT MORE FUNDING FOR MIDDLE EAST DUE TO "ARAB SPRING"**

In his State of the Union address last Tuesday, President Obama said the United States had a "huge stake in the outcome" of the revolutions that have swept the Arab world. He pledged to "support policies that lead to strong and stable democracies," but offered no concrete proposals for additional assistance.

The White House is to unveil its proposed Federal budget for fiscal year 2013, including foreign assistance, on February 13<sup>th</sup>. (Soon after release of the President's budget request, NGO Financial Newsletter will release a summary of it in a Flash.)

It has yet to announce major new aid packages following the overthrow of governments in Egypt, Tunisia and Libya.

U.S. officials have cited fiscal restraints at home, as well as resistance in the Congress. "It's unfortunate the juxtaposition, that our budgetary constraints come at the same time that you have this enormously hopeful series of changes in the region," Undersecretary of State Robert Hormats said.

#### THE OBAMA ADMINISTRATION SET TO SPEED AID TO EGYPT

President Obama plans to accelerate the pace of American aid to Egypt, a top State Department official said, as the most populous Arab nation reaches a critical stage in its uncertain transition away from autocratic rule.

Robert Hormats, part of a U.S. delegation that held unprecedented talks last week with Egypt's Muslim Brotherhood, said Washington wanted to provide "more immediate benefits" to Egyptians, who earlier this month conducted their first democratic elections in decades.

"During this period, we want to be as supportive as we can. This is an historic moment. Egypt's a country of enormous importance," Hormats said.

Under the plan, some non-urgent U.S. aid slated for other countries -- he did not name them -- would be redirected to Egypt. And funding in the pipeline for long-term programs in Egypt would be shifted to quick-impact projects, he said.

Hormats, speaking to *Reuters* on the sidelines of the annual World Economic Forum, emphasized that the White House had not made any final decisions, and that he was providing Washington's "broad thinking" on the subject.

It was unclear whether the total amount of U.S. aid to Egypt would be increased. "Whether it's an increase or whether it's reprioritizing existing assistance, we're still working this out," Hormats said.

Congress approved \$1.3 billion in military aid to Egypt for the current fiscal year, but with conditions attached. It also approved \$250 million in economic aid, as well as an "enterprise fund" of up to \$60 million.

For the money to flow, Secretary of State Hillary Clinton must certify that the Egyptian government is supporting the transition to a civilian government, including holding free and fair elections, and implementing policies to protect freedom of expression, association, and religion, and due process of law.

In addition, the law says that none of the aid, military or economic, can be spent unless Egypt is meeting its obligations under the 1979 Egypt-Israel peace treaty.

## \$1 BILLION OF USAID ASSISTANCE FOR BANGLADESH OVER NEXT FIVE YEARS

USAID will provide Bangladesh with nearly \$1 billion of assistance in the next five years for sectors like food security, health, climate change and good governance.

USAID Bangladesh Mission Director Richard Greene disclosed while sharing the USAID's new Five-Year Assistance Strategy at a reception organized to celebrate its 50 years of global assistance and 40 years of partnership with Bangladesh. He said USAID has been working in Bangladesh's rural areas and expected that such support will continue in the future.

## NGOs TELL STATE AND USAID PROPOSED PARTNER VETTING SYSTEM HARMFUL

In a January 14 *Charity & Security Network* article, “ineffective and problematic is how several nonprofits and experts describe USAID’s proposed Partner Vetting System (PVS) in comments filed at the Department of State in December 2011 and at USAID in January 2012.”

“NGOs are actively objecting this burdensome and unwarranted program in which thousands of nonprofit workers and local partners would have to be screened against secret government databases.”

“In September 2011, the agencies presented parts of the proposed pilot program for NGOs in five countries, but has not yet announced further details. If implemented, the pilot would create hazards for aid workers, prevent some potential grantees from applying for funds, and will hamper the efforts of others to deliver services and programs that serve the interests of the United States.”

“PVS is not adequately designed to protect NGO workers and partners and represents an unwelcome redefinition of the relationship between our community and the federal government, endangering critical aid and development work and consequently harming U.S. national interests,” said the comments sent to USAID by InterAction ...”

“Other groups, including Save the Children and the Peace Appeal Foundation, say PVS is ‘a solution in search of a problem’ because there is no evidence that USAID funds are flowing to terrorist organizations through NGOs. According to the USAID OIG, who conducted the oversight of the initial PVS-like vetting of programs in USAID's West Bank/Gaza portfolio for 2006 and 2007, ‘oversight activities during this period did not identify any instances where terrorist organizations received USAID funds.’ Nor has it reported finding such diversions elsewhere.”

In Section 7034(i) of the FY 2012 Consolidated Appropriations Act (P.L. 112-74), Congress directed State and USAID to implement the Partner Vetting System pilot program no later than September 30, 2012.

#### AFGHAN AID FACES MORE RESTRICTIONS, INCLUDING LIFTING TAXES ON U.S. CONTRACTORS AND SUBCONTRACTORS

In 2012, Congress is trying to tighten the screws on the aid it sends to Afghanistan through the State Department and other civilian agencies, although lawmakers continue to take a more hands-off approach to the much larger pot of money for Afghan assistance governed by the U.S. military.

Congress has strictly conditioned the money it is providing the State Department and USAID in fiscal 2012 on the behavior of the Afghan government -- including a demand for action to tamp down corruption and empower various sectors of society.

But that is only a fraction of the U.S. assistance going to Afghanistan. The billions more being funneled through the Department of Defense face no such conditions.

Those differences underscore the competing priorities between Defense and State Department appropriators in Congress when it comes to assisting Afghanistan. But the lack of consistency may make it harder for the U.S. officials to encourage good behavior by the government in Kabul, whose performance will become increasingly important as it takes on more responsibility in the coming years.

The fiscal 2012 omnibus spending measure (P.L. 112-74), which the Senate cleared Dec. 17, includes more than \$126 billion for the Overseas Contingency Operations (OCO) account -- \$115.1 billion for the Pentagon and \$11.2 billion for the State Department and foreign aid -- a large chunk of which will go toward operations in Afghanistan.

Before releasing any of the money for economic support, counternarcotics or law enforcement funded in the State and Foreign operations account, the Secretary of State will have to certify that the programs are sustainable and transparent and the Afghan government is taking a long list of steps to reduce corruption, improve accountability, protect human rights and empower women. Funding for reconciliation and reintegration of armed insurgents is only available on the condition that Afghan women are participating in the reconciliation process and the program being funded does not pardon any leader of an armed group "responsible for crimes against humanity, war crimes or acts of terrorism."

The legislation also requires the Secretary of State to report back to Congressional appropriators within 90 days on the Afghan government's response to the 2010 Kabul Bank crisis and how Kabul is cooperating with the International Monetary Fund to recover lost funds and restructure the bank. It also threatens to withhold a portion of aid

money in fiscal 2013 if the Afghan government taxes U.S. contractors or subcontractors, as Kabul threatened earlier this year.

USAID PUSHES TO "BROADEN OUR PARTNER BASE," USAID CHIEF ACQUISITION OFFICER TELLS *THE WASHINGTON POST*

According to a December 26 *Washington Post* article, USAID is seeking to increase competition for its contracts and make its programs more accessible to small and disadvantaged businesses as part of a larger agency-wide reform effort.

Concerned that a reduction in contracting staff has led to an increased reliance on a fairly small group of contractors and nongovernmental organizations, USAID has made changes to its procurement program a key part of its reform.

In its plan for change, the Agency says it is "falling short" in accessing the full range of talent in both U.S. businesses and organizations and those in developing countries. USAID has started by promoting more competition within its programs, particularly focusing on setting aside more awards for small and disadvantaged businesses.

The Agency has established a review board that looks at ways to make large contracts more accessible to small businesses, such as by splitting them into smaller pieces, said Aman S. Djahanbani, USAID's chief acquisition officer.

"Broadening our partner base ... just makes good business sense, and it furthers sustainable development," Djahanbani said.

At the same time, the Agency is trying to work with more of the organizations and companies that are local to a given country. Littleton Tazewell, senior adviser to USAID's general counsel for implementation and procurement reform, said the Agency often relies on intermediaries -- such as U.S.-based contractors or international nongovernmental organizations -- to work with local bodies.

"The idea here is to increase our direct engagement with local organizations," said Tazewell, who said a deeper understanding of local organizations will help USAID craft better solicitations.

The Agency also is seeking to make its regulations and rules less burdensome to encourage more companies and organizations to compete for contracts and grants. USAID acknowledged that some larger contractors or NGOs may see reduced work as a result of its procurement reform moves.

"Our partners need to realize that there is more competition," said Djahanbani. "However, they definitely have a role to play -- maybe a different role."

For instance, he said, in some cases a local organization could serve as the prime contractor while an international or U.S.-based organization could function as a subcontractor.

Tazewell said USAID has engaged the companies and organizations it frequently uses as it reforms in an effort to identify their particular problems.

Still, USAID is only about 18 months into what it expects to be a five-year process, Tazewell said.

"We're going to trip and make some mistakes along the way, but our expectation is at the end of that five-year process we'll be a much better organization," he said. "We will have a structure [and a] regulatory framework that allows for a broadened partner base that's both local- and small business-oriented."

#### **RULE FOR GOVERNMENT CONTRACTORS PROPOSES 7% GOAL OF WORKFORCE BE DISABLED WORKERS**

At 76 Fed. Reg. 77056 (December 9, 2011), the Department of Labor's Office of Federal Contract Compliance Programs has proposed a slate of new rules on recruiting and hiring individuals with disabilities, including a requirement that government contractors set a 7 percent goal, not a quota, for each job group. Critics of the proposal say the new rules are so onerous they could drive some contractors out of government projects.

"This proposed rule represents one of the most significant advances in protecting the civil rights of workers with disabilities since the passage of the Americans with Disabilities Act" in 1990, Labor Secretary Hilda Solis said in an announcement.

The proposed rule spells out actions contractors must take in recruitment, training, record-keeping and policy dissemination. The steps are much like those long required for hiring women and minorities. The rule is designed to strengthen the affirmative action requirements established in Section 503 of the 1973 Rehabilitation Act, according to the Labor Department. The announcement noted that the unemployment rate for people with disabilities is 13 percent, or one and a half times the overall jobless rate.

Under the rule, contractors would have to improve their data collection and self-reviews of affirmative action and "reasonable accommodation." They also would have to adjust their lists of job openings to widen their applicant pools.

#### **FAR REVISION CLARIFIES USE OF T&M AND LABOR HOUR CONTRACTS AND MAKES INFORMATION IN FAPIIS POTENTIALLY PUBLICLY AVAILABLE**

At 77 Fed. Reg. 194 (January 3, 2012), a final rule amends the Federal Acquisition Regulation to: (1) ensure that time-and-materials (T&M) and labor-hour (LH) contracts are used to acquire commercial services only when no other contract type is suitable, and

(2) instill discipline in the determination of contract type with a view toward managing the risk to the Government.

The requirement for a determination and findings when no other contract type is suitable is added to FAR 8.404, Use of Federal Supply Schedules. FAR 8.404 has also been amended to address increases in the order ceiling price of T&M and LH contracts, to more closely conform to the language at FAR 12.207. In addition, FAR 16.201 is modified and FAR 16.600 is added to clarify that T&M and LH contracts are not types of fixed-price contracts.

In the same edition, at 77 Fed. Reg. 197, a final FAR rule was adopted requiring the information in the Federal Awardee Performance and Integrity Information System (FAPIIS), excluding past performance reviews, to be made publicly available.

The final rule allows a 14-calendar-day delay before making the data available to the public. Contractors have 7 calendar days within those 14 calendar days to assert a disclosure exemption under the Freedom of Information Act. In addition, the FAPIIS system has been modified to allow more space for contractor comments.

#### FEW MAJOR CHANGES IN ACCOUNTING PRINCIPLES EXPECTED IN 2012

There are no major changes in the accounting principles expected in 2012. What changes that can be expected are in the areas of revenue recognition, accounting for leases and financial statement presentation, as briefly described as follows:

##### Revenue Recognition:

Re-exposed on November 14, 2011, this has the potential to affect every entity's day-to-day accounting and the way business is executed through contracts with customers.

##### Leases:

Under this proposed standard, all leases would result in asset and liability recognition significantly affecting entities' balance sheets. Even if a new principle for accounting for leases is released this year, it will not likely become effective until 2017.

##### Financial Instruments:

The attention financial statements received in the recent financial crisis makes this topic a priority project for both FASB and IASB.

#### FASB WON'T REQUIRE MANAGEMENT TO MAKE GOING-CONCERN ASSESSMENTS

The concept of "going concern" is getting a lot of attention -- both from the Financial Accounting Standards Board (FASB) in its proposed rule-making and separately by USAID in its January 10, 2012, revision to 22 CFR 228. For its part, FASB will not

require management to assess whether there is substantial doubt about an entity's ability to continue as a going concern.

After its January 11<sup>th</sup> board meeting, FASB announced that a majority of board members determined that such a requirement would be difficult to apply. Board members decided that users of financial statements would benefit more from ongoing disclosures about risks and uncertainties.

Disclosures made only after management concludes there is substantial doubt about an entity's ability to continue as a going concern would be less beneficial to users of financial statements, according to the board.

The next step in the project is developing a principle for an entity to determine the adequacy of its disclosures about risks and uncertainties, and to evaluate how the content of those disclosures could be improved. The board directed the FASB staff to develop such a principle.

FASB first issued a Proposed Statement of Financial Accounting Standards, Going Concern, on Oct. 9, 2008, for a 60-day comment period. The proposal would have required an entity to assess its ability to continue as a going concern, preparing financial statements on a going-concern basis unless liquidating or ceasing operations was the entity's intention or only realistic alternative.

Management would have been required to take into account all available information about the future, which was defined as at least, but not limited to, 12 months from the end of the reporting period.

The proposal would have required management to disclose uncertainties that cast substantial doubt upon the entity's ability to continue as a going concern. FASB's summary of the comment letters indicated that a large majority of the 29 respondents generally supported FASB's initial decision to include guidance on going-concern assessments in accounting literature. But respondents also had concerns.

According to FASB's Comment Letter Summary, a few respondents said the wording "all available information about the future" was too broad and could require management to consider an endless amount of information "regardless of its quality or relevance." A few other respondents questioned how much time and money management should devote to considering all available information about the future. A few observed that the purpose of a going-concern assessment is to address the viability of an entity over the next 12 months, not assess the viability of a business model in general.

Currently, AICPA Statement on Auditing Standards (SAS) no. 59, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* (AICPA, *Professional Standards*, vol. 1, AU sec. 341), provides the U.S. guidance on this topic. It states that the auditor is responsible for evaluating whether there is substantial doubt about the entity's ability to continue as a going concern for a reasonable period not more

than one year beyond the date of the financial statements' being audited. Information obtained during a financial statement audit is the basis for this evaluation.

In October 2011, the board decided that improving disclosures to serve as an early warning of an entity's potential inability to continue as a going concern would not be an objective of the project, which was renamed *Disclosures about Risks and Uncertainties and the Liquidation Basis of Accounting*. That decision was partly a result of the board's recent decision to add incremental disclosures about liquidity risk in the separate project on accounting for financial instruments, according to FASB's report from the board meeting.

That left the board to decide whether management or outside accountants of an entity should have the primary responsibility for performing the going-concern assessment.

Another objective of the project was how and when an entity should apply the liquidation basis of accounting.

FASB has previously decided in the project that an entity should prepare financial statements on the going-concern basis unless a plan of liquidation has been approved by the owners or is being imposed by other forces and it appears remote that the entity will become a going concern in the future.

Liquidation basis financial statements, FASB decided, should reflect relevant information about the value of an entity's resources and obligations in liquidation. They should consist of a statement of net assets in liquidation, and a statement of changes in net assets in liquidation.

#### FASB PROPOSAL AIMS TO SIMPLIFY IMPAIRMENT TESTING OF INDEFINITE-LIVED INTANGIBLE ASSETS

On January 25<sup>th</sup>, FASB issued a proposed Accounting Standards Update it said would reduce costs and simplify the guidance for testing indefinite-lived intangible assets other than goodwill for impairment.

The amendments in the proposed update, "*Intangibles – Goodwill and Other. Testing Indefinite-Lived Assets for Impairment*," would allow an organization to assess qualitative factors to determine whether performing the quantitative impairment test is necessary.

An organization that chooses to perform a qualitative assessment would be spared calculating the fair value of an indefinite-lived intangible asset unless the qualitative assessment shows that it is "more likely than not" that the asset's fair value is less than its carrying amount.

Indefinite-lived trademarks, licenses and distribution rights are examples of assets covered by the proposal. All public, private and not-for-profit companies would apply the standard.

The current guidance on the topic is “*FASB Accounting Standards Codification Subtopic 350-30, Intangibles—Goodwill and Other—General Intangibles Other than Goodwill.*” That guidance requires an organization to test an indefinite-lived intangible asset for impairment on at least an annual basis. This is done by comparing the asset’s fair value with its carrying amount. If the carrying amount exceeds the asset’s fair value, the difference in those amounts is recognized as an impairment loss.

But in a recent issue of *FASB in Focus*, FASB said it received comments noting that as a result of the recent amendments to the goodwill-impairment guidance and the existing guidance for testing long-lived assets for impairment, only indefinite-lived intangible assets would not be eligible to use a qualitative assessment.

FASB said it constructed the proposed update in an effort to simplify assessment and lower costs while making testing methods more consistent.

“This proposed amendment is intended to reduce the cost of evaluating indefinite-lived intangible assets for impairment without changing the information provided to investors,” FASB Chair Leslie Seidman said in a statement. “The proposed amendment is similar to the simplification that the board issued last year relating to the impairment testing of goodwill.”

The amendments would be effective for annual and interim impairment tests performed for fiscal years beginning after June 15, 2012, and early adoption would be permitted.

## IRS ISSUES REGULATIONS ON TREATMENT OF REPAIR EXPENDITURES

On December 27<sup>th</sup>, the IRS issued long-awaited temporary and identical proposed regulations (T.D. 9564; REG-168745-03) regarding the treatment of expenditures incurred in selling, acquiring, producing, or improving tangible assets, including rules on determining whether costs related to tangible property are deductible repairs or capital improvements. The temporary regulations affect all taxpayers that acquire, produce or improve tangible property.

The temporary regulations clarify and expand the standards in the current regulations under Secs. 162(a) and 263(a) and provide rules for applying these standards. They also provide guidance on accounting for, and dispositions of, property subject to Sec. 168 and amend the general asset account regulations.

Distinguishing between expenditures for capital improvements or for deductible ordinary repairs is a highly factual determination, and a number of court cases have set out tests for making the distinction. Because it has been difficult for taxpayers to apply the standards set out in case law, the regulations, and IRS guidance, the IRS issued proposed

regulations in 2006 (later withdrawn) and 2008. The temporary and proposed regulations respond to comments received in response to the prior proposed regulations.

The temporary regulations provide a general framework for capitalization and retain many of the provisions of the 2008 proposed regulations, which in many instances incorporated standards from existing authorities under Sec. 263(a).

Among the changes introduced by the temporary regulations are revised rule for determining whether an amount is paid for an improvement to a building, as well as the rule for determining whether an amount is paid for the replacement of a major component or substantial structural part of a unit of property. The temporary regulations also provide several new rules that were not in the 2008 proposed regulations.

#### Materials and Supplies:

The temporary regulations generally retain the framework in the 2008 proposed regulations for materials and supplies. In response to comments, however, the temporary regulations modify and expand the definition of materials and supplies, provide an alternative optional method of accounting for rotatable and temporary spare parts, and provide an election to treat certain materials and supplies under a *de minimis* rule in Temp. Regs. Sec. 1.263(a)-2T. The temporary regulations also allow a taxpayer to elect to capitalize certain materials and supplies.

#### Repairs:

Under the 2008 proposed regulations, amounts paid for repairs and maintenance to tangible property are deductible if the amounts paid are not required to be capitalized under Regs. Sec. 1.263(a)-3. The temporary regulations retain this rule and clarify that a taxpayer is permitted to deduct amounts paid to repair and maintain tangible property provided such amounts are not required to be capitalized under Sec. 263(a) or any other provision of the Code or regulations.

#### Rentals and Leased Property:

The temporary regulations make minor revisions to the rule in Regs. Sec. 1.162-11(b) that provides that the cost of erecting a building or making a permanent improvement to property leased by the taxpayer is a capital expenditure and is not deductible as a business expense.

The temporary regulations amend the rules in Regs. Sec. 1.162-11(b) and 1.167(a)-4 to provide that a lessee or lessor must depreciate or amortize its leasehold improvements under the cost recovery provisions of the Code applicable to the improvements, without regard to the term of the lease. They also remove the rules permitting amortization over the shorter of the estimated useful life or the term of the lease.

#### Amounts Paid to Acquire or Produce Tangible Property:

The temporary regulations retain the rules from the 2008 proposed regulations on capitalization of amounts paid to acquire or produce units of tangible property. These include a general requirement to capitalize acquisition and production costs and a requirement to capitalize amounts paid to defend and perfect title to property.

Responding to comments, the temporary regulations clarify how the rules apply to moving and reinstallation costs. They also retain the rule for costs incurred prior to placing property into service, add and clarify certain rules with respect to transaction costs, and modify and refine the *de minimis* rule.

The *de minimis* rule under the temporary regulations retains the requirement that a taxpayer may deduct certain amounts paid for tangible property if the taxpayer (1) has an applicable financial statement, (2) has written accounting procedures for expensing amounts paid for such property under certain dollar amounts, and (3) treats such amounts as expenses on its applicable financial statement in accordance with such written accounting procedures. However, the temporary regulations replace the “no distortion” requirement in the proposed regulations with an overall ceiling that generally limits the total expenses that a taxpayer may deduct under the *de minimis* rule.

Under the new criteria, the aggregate of amounts paid and not capitalized under the *de minimis* rule for the tax year must be less than or equal to the greater of (1) 0.1% of the taxpayer’s gross receipts for the tax year as determined for federal income tax purposes; or (2) 2% of the taxpayer’s total depreciation and amortization expense for the tax year as determined in its applicable financial statement.

#### Amounts to Improve Property:

The temporary regulations retain the basic framework of the 2008 proposed regulations for determining the unit of property and for determining whether there is an improvement to the unit of property. They also retain many of the simplifying conventions set out in the 2008 proposed regulations, including the routine maintenance safe harbor and the optional regulatory accounting method.

The 2008 proposed regulations provided a safe harbor from capitalization for the costs of performing certain routine maintenance activities. Under the safe harbor, an amount paid was deemed not to improve the unit of property if it was for ongoing activities that a taxpayer (or a lessor) expected to perform as a result of the taxpayer’s (or the lessee’s) use of the unit of property to keep the unit of property in its ordinarily efficient operating condition. The activities count as routine only if, at the time the unit of property was placed in service, the taxpayer reasonably expected to perform the activities more than once during the class life of the unit of property. Despite receiving numerous comments on this safe harbor, the IRS has retained it in the temporary regulations, but it is modified so that it will not apply to buildings.

#### Accounting and Disposition Rules for MACRS Property:

The temporary regulations also revise the rules for accounting for MACRS property (i.e., assets to which Sec. 168 applies) and the rules for determining gain or loss upon the disposition of MACRS property.

The temporary regulations eliminate group accounts, classified accounts, and composite accounts under Regs. Sec. 1.167(a)-7. Instead, each multiple asset account must include, in most cases, assets that have the same depreciation method, recovery period, and convention, and that are placed in service in the same tax year. The temporary regulations also provide rules for determining gain or loss upon the disposition of MACRS property that are consistent with the disposition rules under Prop. Regs. Sec. 1.168-6 of the proposed ACRS regulations.

### INTERNAL CONTROL – INTEGRATED FRAMEWORK – 20 YEARS LATER

Almost 20 years ago, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) produced the landmark *Internal Control – Integrated Framework*. With this published framework, COSO, an organization providing leadership and guidance on internal control, enterprise risk management and fraud deterrence, established a common internal control model against which companies and organizations may develop and assess their control systems. It became the world’s most widely used internal control framework.

With advances in technology and business operations, the time was right for the framework to be updated so it could remain relevant and useful. In November 2010, COSO announced such a project. An online survey in January 2011 gleaned input from a broad audience. Last month COSO released the proposed updated *Internal Control – Integrated Framework Exposure Draft* to obtain input from the users of the framework and the general public.

### Updated COSO Cube



You might be familiar with the COSO Cube, which represents a depiction of the COSO *Internal Control – Integrated Framework*. The good news is that the COSO Cube has

proven the test of time and remains the same in terms of the definition of internal control and the five components of internal control (changed only in their positioning in the cube).

So what has changed? The updated and enhanced framework:

- Clarifies the application of the framework in today's environment with the various business models, technology and related risks
- Codifies criteria that can be used in the development and in evaluating the effectiveness of systems of internal control -- making explicit 17 principles and attributes
- Expands reporting objectives to support internal and non-financial reporting and operational and compliance objectives.

The COSO Board believes these updates will result in a more flexible, reliable and cost-effective approach to the design and evaluation of internal control systems for organizations looking to achieve operational, compliance and reporting objectives. The framework applies to all sizes and types of organizations: public companies, privately held companies, not-for-profits and governmental entities. Companies that currently have effective internal control systems will not experience additional responsibilities under the clarified framework.

Comments on the proposal are due March 31. AICPA members and other stakeholders are encouraged to review and provide feedback on the exposure draft. For more information on the COSO *Internal Control – Integrated Framework* Exposure Draft, visit <http://www.aicpa.org/COSO>.

#### USAID OIG's BARK WORSE THAN ITS BITE

Yes, USAID OIG questioned \$96.87 million in FY 2011 and U.S. contractors and recipients are increasingly exposed to audits of their field offices, particularly security subcontractors, in Iraq, Afghanistan, Haiti, Pakistan and the Middle East. Non-U.S. NGOs have had the greatest cost disallowances, especially in East and Southern Africa.

However, except for a few off-the-charts recoveries from AED and The Louis Berger Group, USAID OIG's actual recoveries from audits of U.S. organizations are typically just pennies on the dollar, i.e., BearingPoint: 0.09¢, IFES: 0.8¢, IRD: 4¢, yet the OIG puts the "big hurt" on auditees and their top management until the audit recommendations are resolved.

NGO Financial Newsletter is not encouraging U.S. NGOs and contractors to lower their guard or reduce their internal controls against potentially paying back huge sums from audits. By and large, though, U.S. organizations have been able to have the in-house capability or retain outside legal and accounting expertise to negotiate most of these OIG cost disallowance recommendations away.

## IG OBTAINS A TOP USAID CONTRACTOR'S DRAFT INTERNAL AUDIT REPORT

Last month, NGO Financial Newsletter reported that the Government Accountability Office (GAO) recommended that the Defense Contract Audit Agency (DCAA) should obtain copies of contractors' internal audit reports. This month, we learned that the USAID Inspector General (IG) obtained a copy of a top USAID contractor's draft internal audit report describing internal control weaknesses. For a copy of this December 26, 2011, IG report, please go to <http://www.usaid.gov/oig/public/fy12rpts/f-306-12-001-s.pdf>.

Many of the disallowed costs cited in the IG's report, which were not contained in the contractor's report, related to the absence of competition for supply contracts, apparently missing documentation, or the lack of prior USAID Contracting Officer approvals -- disallowances that are unlikely to be sustained by a reviewing USAID Contracting Officer.

However, this action by the Inspector General (IG) may signal increased aggressiveness by the IG to force other contractors and recipients to turn over their internal audit reports. After all, using organizations' own internal audit reports would substantially increase the efficiency of the OIG's scarce audit resources.

For this reason, organizations with inhouse or contracted internal auditors should place additional controls over such reporting. Specifically, they should encourage their auditors not to perform the typical auditor "two-step." That is, when auditors don't find a piece of paper supporting an incurred cost, they typically write up the organization for this finding. In such circumstances, program or financial staff should be given additional time to contact the vendor, etc. to obtain the necessary supporting documentation.

Moreover, there should be no place for internal auditors reporting unreasonable costs; this is the task for government auditors. If the internal auditors consider any salary or benefit cost to be somewhat high, they should give program managers the opportunity to find comparative financial data to support such costs.

When it comes to purportedly unapproved costs, the internal auditors should prepare a supplemental schedule, not part of the audit report, listing each of them and giving program managers the time to obtain such approvals from the appropriate USAID official.

A sole source or uncompetitive subcontract or subgrant award should be justified in a "Neg. Memo." These should be prepared soon after the auditors come across any such unsupported awards.

It is not the place of internal auditors to be indicting their own organizations. Internal auditors should be working to find shortfalls, if any, and to have them remedied before

the report is finalized. In light of the release of this IG audit report and possibly others, the management of other organizations should be getting more involved with Internal Audit.

[Editor's Note: The organization which is the subject of this article acquired an affiliated firm of this Newsletter.]

#### AUDITS OF \$500 MILLION IN USAID/WASHINGTON AWARDS TO FOREIGN RECIPIENTS EITHER INCOMPLETE OR NOT SUBMITTED, OIG FINDS

An institutional support contractor is responsible for administering the paperwork in awards of USAID's Office of Foreign Disaster Assistance. The Contract Audit and Support (CAS) Division of the Office of Acquisition and Assistance (OAA) is responsible for determining the financial audit requirements applicable to foreign (and U.S.) recipients of USAID/Washington awards and ensuring that required audits of them are performed. The division of labor for audit oversight of these OFDA foreign recipients between the two parties should be smooth, but has not been.

The USAID OIG issued a December 28, 2011, "Review of Audits of Foreign Organizations Expending Centrally Funded Assistance" (Report No. 2-000-12-002-S), available at <http://www.usaid.gov/oig/public/fy12rpts/2-000-12-002-s.pdf>, reporting that about a half a billion dollars in USAID-provided funding was not audited. Moreover, only 32 of 84 foreign recipients with estimated expenditures of \$500,000 (\$500,000 was used as the threshold due to the absence of a reliable reporting system, even though \$300,000 presently is the threshold as specified in ADS 591.3.2 for non-U.S. recipients) or more had an audit performed, and 13 of the audits were incomplete because they did not cover all USAID awards to the recipients.

The OIG made the Contract Audit and Support Division the fall-guy for the deficiencies cited in this report.

There are some big-name foreign recipients reported therein with incomplete audits, namely, Action contre la Faim/France, German Agro Action, GOAL, Medair, Norwegian Refugee Council, and Oxfam GB. In one instance, ten USAID/Washington funded awards were not included in the recipient's audit.

For these audits, the OIG has recommended that those foreign recipients with active awards be reaudited for FY 2009 according to the "Guidelines for Financial Audits Contracted by Foreign Recipients." For those recipients unable or unwilling to have these reaudits performed, the OIG recommended that the cost of the noncompliant audits not be reimbursed with USAID-provided funds. At the very least, heightened scrutiny of these recipients should be exerted in subsequent periods, the OIG went on to recommend.

In addition, the report lists the names of 52 centrally-funded foreign recipients for whom no audits for FY 2009 were presented to the OIG, including such recipients as: Aga Khan Foundation (Mozambique), Caritas Senegal & Peru, Fauna and Flora International,

Global Alliance for Improved Nutrition (GAIN), HOPE worldwide, Instituto Libertad y Democracia, Kara Counselling and Training Trust, Medical Emergency Relief International (MERLIN), Norwegian People's Aid, People in Need, PRISMA, and the University of Aberdeen.

Over \$400 million of USAID/Washington funding was reported disbursed in 2009 to these 52 foreign implementers and, because no audit was submitted, was not subject to audit scrutiny. For these, the OIG recommended that those with active awards be audited for FY 2009 in accordance with the "Guidelines."

#### USAID OIG REPORTS TOP RECIPIENT'S SUBAWARDS REQUIRE PRIOR AGREEMENT OFFICER APPROVAL, NOT THE AOTR'S

In USAID OIG Report No. 1-521-12-002-P, December 30, 2011, entitled "Audit of USAID/Haiti's Community Health and AIDS Mitigation Project," available at <http://www.usaid.gov/oig/public/fy12rpts/1-521-12-002-p.pdf>, the OIG found that a top USAID recipient had not obtained prior Agreement Officer subaward approvals, relying upon its internal written policy that mistakenly provided for Agreement Officer Technical Representation (AOTR) approvals for subawards that were \$500,000 or less.

According to 22 CFR 226.25(c)(8), for nonconstruction awards, recipients shall request prior approvals from the USAID Agreement Officer (AO) for the subaward, transfer or contracting out of any work under an award, unless described in the application and funded in the approved budget of the award or unless the purchase involves supplies, material, equipment or general support services. Accordingly, the prime recipient must obtain approval of all subawards by the AO.

The Mission did not comply with the aforementioned regulation. The OIG audit reviewed 13 subawards and noted the following:

- The AO confirmed that this prime recipient is required to have AO approval for all subawards and that the current AOTR designation letter does not give the AOTR authority to approve subawards for the project. Yet, in four cases, the AOTR approved the subawards.
- USAID proved initial approval for four of the subawards for a 6-month period; after that, this prime recipient extended the awards (three awards with increases) with no approval from USAID
- No record of USAID approval was found for one of the awards.

In response, the named prime recipient stated that, because several of the subawardees were in the original budget, it did not seek additional approval from the Mission. However, the agreement referenced only two of the subawardees. Because the other subawardees were not included, the AO was required to approve each.

Subawards were issued without the proper approval by the AO because of confusion between the prime recipient and USAID/Haiti regarding the approval requirements. For

example, the recipient’s grants manual did not accurately reflect USAID policy for subawards, stating that the AOTR had authority to approve subawards that were \$500,000 or less. In addition, the AOTR designation letter was revised several times, one revision included clear authority for subaward approvals. (The current designation letter does not contain any authority to approve subawards.)

As a result, some of the subawardees working on the project have not received appropriate reviews and approvals, and USAID/Haiti’s Office of Financial Management may not have conducted payment verification review for these subawardees. Furthermore, it is possible that the Mission’s other programs may have similar problems regarding subaward approvals.

**OIG AUDIT REPORT SHOWS HOW NOT TO MANAGE A COOPERATIVE AGREEMENT BUDGET**

In USAID OIG “Audit of USAID/Sierra Leone’s Agricultural Activities,” Audit Report No. 7-636-12-003-P, December 20, 2011, available at <http://www.usaid.gov/oig/public/fy12rpts/7-636-12-003-p.pdf>, a major recipient significantly overran multiple budget line items without prior approval from USAID on a \$13.2 million, 4-year cooperative agreement.

22 CFR 226.25(a) provides “the budget plan is the financial expression of the project or program as approved during the award process.” Subsection (b) states “Recipients are required to report deviations from the budget and program plans, and request prior approvals for budget and program plan revisions in accordance with this section.”

On this project, the recipient overran the budget on ten line-items, amounting to \$794,664, without prior approval from USAID, as shown next

<u>Line Item</u>	<u>Approved Budget</u>	<u>Actual Costs</u>	<u>Overrun</u>
Fringe Benefits	\$472,912	\$539,471	\$66,559
Travel	183,457	397,138	213,681
Professional Fees	0	99,930	99,930
Equipment & Commodities	424,097	591,570	167,473
Office Supplies & Postage	0	89,489	89,489
Communications	0	103,738	103,738
Publications & Printing Fees	0	35,236	35,236
Meetings & Conferences	0	5,655	5,655
Staff Development & Recruitment	0	5,962	5,962
Staff Recruitment (sic)	0	6,941	6,941
<b>Total</b>	<b>\$1,080,466</b>	<b>\$1,875,130</b>	<b>\$794,664</b>

The recipient's chief of party reported that he recognized that the budget was too small very shortly after the implementation started. Local housing and utility costs were found to be much higher than the budgeted costs once the recipient was on the ground in Sierra Leone.

According to the chief of party, the original budget also underestimated costs -- increasing fuel costs and the high maintenance costs for program vehicles -- associated with regularly sending technical experts from Freetown to the program implementation sites in four of Sierra Leone's most remote districts.

Furthermore, the recipient reportedly focused little on program activities while overspending significantly on administrative costs, the OIG reported. For example, with one year of implementation remaining, the recipient had expended about 97.5% of its total funding, incurring cost overruns on ten line items reacted to administrative costs. However, it had issued only \$508,433 of the \$1 million program budget allocated for the issuance of grants to beneficiaries. This record stood in stark contrast to that of its subpartners, which had both made notable progress in program implementation and still had 23.5% of their budgeted funds remaining.

What is most revealing about this situation is: "Instead of working with USAID to resolve the budget problem, the chief of party only discussed the budget problems with the [recipient's] home office." Chiefs of party must initiate contacts with their USAID counterparts when problems like this come up.

[Editor's Note: Why wasn't the 10% of the bottom-line budgetary discretion in 22 CFR 226.25(f) for line-item variances observed on this project budget and cited in this OIG report. This would have afforded the recipient up to \$1.32 million in direct-to-direct line-item authority vs. \$794,664 the recipient varied from for all these line items? Secondly, why aren't many of USAID Missions observing the Budget guidance in its Sample Award Format and Schedule, available at ADS 303.5r, which states: "Note - the items included in the Budget, including local cost financing items, should relate to the results, activities or functions ... not to specific cost items (such as salaries or travel) ...?"]

#### USAID MISSION CAN'T FIGURE OUT HOW TO DISPOSE OF A RECIPIENT'S TOTALED VEHICLE AND INSURANCE PROCEEDS

In USAID OIG Report No. 6-268-12-004-P available at <http://www.usaid.gov/oig/public/fy12rpts/6-268-12-004-p.pdf>, USAID/RIG Cairo invoked 22 CFR 226.34 for the need of a recipient to obtain prior approval from the Agreement Officer (AO) for disposition of the remains of a vehicle totaled in an accident.

While driving a USAID-funded vehicle, a recipient employee was involved in an accident that totaled the vehicle. In accordance with the vehicle's insurance policy, an insurance company determined the damaged vehicle to be a total loss valued at \$8,000. Although the recipient submitted the insurance reports to the AOTR and requested guidance regarding the disposal of the vehicle, the AOTR did not request disposition

instructions from the cognizant AO. Moreover, the AOTR at the time stated that USAID does not get involved in the terms of the implementer's contract with an insurance company.

According to the current AOTR, she was not aware that AO approval was needed prior to disposition of equipment. In addition, Mission officials stated that the AOTR made an error in responding that USAID does not get involved in the terms of the implementer's contract with an insurance company.

The AO did not ensure that the recipient used the proceeds from the totaled vehicle loss toward project expenditures, the RIG also reported. According to USAID/Lebanon officials, the recipient deposited the insurance funds in its account and expected instructions from USAID on procedures to reimburse the project. As a result, the AO could not make a disposition determination that would allow the \$8,000 from the insurance company to be put to better use.

RIG/Cairo opined that, if USAID-funded equipment has been destroyed, is not usable, and does not reach its projected remaining service life, the AOTR and the implementer should inform "management officials," not stated, but presumably the AO, and ask for instructions on proper disposition.

#### DCAA REVISES ITS "GUIDE FOR DETERMINING ADEQUACY OF CONTRACTOR INCURRED COST PROPOSAL" CALLING FOR SUBMISSION OF SCHEDULES, NOT THE INCURRED COST ELECTRONICALLY (ICE)

At 11-PPD-020, dated November 4, 2011, available at <http://www.dcaa.mil> under the left-hand sidebar titled "Open Audit Guidance," the Defense Contract Audit Agency (DCAA) has revised its "Guide for Determining Adequacy of Contractor Incurred Cost Proposal" to provide a more comprehensive guide for its auditors to use in determining the adequacy of final indirect cost proposals. Auditors are reminded to evaluate the contractor's incurred cost submission for adequacy upon receipt and immediately notify the Contracting Officer and contractor, in writing, of significant inadequacies.

In its instructions to its auditors, DCAA provides that the proposal should contain all the required, as it calls them, "schedules." It goes on to state that, if the contractor generates internal reports identifying the required information in lieu of the example schedule, the auditor should reference the contractor report on this form where the applicable schedule is listed. All information contained in the example schedules or internal reports, if applicable, as required by FAR 52.216-7(d), must be provided or made available to determine proposal adequacy. As such, it does not mandate that contractors submit its proposal in the format of the Incurred Cost Electronically (ICE), which is also available at DCAA's website, but you know that DCAA auditors will still prefer and encourage contractors to use ICE.

Following up on the above article on the IG obtaining a top USAID contractor's draft internal audit report, FAR 52.216-7(d)(2)(iv)(I) does provide for the submission, as part

of the incurred cost proposal, of a list of all internal audit reports issued since the last disclosure of internal audit reports to the Government, and Subsection (J) follows this up with the submission of the annual audit plan of scheduled [internal] audits to be performed in the fiscal year when the final indirect cost rate submission is made, as supplemental information that could be required during the audit process.

DCAA's newest Memorandum for Regional Directors, 11-PAC-021, December 14, 2011, alerts its auditors to its existing policy to consider compliance with the applicable Cost Accounting Standards (CAS) in every contract audit. Current DCAA policy also states that a comprehensive audit of compliance with each applicable CAS standard, except for the consistency standards in CAS 401, 402, 405 and 406, shall be conducted once every three years, unless circumstances warrant conducting the audit earlier.

#### NGO EXECUTIVE DIRECTOR SENTENCED TO ALMOST 5 YEARS IN JAIL FOR ILLEGAL FUNDS TRANSFERS TO IRAQ, IMPLICATED FORMER CONGRESSMAN GETS 1 YEAR

According to a January 11 article appearing in the *Kansas City Star*, a long-running terrorist financing investigation ended when a Federal judge ordered two men, including a former U.S. Congressman, to prison.

U.S. District Judge Nanette Laughrey also sentenced three other defendants to probation for their work with a Missouri organization that purportedly had ties to Islamic extremists. Those ties had subjected the organization to intense scrutiny for 13 years.

All five men either were employees or associates of the USAID-funded Islamic American Relief Agency (not to be confused with a namesake, the Islamic Relief Agency, an entirely different and highly reputable organization). The organization closed its doors in October 2004 after the U.S. Treasury Department declared it to be one piece of a global network, based in Khartoum, Sudan, that supported Osama bin Laden and other terrorists.

Most of the defendants sentenced pleaded guilty to illegally funneling money to Iraq in violation of economic sanctions enacted during the Saddam Hussein era. Others pleaded guilty to acting as unregistered foreign agents while representing the NGO before the U.S. government.

Those sentenced:

- Mubarak Hamed, the NGO's executive director, to four years and 10 months in prison for sending more than \$1 million to Iraq in violations of U.S. sanctions
- Former Michigan Rep. Mark Deli Siljander, to one year and a day in prison for obstruction of justice and acting as an unregistered foreign agent.
- Abdel Azim Elsiddig, a part-time fundraiser, to two years of probation for acting as an unregistered foreign agent.
- Ali Mohamed Bagegni, a board member, to six months of probation and 50 hours of community service for violating the Iraq sanctions law.

- Ahmad Mustafa, a fundraiser, to six months of probation and 50 hours of community service for his role in the sanctions violations.

Judge Laughrey heaped the most criticism on Hamed, the NGO's executive director, who sent more than \$1.5 million meant for humanitarian work in Iraq without getting the proper permission from the U.S. government. The money went through a middleman in Jordan, Khalid Ahmad Jumah Al-Sudani, whose ties to terrorists earned him a special terrorist designation in 2004.

At his guilty plea in July 2010, Elsiddig admitted that he hired and paid former Congressman Siljander to persuade government officials to remove the organization from a Senate Finance Committee list of Islamic organizations suspected of supporting terrorism and to restore the NGO's ability to receive U.S. government awards.

On December 20 and 21, 1999, for the first time ever involving any recipient, USAID terminated two cooperative agreements to IARA in accordance with 22 CFR 226.61(a)(3), determining that continuing such agreements is not in the "national interest of the United States." In connection with this, attorneys for IARA appealed the national interest terminations to USAID's then Assistance Executive Marcus L. Stevenson who denied IARA's appeal on February 26, 2000.

In his plea agreement, former Congressman Siljander admitted that he lied to Federal authorities about the organization's payments to him, telling them that the money was to have assisted him in writing a book about reconciling differences between Muslims and Christians.

Judge Nanette Laughrey noted that Siljander's lobbying ultimately was ineffective, but she said he needed prison time primarily to serve as a deterrent to others. "When you look at this objectively, it was not the case of someone aiding a terrorist and it would be wrong of me to do that," Laughrey said.

The remaining defendants, each of whom received probation, became ensnared in the case because of Hamed's decisions, Laughrey noted.

Mustafa violated the sanctions when he sent \$800 to his brother in Iraq to keep him from losing his home. Mustafa's brother had declined to join Saddam's Baath Party and could not depend on government support.

Begegni, the only IARA board member, signed checks as directed by Hamed. Laughrey called his transgression a "technical violation" and said he played a "very, very minor role."

This court action ends a long and very sad saga of an organization that veered from the right path.

Separately, Neil Campbell, an Australian and an ex-agent for the International Organization on Migration working with USAID, was sentenced to 22 months in prison for seeking \$190,000 in payments as a reward for steering U.S.-funded contracts in Afghanistan. Also in Afghanistan, an Afghan national was arrested on bribery charges for demanding and receiving a kickback in exchange for processing a grant to a program beneficiary.

#### SINCE BANKRUPT FIRM FAILED TO LIST CLAIM FOR \$1.5 MILLION IN SCHEDULE OF ASSETS, ITS SUCCESSOR LACKS STANDING TO PURSUE RECOVERY AGAINST USAID

In *USCS Chemical Chartering LLC v. Agency for International Development*, CBCA No. 2058, January 11, 2012, appellant's predecessor, Chemical I, filed a certified claim for \$1,505,833 with the USAID Contracting Officer on March 9, 2009, under the Delivery Delay Assessment(s) clause of the contract.

This decision is available at <http://www.cbca.gsa.gov>. Point-and-click at "Decisions" on the left-hand sidebar, then to "Appeals Decisions" on the next page, and scroll down and point to January 2012, and finally to USCS Chemical Chartering appearing on the following page.

This claim arose as a result of a delay in berthing at the port of Djibouti to discharge a shipment of bulk grain intended for Mekele and Dessie, Ethiopia. The claim asserted that the contractor had suffered damages in the amount of \$40,000 per day for 37.6 days while "on detention" at Djibouti.

In rejecting the claim on April 15, 2010, the USAID Contracting Officer held the "claim to be unfounded as the very nature of the emergency cargo going into a region with known infrastructure challenges is an understood risk accepted by experienced transportation providers servicing the region." Further, she said that USAID has "limited or no control over port operations at a foreign port and cannot be held responsible for events outside its control." Soon thereafter, an appeal of her decision denying the claim was filed with the Civilian Board of Contract Appeals (CBCA).

The appellant's predecessor subsequently filed for Chapter 11 bankruptcy, becoming Chemical II, but did not list the claim against USAID as an asset. On March 31, 2010, the bankruptcy court issued its final order and appellant emerged from bankruptcy. As noted above, on April 15, 2010, USAID denied the certified claim made by appellant's predecessor. The appellant, Chemical III, in this dispute appeals the denial of the claim made by Chemical I. As argued by Natalie Thingelstad, Office of General Counsel, USAID moves to dismiss on the basis that judicial estoppel bars the claim or that appellant lacks standing to pursue the claim. The CBCA dismisses the claim for lack of standing and does not elaborate on the estoppel argument.

Board Judge Stephen M. Daniels summarizes the case as follows: "The contractor to USAID -- the only party which may have suffered an injury to a legally protected

interest, as a consequence of the Contracting Officer's decision -- was Chemical I. Chemical I no longer exists; whatever assets and liabilities it had, and informed the bankruptcy court about, have now been assumed, through reorganization sanctioned by that court, by Chemical III. Chemical III may proceed with this case only if one of the Chemical I assets it holds is the right to proceed with the Chemical I claim which was presented to the Contracting Officer."

"It is clear that Chemical III does not own that right. Under 11 U.S.C. § 554, property of a bankruptcy estate may be abandoned by the trustee in bankruptcy or by order of the bankruptcy court. Unless the court orders otherwise, property which is listed on a debtor's schedule of assets, and the disposition of which is not provided for by the order ending the proceedings, is considered to have been abandoned to the debtor. However, property which is not listed on a schedule remains property of the bankruptcy estate."

"Because Chemical I's claim against USAID was not listed on the schedule of assets the debtor presented to the bankruptcy court, it did not pass to Chemical III when that court approved reorganization of USCS Chemical Chartering LLC. Instead, ownership of the claim remained with Chemical II. Chemical III consequently has no right to pursue it."

#### **MAERSK TO PAY \$31.9 MILLION TO RESOLVE FALSE CLAIMS ALLEGATIONS FOR INFLATED SHIPPING CHARGES TO AFGHANISTAN AND IRAQ**

Maersk Line Limited has agreed to pay the government \$31.9 million to resolve allegations that it submitted false claims to the United States in connection with contracts to transport cargo in shipping containers to support U.S. troops in Afghanistan and Iraq, the Justice Department announced today. The government alleges that Maersk knowingly overcharged the Department of Defense to transport thousands of containers from ports to inland delivery destinations in Iraq and Afghanistan.

The government contends that Maersk inflated its invoices in various ways. For example, Maersk allegedly billed in excess of the contractual rate to maintain the operation of refrigerated containers holding perishable cargo at a port in Karachi, Pakistan, and at U.S. military bases in Afghanistan; allegedly billed excessive detention charges (or late fees) by failing to account for cargo transit times and a contractual grace period; allegedly billed for container delivery delays improperly attributed to the U.S. government; allegedly billed for container GPS-tracking and security services that were not provided or only partially provided; and allegedly failed to credit the government for rebates of container storage fees received by Maersk's subcontractor at a Kuwaiti port.

#### **WHISTLEBLOWERS EARN A RECORD \$532 MILLION IN 2011**

Whistleblowers earned more than \$532 million in 2011 through lawsuits alleging fraud against the U.S. government, a record for such payouts, according to a law firm study recently published.

Private parties suing on the behalf of the government collected \$140 million more than they did the previous year, even as the Justice Department's total civil fraud sanctions remained consistent, the law firm Gibson, Dunn & Crutcher said.

The DOJ recovered some \$3.02 billion last year through cases under the False Claims Act -- the third-largest recovery ever, just shy of the \$3.09 billion it won through cases in 2010.

But for the whistleblowers that helped bring them, 2011 was an even better year. "The bounty provisions are so attractive," said Andrew Tulumello, who helps lead Gibson Dunn's Washington office and worked on the report. "When you look at \$532 million going to basically the plaintiff's bar, that is going to attract more and more interest."

The Justice Department has used the Civil War-era law, designed to root out unscrupulous contractors, to aggressively go after healthcare providers and pharmaceutical companies for overcharging Medicare and Medicaid.

The law provides for whistleblowers to earn up to 30 percent of any recovery and in recent years such tipsters -- referred to as relators in False Claims parlance -- have helped bring an increasing number of the government's cases.

Eighty-four percent of such cases opened last year were brought by whistleblowers, up from 75 percent the year before. Twenty-five years ago, only 8 percent of the government's cases were based on lawsuits from relators.

The record payouts in 2011 come amid the ramp-up of a new whistleblower bounty program created by the Dodd-Frank financial regulatory overhaul to encourage individuals with information about securities law violations to come forward. That program has yet to provide its first award.

The 2011 numbers -- based on the government's fiscal year from October through September -- are helped by one of the largest payouts ever, to a former GlaxoSmithKline Plc (GSK) employee.

In October 2010, a GSK quality manager won \$96 million for exposing manufacturing defects at a plant in Puerto Rico. The company paid \$750 million to settle the charges. Whistleblowers earn a cut based on how far they advance a case before the government takes over. In cases where the Justice Department declines to intervene, they can win an even greater share of any eventual settlement.

The vast majority of the 2011 awards -- some \$490 million -- came in cases where the Justice Department joined the case. Another \$42 million came from cases the government declined to pursue.

## NEW TAX PROVISIONS FOR 2012

With the ringing in of the new year, several new tax provisions took effect. While the list of new items does not compare with the number of tax provisions that expired at the end of 2011, organizations should be aware of what has changed.

#### Inflation Adjustment:

The standard mileage rate for business use of an automobile remains at 55½ cents per mile for 2012; for medical and moving expenses it decreases to 23 cents per mile (Notice 2012-1), down a half-cent from the second half of 2011.

#### Veterans Work Opportunity Credits:

The Three Percent Withholding Repeal and Job Creation Act, P.L. 112-56, extended the work opportunity tax credit (now called the returning heroes and wounded warriors work opportunity tax credits) for businesses that hire certain military veterans. Employers will be eligible for a credit of up to \$9,600 for each qualified veteran that they hire after the law's enactment date (November 21, 2011) and before January 1, 2013.

Under the returning heroes tax credit, an employer may be eligible for a credit of up to \$2,400 for hiring a veteran who has been unemployed for at least four weeks and up to \$5,600 for hiring a veteran who has been unemployed for more than six months. Under the wounded warriors tax credit, an employer may be eligible for a credit of up to \$9,600 for hiring a veteran with a service-connected disability who has been unemployed for more than six months and up to \$4,800 for hiring a veteran with a service-connected disability (who does not meet the returning hero credit requirements) or who qualifies as a food stamp recipient.

#### Foreign Asset Reporting:

Under the Foreign Account Tax Compliance Act, individuals are required to report interests in specified foreign financial assets when filing their federal income tax returns (Sec. 6038D). This requirement was suspended until the Form 8938, *Statement of Specified Foreign Financial Assets*, was released (Notice 2011-55). The IRS posted the final version of the form and its instructions in December; taxpayers subject to the reporting requirement must file the form in 2012 for 2011 tax years. In addition, taxpayers who would have been required (except for the suspension of the requirement) to file Form 8938 in 2011 for a tax year that began after March 18, 2010, must file it for the prior year with their return for the current tax year.

#### Bonus Depreciation:

The 100% first-year bonus depreciation provision expired on December 31, but 50% bonus depreciation is available for property placed in service in 2012. (100% bonus depreciation does still apply in the case of certain longer-lived and transportation property placed in service before 2013.)

## Voluntary Classification Settlement Program:

A new voluntary classification settlement program (VCSP) introduced in September (Announcement 2011-64)) allows eligible taxpayers to voluntarily reclassify their workers as employees for federal employment tax purposes for future tax periods while receiving relief for part of the tax liability relating to the past treatment of the workers as nonemployees. Taxpayers are eligible if they have consistently treated the workers as nonemployees, filed all required Forms 1099 for the previous three years, are not currently under IRS audit, are not currently under audit by the U.S. Department of Labor or a state agency, and complied with the audit results if the taxpayers were previously audited by the IRS or the Department of Labor.

The VCSP limits the tax liability to 10% of the employment tax liability that would have been due on the compensation paid to the workers in the most recent tax year, as calculated under the reduced rates of Sec. 3509. Interest and penalties are not charged on the liability.

The classification of these workers for prior years is not subject to an employment tax audit, but the statute of limitation on assessment of employment taxes is extended from three to six years for the first, second and third calendar years beginning after the date the taxpayers begin treating the workers as employees under the VCSP closing agreement.

## NEW IRS FORM 990 CONTAINS A FEW SIGNIFICANT CHANGES FOR 2011

The IRS posted the final 2011 Form 990, *Return of Organization Exempt From Income Tax*, and instructions on its website at <http://www.irs.gov/pub/irs-pdf/i990.pdf>. Form 990 has become more complex as the role of nonprofit organizations has evolved in the United States.

The latest version of the form contains a few significant changes, among them the requirement that an organization must complete Form 990, Part I of Schedule F, *Statement of Activities Outside the United States*, if it had foreign investments during the tax year valued at \$100,000 or more. Previously, Part I of Schedule F needed to be completed only if the organization had aggregate revenues or expenses of more than \$10,000 attributable to various foreign activities.

Another big change is the new requirement that an organization complete Part X, Balance Sheet, by reporting its distributive share of assets in any joint ventures and other entities treated as partnerships for federal tax purposes according to the ending capital account in the partnership reported on Schedule K-1.

Other changes/clarifications listed by the IRS include: (1) Contributions of conservation easements and other qualified conservation contributions must be reported consistently with how the organization reports revenue from such contributions in its books, records and financial statements, and (2) the organization's distributive share of investment

income, royalties and rental income from joint ventures should be reported on specific lines of Part VIII, Statement of Revenue.

Line 26 instructions clarify how joint costs should be reported and when the Statement of Position (SOP) 98-2, *Accounting for Costs of Activities of Not-for-Profit Organizations and State and Local Governmental Entities That Include Fund Raising* box should be checked.

The Form 990 instructions contain several changes to the Form 990 Glossary, including revising the definition of “grants and other assistance” to exclude certain payments by voluntary employees’ beneficiary associations. The definition of “significant disposition of net assets” is revised to exclude grants or other assistance made in the ordinary course of the organization’s exempt activities to accomplish the organization’s exempt purposes.

Another definition that meaningfully changed is “term endowment.” Term endowment is renamed “Temporary restricted endowment” and includes not only endowment funds established by donor-restricted gifts for a specified period, but all other temporarily restricted net assets held in a donor-restricted endowment, including income from permanent endowments.

#### PRIMES AWARDING NICRAs TO SUBCONTRACTORS/RECIPIENTS

There has been continuing uncertainty among prime contractors/recipients as to whether they could award a negotiated indirect cost rate agreement (NICRA) to a subcontractor/recipient, whether a U.S. or non-U.S. entity and whether affiliated or non-affiliated, lacking one issued by a Federal cognizant agency.

On May 31, 2011, FAR Clause 52.216-7(d)(v)(5) was added specifying the authority of a prime with regard to indirect costs, providing that “*the completion invoice or voucher shall include settled subcontract amounts and [importantly] rates. The prime contractor is responsible for settling subcontractor amounts and rates...*” This policy position should apply equally to grants and cooperative agreements.

To award a NICRA to a subcontractor/recipient, the prime would have to receive an indirect cost rate proposal from the subcontractor/recipient and negotiate the rate(s) with the sub. Preferably, the subcontractor/recipient could furnish audited financial statements for the prior three fiscal years in order to arrive at a plausible estimate of the sub’s costs for the prospective fiscal year. Lacking this, the sub’s indirect cost rate proposal should be reviewed by a certified public accountant knowledgeable of indirect costs.

To withstand later possible questioning, it would be wise for the prime to thoroughly document the steps it went through in performing cost analysis of the indirect cost rate proposal and awarding the NICRA to the sub. It also would not be unwise for the prime to notify the Contracting/Agreement Officer, in writing, of its findings and determinations in awarding the NICRA. The prime should also be prepared to submit,

upon request, the results of its indirect cost analysis to USAID to further ensure the transparency of its actions.

Subcontractors/recipients should be made aware that they would have to separately account for their indirect costs and have documentation (i.e., timesheets, etc.) substantiating their actual indirect costs. Furthermore, if the sub is a nonprofit organization, it would have to submit to an audit by its outside auditors with a separate opinion on its indirect costs being issued in accordance with Statement on Auditing Standards No. 29, as part of its OMB Circular A-133 audit for a U.S. entity if it expends more than \$500,000 in federal financial participation, or a “Recipient-Contracting Audit Guide” audit for a non-U.S. entity if it expends more than \$300,000 on USAID awards. For subcontractors on cost-reimbursement contracts, their award above a certain threshold should specify the requirement for an independent audit.

The NICRA obtained from a prime in this circumstance would, however, not be accepted, as such, by a Federal awarding agency when the sub bids on a prime award, and the rate accepted from one prime would probably have to be renegotiated with another prime.

Receiving a prime-issued NICRA would still be advantageous from a forecasting and cost control standpoint to a subcontractor/recipient without a Federally-issued NICRA, instead of charging and accounting for all its project costs directly.

## **UPCOMING SEMINARS**

The Center for Development Excellence (CDE) announces the following seminar schedule for 2012:

*NEW* February 15/USAID Year in Review – Implications for 2012/Bethesda, Maryland

February 19-21/USAID Regulations & Policies/Kabul, Afghanistan

February 22-23/Field Financial Management for USAID Awards/Kabul, Afghanistan

February 28-29/Advanced Award Management/Bethesda, Maryland

March 26-28/USAID Regulations & Policies/Monrovia, Liberia

March 29-30/Field Financial Management for USAID Awards/Monrovia, Liberia

April 16-18/USAID Regulations & Policies/Juba, South Sudan

April 19-20/Field Financial Management for USAID Awards/Juba, South Sudan

May 7-9/USAID Regulations & Policies/Port-au-Prince, Haiti

May 10-11/Field Financial Management for USAID Awards/Port-au-Prince, Haiti

May 16/Preventing Fraud and Embezzlement on USAID Awards/Bethesda, Maryland

June 5/Mastering USAID’s Rules & Regulations/Bethesda, Maryland

June 6-7/Advanced Award Management/Bethesda, Maryland

June 11-13/USAID Regulations & Policies/Dubai, UAE

June 14-15/Field Financial Management for USAID Awards/Dubai, UAE

July 9-11/USAID and CDC Regulations & Policies/Addis Ababa, Ethiopia

July 12-13/Advanced Award Management/Addis Ababa, Ethiopia

July 23-25/Doing Business with USAID/Port-au-Prince, Haiti

September 17-19/USAID Regulations & Policies/Cairo, Egypt

September 20-21/Advanced Award Management/Cairo, Egypt

November 26-28/USAID and CDC Regulations & Policies/Abuja, Nigeria

November 29-30/Field Financial Management for USAID Awards/Abuja, Nigeria

For more information on these seminars, please consult:

<http://www.cderesources.com/trainings/schedule>.

Seminar Fees: 1-Day Seminar: US\$495, 2-Day Seminar: \$695, 3-Day Seminar: \$795; take a 10% discount when registration is for more than one course by the same participant. Prepayment is required.

### **NEW MASTER'S CERTIFICATE PROGRAM**

In recognition of the dedication and advanced knowledge of those participants who have completed a comprehensive set of seminars in a select area, the Center for Development Excellence has instituted a Master's Certificate Program by conferring a **Master's Certificate in USAID Financial Management**, **Master's Certificate in USAID Assistance Management**, and a **Master's Certificate in USAID Contract Management**. These programs require completion of 70 hours of core and elective seminars offered by the Center for Development Excellence, although required seminars completed over the past three years will be recognized towards earning a master's certificate. More information on this Program and its requirements are posted on its webpage at [http://www.cderesources.com/courses\\_trainings/certificates](http://www.cderesources.com/courses_trainings/certificates).

### **ACCOUNTING, FIELD OFFICE FINANCE, PROCUREMENT, SUBGRANTING AND OVERSEAS BENEFITS POLICIES MANUAL SOFTCOPY**

The Center for Development Excellence's "USAID Accounting Policies and Procedures Manual Softcopy" with 177 policies and 51 processes and its 155-page "NGO Field Office Finance Manual Softcopy" contain prewritten policies and procedures for an organization's headquarters and field office accounting operations which will allow you to customize your own policies and procedures manual in as little as a day. The price of each is only US\$395.

The Center for Development Excellence also offers a fully-featured “Procurement Manual” to allow an organization to effectively subcontract for goods and services. This package is suitable to meet the requirements of a contractor procurement system review under FAR 44.3. For those making subgrants, its “Subgranting Manual” should come in handy in managing the entire process of competing, awarding and administering subgrants and subcooperative agreements. This manual reflects the recent changes in USAID’s ADS 303 grantmaking procedures. Each of these manuals is US\$395.

For those organizations with overseas-posted personnel, the Center for Development Excellence offers a complete set of pre-written “Benefits Policies for Overseas Employees” for expatriates, resident-hire U.S. citizens, third country nationals, key local nationals and cooperating country nationals. These fully-researched policies comport to the State Department’s Standardized Regulations, Foreign Affairs Manual and Foreign Affairs Handbook as to allowances, differentials, pay and travel. Guidance is also provided herein on which benefits other NGOs are providing their overseas staff. The price of this softcopy package and guidance is only US\$250.

Operated in a Windows environment, separate softcopy packages are available for nonprofit organizations and for-profit concerns. You may inspect a sample of the USAID Accounting Policies and Procedures Manual and the NGO Field Office Finance Manual at: <http://www.cderesources.com/products>.

## **INDIRECT COST RATE PROPOSAL PREPARATION AND NEGOTIATION OF NICRAs**

Mr. Stross is an expert in preparing indirect cost rate proposals, establishing separate Facilities and Administration (F&A) rates, negotiating NICRAs with USAID’s Overhead Branch, conducting sensitivity analyses of optimum cost recovery structures, restructuring indirect costs, preparing Cost Accounting Standards (CAS) Disclosure Statements, and conducting fiscal assessments of an organization’s indirect costs.

## **AUDIT RESOLUTION**

In responding to an OMB Circular A-133, recipient-contracted or DCAA audit, Mr. Stross can apply his extensive knowledge of authoritative U.S. Government and USAID rules in challenging questioned costs. His expertise is so well regarded that even USAID itself retained him to rebut the major findings in one of its own IG audit reports. He has also consulted with a host of NGOs and contractors in responding to, and negotiating, their audit findings.

## **COMPLIANCE SERVICES**

On a contract basis serving as the organization’s Compliance Officer, a CPA, with 30 years of experience in advising organizations on how to withstand audit disallowances, and 15 years with specific USAID regulatory experience, would conduct a vulnerability assessment of the organization’s compliance with USAID’s rules and regulations, prepare

its policies and procedures, train its key personnel in USAID's compliance requirements, and conduct periodic, risk-based compliance testing of agreed upon high-risk areas, reporting the results solely to the organization's CFO, CEO or Finance/Audit Committee.

## **INTERNET-BASED CONSULTING**

Either over the Internet or by telephone, Robert Stross, who prepares this Newsletter and has over 42 years in the Federal marketplace, provides consultations under retainer to a limited number of NGOs on the range of accounting, bidding, pricing, indirect costing, teaming and contracting, regulatory compliance, and audit resolution issues involving USAID. Inquire about this service and his low initial retainer and hourly rate.

Please consult our homepage at <http://www.robertstrosschartered.net> for more details on these consulting services.

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