



UNITED STATES GENERAL ACCOUNTING OFFICE

WASHINGTON, D.C. 20548

CIVIL DIVISION

JUL 30 1970

Dear Mr. Smith:

The General Accounting Office has reviewed the manner in which independent auditors are used by the Farmers Home Administration (FHA) and the Rural Electrification Administration in administering loan programs. A draft of our proposed report to the Congress on the results of the review was furnished to you for your review and comment on May 28, 1970.

During our review, we noted one other matter--not included in our proposed report to the Congress--which we believe warrants your attention. This matter relates to the need for establishing more specific requirements regarding the types of accounts and records which borrowers should establish and maintain.

Although FHA makes loans to various types of organization borrowers for purposes, such as water and sewer construction, recreation, and grazing, it has not developed specific instructions concerning the types of accounts and other records that should be established and maintained by the different types of borrowers. We believe that the absence of more specific instructions has hindered FHA State and county personnel in the counseling and supervision of borrowers on financial and accounting matters, particularly since many of the personnel do not have specific training in the area of financial management.

Existing FHA instructions provide that borrowers will be required to maintain such accounts as are necessary to successfully continue their operations, meet the requirements of State and local laws and regulations, and meet the terms of their loan agreements with FHA and other creditors. In our view, the instructions should also

- describe the specific type of balance sheet and income accounts and other records that should be maintained by each of the different types of organization borrowers.
- provide criteria or guidelines for use by FHA field personnel in determining whether a borrower's accounts and other records are adequate.

We discussed with 18 FHA county supervisors in the States of Colorado and Idaho their involvement in the establishment of accounts and other records for borrowers. Generally, the supervisors informed us that they

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did not (1) provide advice and assistance to borrowers in the establishment of accounts and other records but, generally relied on the borrowers or their accountants to handle such matters, and (2) determine prior to loan closing, whether the borrowers had established adequate accounts and other records. For the most part, they stated that they were not thoroughly familiar with financial management matters relative to the types of balance sheet and income accounts and other records that should be maintained by borrowers and that prescribed guidelines covering such matters would assist them in carrying out their responsibilities in this area.

In our opinion, appropriate balance sheet and income accounts, and all other records which support entries in the accounts, should be maintained in such a manner that a borrower could readily obtain complete information relative to any item included in any account. Records which a borrower may maintain to supplement the accounts include minute books, financial reports, related correspondence, and memoranda which may be useful in developing the history of, or facts regarding any transaction.

We believe that specific instructions setting forth the accounts and other records which should be maintained by each of the different types of organization borrowers can be useful to FHA field personnel in the supervision of organization-type borrowers, particularly from the standpoint of determining that the borrower's financial policies are being carried out in accordance with loan requirements, and that the financial position of the borrower is being preserved so as to adequately protect the Government's interest.

RECOMMENDATION

We recommend that FHA instructions be revised to define the types of accounts and other records that should be maintained by each of the various types of organization borrowers; and that borrowers be required to meet the requirements set forth in FHA instructions before a loan and/or grant is closed.

We have discussed our recommendation with FHA officials responsible for association loan programs who agreed to consider it in the rewriting of FHA instructions relating to organization borrowers.

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We would appreciate being advised of the specific actions taken pursuant to our recommendation.

Copies of this report are being sent to the Inspector General,
Department of Agriculture.

Sincerely yours,

Victor L. Lowe

Victor L. Lowe
Associate Director

Mr. James V. Smith, Administrator
Farmers Home Administration
Department of Agriculture