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BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The President Of The Overseas Private Investment Corporation

Examination Of Fiscal Year 1981 Overseas Private Investment Corporation Financial Statements And Related Issues

The overseas Private Investment Corporation's fiscal year 1981 financial statements present fairly the corporation's financial position at September 30, 1981, and its operating results for the year then ended. GAO found that

--the Corporation's insurance and guaranty reserves appear to be adequate to cover existing commitments,

--the Corporation did not fully disclose the effects of delinquent project financing in its statement, and

--tighter control and monitoring of the Corporation's administrative expenditures were needed.

GAO's recommendations are aimed at improving the Corporation's financial disclosures and oversight of its activities.

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GAO/ID-82-33

AUGUST 16, 1982

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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

INTERNATIONAL DIVISION

B-201607

The Honorable Craig A. Nalen
President, Overseas Private
Investment Corporation

Dear Mr. Nalen:

This report supplements our opinion on the examination of the Overseas Private Investment Corporation's comparative financial statements for fiscal years 1981 and 1980, which was previously sent to your Board of Directors on February 17, 1982. The report discusses weaknesses in the Corporation's financial reporting and administrative controls which are of concern but not of sufficient materiality to adversely affect our opinion on the statements.

Our examination was made pursuant to the Government Corporation Control Act (31 U.S.C. 841-871) and in accordance with Comptroller General standards for financial and compliance audits.

This report contains recommendations to you on pages 10, 16, 20, and 25. As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the agency's first request for appropriations made more than 60 days after the date of the report.

Copies of this report are being sent to the Director, Office of Management and Budget; the Secretary of the Treasury; the Director, Office of Personnel Management; the Administrator, Agency for International Development; and appropriate congressional committees.

Sincerely yours,

Frank C Conahan

Frank C. Conahan
Director

GENERAL ACCOUNTING OFFICE REPORT TO THE PRESIDENT OF THE OVERSEAS PRIVATE INVESTMENT CORPORATION

EXAMINATION OF FISCAL YEAR 1981 OVERSEAS PRIVATE INVESTMENT CORPORATION FINANCIAL STATEMENTS AND TREATY RELATED ISSUES

D I G E S T

GAO's examination of the Overseas Private Investment Corporation's fiscal year 1981 financial statements disclosed no exception, weakness of internal control, or departure from law and regulation having a material impact on its financial position at September 30, 1981, and its operating results for the year then ended. GAO found, however, that the Corporation

--was experiencing significant losses on its loans,

--did not fully disclose the effects of its financial policies regarding delinquent projects, and

--lacked controls necessary to ensure that certain administrative costs were in accord with congressional intent and Federal guidelines.

In addition, GAO concluded that the Corporation's insurance and guaranty reserves of $664 million were adequate to discharge obligations arising from its estimated maximum exposure of $3.3 billion.

LOAN PROGRAM INCURS LOSSES

The Corporation is a profitmaking and self-sustaining insurer and guarantor of U.S. private investments in friendly developing countries. It also makes direct loans to small businesses in these countries, but this program operates at a loss. Overall net income in fiscal year 1981 was $76 million, mainly derived from interest on investment of fees and reserve funds in U.S. Treasury securities. Since the Corporation does not maintain its accounts by program category, GAO could not determine the extent of its loan program costs. However, the Corporation's fiscal year 1981 net income, and possibly its future earnings, were being appreciably diminished on projects it financed by

--loan write-offs and settlement costs,

Tear Sheet

--delinquent interest revenue, and

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--guaranty claims payments.

A provision in the Overseas Private Investment Corporation Amendments Act of 1981 could make more development loan funds available in fiscal year 1982 and subsequent years. In view of the high loan loss rate currently being experienced (estimated at 20 percent), GAO thinks the Congress should be fully informed about this loss experience and recommends that OPIC seek congressional clarification regarding how proposed additional loan funds are to be made available. (See p. 16.)

EFFECTS OF FINANCIAL POLICIES NOT FULLY DISCLOSED

The Corporation did not disclose the effects of its policy not to recognize delinquent interest on finance projects as revenue until the interest is received. The cumulative amount of such uncollected (and unrecognized) interest revenue due OPIC at September 30, 1981, was $4.8 million, including $1.2 million representing one-fourth of the total investment interest "earned" during fiscal year 1981.

There were 10 investment projects in delinquency status at year-end, with an outstanding balance of $15.7 million. Of this amount, $5.4 million was for direct loans and $10.3 million was for claims related assets obtained as a result of claims payments made by the Corporation pursuant to its guaranties.

Also, costs incurred in connection with the Corporation's direct loan fund may have been substantially greater than the $7.8 million shown as realized losses in the financial statements because administrative expenses such as private legal costs incurred in connection with loan settlements have been charged to overall operations rather than to the loan fund.

GAO recommends that the Corporation make these disclosures and account for all loan fund gains and losses in presenting future years' financial statements. (See p. 10.)

NEED FOR TIGHTER ADMINISTRATIVE CONTROLS

GAO also observed a need for tighter financial management controls and closer audit surveillance over the Corporation's administrative expenditures. Operating policies were not clearly defined and certain costs, including employee business entertainment and cash incentive awards, lacked adequate documentation or appeared to be high in relation to established ceilings and guidelines.

GAO recommends that OPIC obtain congressional clarification regarding what costs should be charged against OPIC's ceiling for entertainment. (See p. 20.)

GAO also recommends that the Corporation's President require that significant operating policies be placed in writing and that he request AID's Inspector General to monitor and review these administrative controls and related expenditures more closely. (See p. 24.)

AGENCY COMMENTS AND GAO EVALUATION

OPIC disagrees with the report recommendations. It acknowledges GAO's reporting responsibility to the Congress but feels that the recommended financial statement disclosures and accounting change are unnecessary and inappropriate. Also, while OPIC agreed to prepare certain more formal and detailed policies and procedures, it commented that because its senior management was involved in all expenditure matters there was no need to have the same volume of policies and procedures that might exist in a larger agency with an extended chain of command.

GAO believes full disclosure of significant operating and program data is essential for complete and useful financial reporting and need not increase the risk to OPIC of delinquent payments by borrowers. Also, while GAO notes that OPIC's enabling legislation confers on it great discretion over how it may make expenditures, better documentation of agency policies and procedures will allow more effective review of OPIC expenditures in future years.

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ABBREVIATIONS

AID	Agency for International Development
DIF	Direct Investment Fund
GAO	General Accounting Office
OPIC	Overseas Private Investment Corporation
OPM	Office of Personnel Management

CHAPTER 1

INTRODUCTION

The Overseas Private Investment Corporation (OPIC) was created by the Foreign Assistance Act of 1969 (Public Law 91-175, Dec. 30, 1969) to mobilize and facilitate the participation of U.S. private capital and skills in the economic and social development of developing friendly countries. OPIC accomplishes its mission primarily by insuring U.S. investors against political risks. It also guarantees repayment of U.S. investments, makes loans, and finances pre-investment surveys. Before OPIC's creation, these functions were performed by the Agency for International Development (AID).

OPIC assumed some of the assets and all of the liabilities of AID's predecessor investment insurance program. In its start-up years, OPIC received appropriations of $106.25 million for its operations and reserves to augment approximately $98 million in program funds transferred from AID. These funds were made available to OPIC to support OPIC assumption of liability with respect to AID-issued insurance and guaranty contracts having a face amount of approximately $8 billion. No appropriated funds have been requested or provided since 1974--OPIC has financed its investment projects and operating costs from its income from insurance premiums, repayments, and user charges of OPIC programs. As of September 30, 1981, OPIC had built up its capital and reserves to $725 million. Beginning with fiscal year 1982 and each fiscal year thereafter, OPIC will be required to make payments to the Treasury from its net income until it has returned an amount equal to the $106.25 million originally appropriated to it.

OPIC operates on a self-sustaining basis. Its revenues and net income, most of which are currently derived from interest on investment of fees and other receipts in U.S. Treasury securities, have grown steadily--generally in excess of 10 percent per year. Gross revenues and net income totaled $87 million and $76 million, respectively, in fiscal year 1981.

By law, all obligations arising under investment insurance and guaranties issued by OPIC are backed by the full faith and credit of the U.S. Government. OPIC management estimated that its maximum potential exposure, prior to reinsurance, under investment insurance contracts in force at September 30, 1981, was $3.0 billion. In addition, outstanding commitments for guaranties on this date totaled $317 million. Thus, if claim settlements resulting from these contingent liabilities would exceed OPIC's available resources (about $776 million at September 30, 1981), the Congress would have to appropriate funds to fulfill its pledge.

The heart of OPIC programs traditionally has been and remains providing political risk insurance. However, in recent years, the

Congress has asked OPIC to give increased focus to assisting smaller U.S. firms investing in developing countries. Investment projects involving firms smaller than the "Fortune 1000" for fiscal years 1980 and 1981 remained constant at about 34 percent of all OPIC finance and insurance projects, surpassing a 1978 congressional goal that such projects constitute at least 30 percent of OPIC program activity.

OPIC's direct loan program is restricted to projects sponsored by or significantly involving U.S. small businesses. The Congress originally established a $40-million Direct Investment Fund (DIF) whereby OPIC could make loans on a revolving fund basis to eligible smaller business projects on its own terms and conditions. In 1976, OPIC increased the DIF by $10 million in connection with the transfer of a like amount from its retained earnings to capital which is held by the U.S. Treasury. As of September 30, 1981, $34.7 million of the $50 million loan fund was in outstanding ($25.5 million) or committed ($9.2 million) loans.

The Overseas Private Investment Corporation Amendments Act of 1981 (Public Law 97-65, Oct. 16, 1981) extended the program authority through September 30, 1985, and made certain provisions with respect to how funds were to be applied. Beginning in fiscal year 1982, OPIC is required to increase the DIF loan fund by the amount of principal and interest repayments received during the previous year, and at least 10 percent of net income for the previous year (see ch. 4). Also, OPIC will start to repay the U.S. Treasury the aggregate amount appropriated to it in installments of 25 percent of its net income, after making suitable provisions for transfers to its capital and reserves.

OPIC, located in Washington, D.C., has a full-time administrative staff of 125 and an annual operating budget of $10.8 million, financed out of its earnings. In fiscal year 1981, it spent $7.6 million, or only about 70 percent of budgeted funds. The chief reason for the shortfall was that only $1.5 million was spent in contrast to more than $3.5 million budgeted for contractual services and investment encouragement. Payroll, travel, and printing costs were also well below budgeted amounts.

OPIC is organized as a corporation in order to ensure that its operations are conducted in a business-like manner and that it have suitable flexibility to deal with private sector investors. By law, all corporate power of OPIC is vested in a 15-member Board of Directors which has, in turn, delegated substantial responsibility for OPIC day-to-day operations to OPIC management. Eight of these directors, appointed by the President with the consent of the Senate, are selected from the private sector, and at least two must be experienced in small business, one in organized labor, and one in cooperatives. The remaining seven directors, appointed by the

President, are to be U.S. Government officials, including the Administrator of AID (who is board chairman), the U.S. Trade Representative, a Department of Labor official, and the President of OPIC. The other U.S. Government officials are, by tradition, Under Secretaries or Assistant Secretaries from the Departments of State, Treasury, and Commerce.

The Inspector General of the Agency for International Development is authorized by law to review or investigate all phases of OPIC's operations and activities. The cost of the reviews is borne by OPIC and the Inspector General reports his findings to the Corporation's Board of Directors.

The Government Corporation Control Act requires that OPIC, as a wholly owned Government corporation, be audited by us on a reimbursable basis at least once every 3 years. Our practice, pursuant to OPIC's request, has been to audit the Corporation's financial statements annually.

OBJECTIVES, SCOPE, AND METHODOLOGY

We examined the Corporation's comparative balance sheets as of September 30, 1981 and 1980, and the related statements of income, changes in capital and reserves, and changes in financial position for the years then ended. Our examination was made in accordance with the Comptroller General's standards for financial and compliance audits of governmental organizations, and included such tests of the accounting records, internal accounting controls, compliance with the terms and provisions of laws and regulations, and other audit procedures as we considered necessary under the circumstances. We confirmed OPIC's outstanding insurance contracts by means of a stratified sample and independently verified all its investments in U.S. Treasury securities, outstanding loans and loan guarantees, and cash balances with the U.S. Treasury.

In addition, we reviewed the adequacy of OPIC's insurance and guaranty reserves and costs associated with the DIF. Our review was to determine how they are likely to be affected by the OPIC Amendments Act of 1981. All work was conducted at OPIC offices located in Washington, D.C.

This report presents OPIC's comparative financial statements as of September 30, 1981 and 1980, and our opinion thereon (see apps. I and III), and discusses aspects of OPIC's financial reporting and administrative policies observed during our audit which we feel deserve increased management attention. OPIC officials reviewed a draft of the report, and their views and our analysis of them have been incorporated in this report where appropriate.

CHAPTER 2

INSURANCE AND GUARANTY RESERVES

ADEQUATE TO COVER CLAIMS

Section 237(c) of the Foreign Assistance Act of 1961, as amended, provides that the full faith and credit of the United States is pledged for the full payment and performance of obligations incurred by OPIC under its insurance and guaranty contracts. OPIC is required to maintain separate insurance and guaranty reserves to discharge respective liabilities incurred under these contracts. If claim settlements exceed available reserves, then the Corporation would be required to either borrow funds from the U.S. Treasury or request supplemental funds from the Congress to pay the claims.

Funds available to meet claims arising from OPIC insurance and guaranty investments amounted to $775.8 million at September 30, 1981, before additional funds would have to be requested from the Congress. These resources consisted of the following:

	(millions)
Insurance reserve	$531.0
Guaranty reserve	133.4
Treasury borrowing authority	100.0
Unallocated retained earnings	11.4
Total	$775.8

On the basis of recent and historical claims experience, we believe this amount is reasonable in relation to what OPIC management estimates is approximately $3.3 billion in outstanding insurance and guaranty contracts and commitments, as discussed further below.

INSURANCE RESERVE

OPIC's insurance reserve at September 30, 1981, totaled $530,954,045. Of this amount, $120 million was provided by congressional appropriations ($65.5 million to OPIC and $54.5 million from the assumed AID investment insurance program). The balance was transferred from the Corporation's retained earnings, including $80 million in fiscal year 1981. Charges against the reserve may be made from obligations which derive from guaranties issued in settlement of insurance claims, pending claims, and future claims that might arise from existing investment insurance contracts. These three categories of obligations and their possible effect on the reserve are discussed in some detail in note 5 of the accompanying financial statements (see app. III). OPIC estimates that its maximum potential exposure is $3.0 billion on outstanding insurance contracts.

Insurance claim payments net of recoveries in the decade of OPIC's operations have not been unduly significant. Cumulative payments on $166.1 million in claims resolved by cash settlements through September 30, 1981, amounted to $73.4 million (the main difference being accounted for by one claim being reduced by $89.2 million through arbitration). Of the $73.4 million paid out, $47.4 million has been recovered in principal and interest to date with potential additional recoveries estimated at $20 million. Recoveries due from private reinsurers further reduce OPIC's ultimate liability on these cash settlements by possibly several million dollars. Insurance claims settled or backed by OPIC guaranties have resulted in additional cash payments of $126.6 million against which recoveries of $100.6 million, including interest of $33.8 million, have been made.

Finally, there were current indications that actual and potential charges against the insurance reserve were moderating. Losses on claim settlements involving political risk insurance declined from $2.4 million in fiscal year 1980 to $1.8 million in fiscal year 1981. Net assets acquired in insurance claim settlements, consisting mainly of notes related to Chilean expropriation claims payments, declined during the fiscal year by $9.1 million--from $46.5 million at the end of 1980 to $37.4 million at the close of 1981.

GUARANTY RESERVE

OPIC's guaranty reserve at September 30, 1981, totaled $133,390,969. The Foreign Assistance Act of 1961, as amended, requires OPIC to have a reserve related and equal to at least 25 percent of outstanding or committed guaranties. Outstanding commitments at September 30, 1981, totaled $317.3 million. Twenty-five percent of this amount, or $79.3 million, thus constitutes the required reserve. As can be seen, the reserve at September 30, 1981, surpasses the required amount by more than $54 million or by a ratio of about 1.7:1.0.

In addition, actual and anticipated charges against the guaranty reserve are relatively insignificant. Net losses on claim settlements written off against the reserve for fiscal years 1980 and 1981 totaled less than $100,000. Net assets acquired in guaranty claim settlements rose by $2.0 million in fiscal year 1981 to $14.5 million, and estimated uncollectible accounts remained stable at $6.5 million.

OTHER RESOURCES

The insurance and guaranty reserves may be replenished or increased by transfers from retained earnings or by new congressional appropriations. During fiscal year 1981, $80 million was transferred to the insurance reserve and $10 million was transferred to the guaranty reserve from retained earnings. At September 30, 1981, unallocated retained earnings available for transfer to the insurance and guaranty reserves amounted to $11,425,823.

In addition, OPIC is authorized to borrow up to $100 million from the U.S. Treasury to discharge its insurance and guaranty liabilities. OPIC has not used this borrowing authority, which was granted by the OPIC Amendments Act of 1974, nor has it requested or received any appropriated funds to augment its reserves since 1974.

CONCLUSION

Funds in OPIC's insurance and guaranty reserves at September 30, 1981, appeared to be sufficient to discharge obligations arising under its investment insurance contracts and guaranties. The insurance reserve of $531 million easily covered contingent liabilities and, on the basis of historical claims experience, represented a reasonable safeguard against the estimated $3.0 billion maximum potential exposure. The guaranty reserve of $133 million exceeded by $54 million the 25 percent minimum reserve required by law on outstanding commitments and easily covered current anticipated uncollectible accounts. Moreover, we believe OPIC's total available resources of about $776 million at year-end was sufficient to preclude a need for OPIC to seek supplemental funds from the Congress for the foreseeable future. Finally, based on the present magnitude and earning power of its insurance and guaranty reserves and operations, the Corporation should have no difficulty in starting to repay the U.S. Treasury the aggregate amount appropriated to it in fiscal year 1982, as required by the OPIC Amendments Act of 1981.

CHAPTER 3

EFFECTS OF FINANCIAL POLICIES NOT FULLY DISCLOSED

Taken as a whole, we consider that the accompanying financial statements do fairly present OPIC's overall financial position and the results of its operations for the year ended at September 30, 1981. OPIC observes conservative accounting policies and summarizes those significant to its operations in notes 1 and 3 to the statements (see app. III). However, it does not disclose the effects of some of these policies. The effects relate to (1) nonrecognition of delinquent interest revenue, (2) noncapitalization of rescheduled interest, (3) nondisclosure of delinquent finance projects, and (4) only partial disclosure of DIF realized gains and losses.

We believe that disclosure of these effects by OPIC in its financial statements and notes thereto would enhance their usefulness to the Congress, other executive agencies, and the public. Accounting principles and standards prescribed by the Comptroller General for guidance of Federal agencies state that receivables due under contractual or other arrangements shall be accounted for as assets until they are collected, converted into other resources, or determined to be uncollectible; and that such receivables shall be clearly and fully disclosed in agency financial reports. Also, this prescribed guidance also states that where it is important to determine the financial results of a specific program activity, the agency accounting and financial reporting system shall clearly identify all significant costs incurred in carrying out the program. In our opinion, it is of such importance to measure and report specifically identifiable DIF gains and losses. Further, these standards of disclosure are consistent with generally accepted accounting principles.

NONRECOGNITION OF DELINQUENT INTEREST REVENUE

As a matter of conservative accounting policy, OPIC does not recognize delinquent interest on investments as revenue until it is received. It accrues such interest income until it is 90 days past due, then places the related investment on nonaccrual status, reverses previously accrued interest, and recognizes the income only when cash is received. Although OPIC for years has observed this policy, which is widely accepted in the banking industry, OPIC did not disclose that it was following such a reporting procedure until this year (see note 1, app. III). OPIC did so at our request. While we prefer that OPIC also disclose this policy's effect, it did not agree to do so for the reason stated on pages 10 and 11. However, we did not consider the omission of sufficient materiality to adversely affect our opinion on the current year financial statements.

As of September 30, 1981, cumulative delinquent interest due OPIC on DIF loans and claims related assets but not reflected on its financial statements amounted to approximately $4.8 million, as shown below.

Schedule of Unreported Interest Revenue from Nonaccruing Assets

DIF loans	Amount (000 omitted)
Direct investment interest	
Fiscal year 1981	$ 436
Fiscal year 1980	295
Prior years	423
Capitalized interest and fees	304
	$1,458
Assets acquired in claims settlements	
Direct investment interest	
Fiscal year 1981	$ 816
Fiscal year 1980	770
Prior years	1,140
Capitalized interest and fees	641
	$3,367
Total	$4,825

The accounting procedure followed by OPIC had the effect of reducing, from $6.9 million to $2.1 million, the amount of accrued interest receivable generated from these assets and shown by OPIC on its September 30, 1981, balance sheet. Also significant was the fact that unrecognized delinquent interest revenue in fiscal year 1981 amounted to $1.25 million, or approximately one-fourth of the total $4.75 million interest due on these assets during the period. Appropriate adjustment should be made for doubtful collections.

NONCAPITALIZATION OF RESCHEDULED INTEREST

OPIC's policy of not accruing interest on its delinquent investments extends to interest that has been capitalized, resulting in the base of assets held for investment being understated. This policy was also first disclosed in the current year financial statements (see note 1, app. III), but the effect was not given. We think that capitalized interest, unless determined to be uncollectible, should be disclosed on the balance sheet. As presented in the above schedule, unreported capitalized interest and fees at September 30, 1981 totaled $945,000, of which $877,000 applied to two ailing investment projects supported by a combination of OPIC loans and guaranties. If OPIC followed the procedure of disclosing interest earnings on its delinquent investments, this amount would more appropriately have been shown as an increase in outstanding loans. Interest due OPIC is computed on capitalized amounts, the same as for revenue on other nonearning assets, and income is recognized only as cash is received.

NONDISCLOSURE OF DELINQUENT FINANCE PROJECTS

As of September 30, 1981, OPIC had 10 investment projects on its books that were in a delinquent, or nonaccruing asset category, but their delinquent status was not identified in the financial statements. They had an outstanding balance, net of capitalized interest, of $15.7 million. Of this amount, $5.7 million was for DIF loans (21 percent of the value of DIF loans outstanding) and $10.0 million was for claims related assets obtained as a result of payments made by OPIC pursuant to its guaranty provisions. According to agency records, most of the delinquent projects are in various stages of financial distress. Thus, it appears likely that the amount of interest earnings attributable to nonaccruing assets will continue to mount in future years. OPIC's allowance reserve for uncollectible claims related assets is linked to specific accounts, whereas the allowance reserve for loans is an overall estimation. We found that the total loss allowances for DIF loans ($5.1 million) and assets acquired in claims settlements related assets ($6.5 million) appeared to be reasonable in relation to anticipated future principal write-offs.

DIF GAINS AND LOSSES ONLY PARTIALLY DISCLOSED

The Foreign Assistance Act of 1961, as amended, requires that the DIF, established as a revolving fund, shall be charged with realized losses and credited with realized gains. In its financial statements, OPIC reports the status of commitments it has made against the $50 million DIF loan authority available at September 30, 1981, but does not show the Fund's operating revenues and costs. Uncommitted funds were reduced by net losses reflecting actual and estimated write-offs of loan principal. However, no adjustment was made for other operating gains and losses such as interest revenue and the costs of administering and collecting the loans. Thus, from the information presented, it was not possible to tell whether --or to what extent--the DIF was being operated at a loss.

Administrative costs allocable to the DIF generally could not be identified because OPIC does not maintain its accounts by program cost category. Even costs that were clearly identified as loan program expenses were not charged to the DIF. They include legal costs paid to private law firms in connection with the attempted recovery or settlement of loans. While we did not determine the aggregate amount of such legal costs, we believe they may be substantial.

For example, we determined that $85,000 has been paid to a South American law firm in attempts to recover a $450,000 loan disbursed in 1975. No payment has yet been received, but OPIC has successfully appealed a lower court ruling which denied recovery. In another instance, $54,000 was paid to an Asian firm in connection with a restructuring of the borrower's debt though the prospect for ultimate and full repayment of over $7.5 million in loans and guaranties was doubtful. Finally, OPIC has started or is contemplating legal action in a number of other cases which could substantially add to these costs.

CONCLUSIONS

We believe that full disclosure of the amount of interest contractually due or capitalized, and identification of projects which have been placed on nonaccrual status, would enhance a reader's understanding of the accompanying financial statements and notes thereto. However, adequate provision should be made for delinquent interest determined to be uncollectible so as not to overstate receivables and revenues. The reader would thus be made aware of the extent to which investments comprising OPIC's finance portfolio are not current in repayment. We are also concerned that not all DIF gains and losses are being identified, precluding a determination of the operating results of the Fund.

Accordingly, we believe that OPIC should disclose in future years' financial statements the value of assets that it has placed in the nonaccruing category and amounts of principal and interest that are delinquent. Also, we think that OPIC should separately account for and disclose all gains and losses related to DIF lending activity so that the cost of operating the revolving fund can be determined.

RECOMMENDATIONS

We recommend that the President of OPIC require that future years' financial statements:

1 --Disclose the outstanding balance of delinquent, nonearning assets held for investment and the related amounts of principal and interest that are due from them.

2 --Show all net gains or losses realized from DIF lending activity.

AGENCY COMMENTS AND OUR ANALYSIS

OPIC disagrees with the recommended financial statement disclosures. It believes generally accepted accounting principles would not require delinquent interest revenue to be shown and cites a limited review of financial statements of publicly traded companies to back its position. Furthermore, OPIC stated that it does not want to highlight in a widely publicized document that specific or lumped interest payments due to OPIC are not current. It considers that disclosure of such information could encourage other OPIC borrowers to be less strict in timely repayment of their obligations.

Also, OPIC believes it is consistent with its policy on nonrecognition of delinquent interest and more prudent not to disclose delinquent interest that has been capitalized since it views rescheduled interest to be fundamentally the same as delinquent interest. In the same vein, OPIC believes that disclosure of delinquent finance projects would not be beneficial because it might induce other borrowers or potential borrowers to try to reschedule their payments as well, especially in hard economic times.

In OPIC's view, to charge other administrative costs against the DIF would result in an unwarranted reduction of funds available for development lending and a corresponding increase in funds available for higher yielding investment earnings. With regard to outside legal costs, OPIC states that it has charged all such costs from program inception to administrative expense because it considers that the DIF, consisting primarily of appropriated funds, was earmarked by the Congress for specific use in making developmental project loans.

OPIC does not object to making the foregoing disclosures to appropriate parties, such as its oversight committees in the Congress, but believes the financial statements which are widely read by investors are not the proper place to make them known.

As stated at the outset, we are not taking issue with the fairness of the financial statements but rather with the lack of full disclosure of significant data regarding program results. Financial presentations should be concise, but also complete. Concerning OPIC's comment that making disclosures of delinquencies could prompt other borrowers to seek similar delays in making payments, we do not contemplate that such disclosures need to be detailed by project or country. We do not believe there is a significant risk of increased delays if the information is presented on an aggregated basis. Moreover, we think the disclosures are necessary for readers of the statements to obtain not only a fair but complete and useful understanding of OPIC's financial reporting.

CHAPTER 4

DEVELOPMENT LOAN PROGRAM INCURS LOSSES

OPIC's status as a profitmaking and self-sustaining organization seems reasonably well assured for years to come. However, the prospect of additional funds being made available for small business lending could have a detrimental effect on future earnings if current indications of loan losses and related guaranty claims on this type of development financing are realized. Our view is based on OPIC's actual and estimated loss experience on outstanding DIF loans and the additional amount of claims payments it has made to private lenders on loan projects that are in default. Recovery of some of these loans and claims payments appears doubtful, as discussed later in this chapter and as reflected by OPIC's allowance reserves.

SELF-SUSTAINABILITY OF MAJOR OPIC PROGRAMS

OPIC profitability is mainly attributable to its investment insurance activities. We could not determine the exact contribution of each major program to overall income because OPIC does not maintain its accounts by such profit center categories. However, in fiscal year 1981 the greatest portion of gross revenues ($87 million) and net income ($76 million) were derived from interest on Treasury securities using funds predominantly supplied by insurance fees and reserves, and were only minimally offset by claims write-offs.

The contribution to profitability made by OPIC's finance programs, consisting of direct lending and guaranties of private sector loans, was less clear. Interest earned on the guaranty reserve was almost certainly more than sufficient to cover this program's costs. Nevertheless, claims payments on investment guaranties during fiscal year 1981 ($2.3 million) was up by more than one-third over the previous year and was more than the total guaranty fees collected during the year. Recoveries made on prior claims payments, however, reduced net outlays in 1981 to $0.7 million.

In contrast to these profitmaking programs, OPIC's direct loan program operates on a loss basis. As of September 30, 1981, OPIC estimated that one-fifth ($5.1 million) of its outstanding loans ($25.5 million) were uncollectible. Interest income on loans amounted to $2.5 million during the year, resulting in an approximate yield of 10 percent, well below the current earning rate on Treasury securities. Additional loan interest due of $436,000 was not recognized as revenue in fiscal year 1981 because it was delinquent 90 days or more. Since 1971, net write-offs of $2.5 million, including $0.8 million in fiscal year 1981, have been made against the $50 million loan fund. Finally, loan program administrative costs are costly. In addition to standard operating overhead, OPIC spent over $1 million in fiscal year 1981 for loan loss reserves and outside legal expenses in direct support of the DIF loan program.

OPIC's overall operations should be and are self-sustaining, but it considers that the Congress has specifically exempted small business programs from the self-sustaining mandate. By law, OPIC is required to limit its lending activity to U.S. small businesses and must give them preferential consideration in its investment insurance, reinsurance, and guaranty programs. Furthermore, the House-Senate Conference Committee on the OPIC Amendments Act of 1978 told OPIC that

> "* * * programs of assistance to small business development can be carried out without regard to the statutory provision that OPIC conduct its operations on a self-sustaining basis * * *."

PROJECT FINANCING

OPIC's principal method of assisting in development financing is to provide loan guaranties for U.S. investors in support of viable private sector projects in low income countries. At September 30, 1981, it had outstanding commitments of $317 million and $131 million currently at risk versus a legislative authorization of $760 million. Effective October 1, 1981, OPIC could issue guaranties only to the extent or in amounts provided for in congressional appropriation acts. The fiscal year 1982 limitation was $100 million. In addition, OPIC was authorized to make loans to smaller businesses from the DIF, consisting of $40 million paid in as appropriated capital of the corporation, and $10 million transferred from retained earnings. As of September 30, 1981, $7.8 million of the available loan funds remained uncommitted.

In order to attract sufficient private capital to put some project financing packages together, OPIC has had to guarantee the U.S private lender's segments in addition to its own loan commitment. This has led to an increase in OPIC risk which went far beyond its original loan investment. For example, a $2 million increase which occurred in OPIC claims related assets during fiscal year 1981 was the result of guaranty payments made or committed on a Caribbean project currently in default on its payments. For this and an Asian project, OPIC had established a $6.5 million allowance reserve for doubtful recovery of its guaranty claims payments. To illustrate how loans made to these projects have resulted in additional claims against OPIC and the substantial risks that it encounters in conducting business in less developed countries, we have summarized below OPIC's exposure resulting from the two finance projects.

Caribbean project

Recovery appears uncertain of $4.75 million in principal and approximately $900,000 in interest and fees already paid out or committed to by OPIC for a Caribbean project. Pursuant to a May 1976 financing agreement, OPIC disbursed $1 million in DIF loan proceeds and guaranteed the repayment of a $4 million loan made by a private U.S. lender. After paying one installment of $250,000 due the private lender in December 1977, the borrower defaulted on all subsequent repayment obligations. The U.S. lender did not agree to a debt rescheduling, but instead looked to OPIC for relief under the guaranty provisions. OPIC pays the U.S. lender the principal and interest as they have fallen due following borrower default.

Under a debt restructuring in October 1980, OPIC agreed to assume responsibility for repayment of the then-remaining unpaid installments of principal and interest owed by the Caribbean borrower to the U.S. lender, in return for the borrower signing a $5.5 million promissory note to OPIC. The note consolidated the $4.75 million in principal loan and guaranty repayments due OPIC, with the accumulated interest and fees on the guaranteed loans paid the U.S. lender by OPIC through January 1980. Subsequent interest paid to the U.S. lender was charged off as a loss on claim settlements. OPIC had made principal payments of $500,000 and incurred related interest expenses of $177,000 under the debt-restructuring agreement as of September 30, 1981. A liability remained for principal repayments of $2 million, plus interest expense (at 7-7/8% of approximately $315,000). OPIC had not recorded the $2 million claim liability and corresponding claim-related asset in the pre-closing trial balance at September 30, 1981, but OPIC officials recorded them after we pointed out the omission and they were included on the accompanying fiscal year 1981 financial statements.

The Caribbean project remains in operation under new management. It is currently scheduled to repay its obligations to OPIC in full by April 30, 1990. Its ability to do so appears doubtful although OPIC is receiving interest payments under the latest restructuring agreement. OPIC's investment is secured by mortgages on the borrower's land, buildings, and equipment. OPIC's obligations to the U.S. lender mature on June 30, 1984.

Asian project

Recovery prospects also appear dim on DIF loans of $1.35 million and guaranty claims payments of $5.6 million made by OPIC since 1973 in support of a textile project in South Asia. The project, also sponsored by the International Finance Corporation (IFC), has never operated successfully and is facing possible liquidation.

INCREASED DIF LENDING AUTHORITY

A provision in the OPIC Amendments Act of 1981 mandates the transfer of OPIC resources to the DIF and the use of such funds for eligible small business investment projects in fiscal year 1982 and subsequent years. The Act states in part, that the Corporation shall transfer to the DIF, a revolving fund, in fiscal year 1982 and in each fiscal year thereafter:

> "(1) at least 10 per centum of the net income of the Corporation for the preceding fiscal year, and
>
> (2) all amounts received by the Corporation during the preceding fiscal year as repayment of principal and interest on loans * * *." (Underscoring supplied.)

The Act added the proviso that "loans from the Direct Investment Fund are authorized for any fiscal year only to the extent or in such amounts as provided in advance in appropriation Acts." However, the Act did not state the source of the funds. In lieu thereof, the House report (No. 97-195, July 23, 1981), which addressed the proposed legislation, provides in part, "* * * Any increase in the DIF will not be accompanied by an increase in OPIC's capital account or by any allocation of retained earnings." Other legislative history indicates an intent to increase the amount of OPIC resources available for direct loans.

The OPIC Amendments Act of 1981 overrode the Office of Management and Budget recommendation that would have cut off DIF loan authority in fiscal year 1982. The legislation shows that the Congress clearly intended to continue the DIF loan program. According to OPIC, application of the statutory formula provided in the Act will hereafter establish, without any physical transfer of funds from retained earnings, the outer limits of DIF loan authority which is subject to approval limitations through the appropriations process. Calculation of what constitutes this outer limit of DIF loan authority would be made by OPIC annually. While OPIC made clear that it would not increase funds available for the DIF through transfers from retained earnings, it did not specify how any increase in the DIF loan authority would be funded.

CONCLUSION

Our concern is twofold. First, we wonder whether the Congress was fully aware of the extent of losses and additional claims and administrative costs being experienced on OPIC loan projects when it acted to extend the DIF authority. While it is unlikely that a modest increase in this comparatively small but high-risk loan program would threaten OPIC's overall self-sustaining status, we do feel that the program should be guided by economic as well as developmental and political considerations and that, to this end, it is important that the Congress be fully informed regarding the cost of OPIC's development financing activities when it acts to appropriate additional loan funds. The additional financial statement disclosures recommended in chapter 3 should aid the Congress in these deliberations.

Second, we are not certain from what source or through which means any increase in the DIF authority is to be funded. If, as the 1981 Act states, OPIC shall "transfer" funds to the DIF in a prescribed manner but the transfer is not to be accompanied by an increase in its capital account or by any allocation of retained earnings, how will the fund transfers be accomplished? Also, under the prescribed formula for increasing the DIF authority, principal repayments would serve not only to restore the revolving fund's uncommitted loan capital but also as a factor to expand its ceiling--thus, having a possible pyramiding effect.

RECOMMENDATION

To preclude a possible misunderstanding of how the Congress intended additional authorized resources to be made available for DIF lending, we recommend that the President of OPIC seek clarification from the Congress regarding how the funds are to be transferred to the DIF.

AGENCY COMMENTS AND OUR ANALYSIS

In commenting on our draft report, OPIC emphasized what it considers to be the expressed congressional desire for OPIC to do more for small businesses and that its small business programs should not be bound by the same profitability standard applying to the overall OPIC program. OPIC further stated that the Congress was aware that the small business loan program involves very substantial risks in any less developed country, but felt that the report should note that OPIC considers the basic underlying cause for the problems noted in the illustrated Caribbean project to be the severe economic problems existing in that country.

OPIC also commented on what its views were of the congressional intent and what its proposed actions would be stemming from the 1981 legislative provision making additional amounts available for the DIF. OPIC said there is no evidence that the Congress felt its action would lead to OPIC making a major increase in loans or that this would adversely affect its earnings; it thus considers our concerns unjustified.

We do not imply that OPIC's small business loan program should be profitmaking, but rather we believe that caution should be exercised in committing additional funds and OPIC should properly carry out congressional intent with regard to additional DIF resources being made available.

CHAPTER 5

TIGHTER CONTROLS ON ADMINISTRATIVE EXPENDITURES NEEDED

While we are satisfied that the accompanying financial statements were not materially affected by any weakness in OPIC's system of internal accounting controls or its compliance with applicable laws and regulations, we did observe a need for operating policies and procedures to be better defined. Among other things, this would aid in determinations that OPIC expenditures are in accord with congressional limitations and Federal guidelines. We found, for example, that because we could not clearly distinguish whether some $16,000 expended by OPIC for food and beverages were in connection with business promotion or entertainment, we could not determine whether OPIC spent more for representation in fiscal year 1981 than what the Congress intended when it set a $10,000 limitation. Also, OPIC spent over $230,000 on cash incentive awards for sustained superior employee performance in 1980 and 1981. The awards, in relation to payroll costs and exclusive of other bonus programs, were significantly higher than those recommended by the Office of Personnel Management and were six times the average of those made by other Federal agencies. Moreover, OPIC paid nearly double the original fixed contract price for consulting services to create a performance management system. The cost increase resulted from three contract extensions without a documented revision to the work scope.

OPERATING POLICIES NOT CLEARLY DEFINED

Formal operating policies and procedures for key Corporation financial activities either did not exist or were not current at the time of our review. For example, we found that despite previously reporting our concerns on these issues to OPIC, (1) the accounting manual had not been updated to show changes occurring since 1976, (2) written procedures for cash and property management were generally incomplete, and (3) control records in some instances were not fully supported or explained in subsidiary ledgers. However, we determined that OPIC asset valuations were fairly stated and operating results were not significantly affected by these weaknesses in internal accounting controls.

The Washington Regional Inspector General for Audit, Agency for International Development, terminated a survey of OPIC operating expenses in June 1981 because it concluded that there was nothing to use as a guide in determining expenditure reasonableness, other than prudent business management. Previous to this survey, the Inspector General had not conducted a review at OPIC since at least 1976.

We noted some progress. OPIC issued a procurement guide in May 1981 and at year-end neared completion of its first property inventory in 2 years. Also, OPIC was in the process of converting its predominantly manual accounting and financial operations to an automated system as part of a planned comprehensive management information system. The accounting subsystem was still in the developmental stage as fiscal year 1981 ended, but we learned it was designed to be in compliance with our standards and generally accepted accounting principles. This phase of the project, which was being performed under a Small Business Administration set-aside contract for local minority-owned firms, was completed and fully operational by March 1982.

As a Government-owned corporation operating as a business entity for profit, OPIC exercises greater flexibility over the use of its funds than do Federal entities receiving appropriated funds. It does not necessarily consider itself subject to the various rules and regulations which control most government agencies and departments. In its recently published procurement guide, OPIC states in part that it is its policy:

> "To follow procurement policies and procedures generally established in Government procurement, the Federal Procurement Regulations and the Federal Property Management Regulations <u>except when these procedures are not adapted to the special needs of OPIC</u> in fulfilling its responsibilities under the Foreign Assistance Act or require capabilities not available to OPIC and deviation from the procedures are clearly in the best interest of the Government." (Underscoring supplied.)

We believe that, consistent with exercising such increased flexibility of operation, OPIC needs to maintain tighter management control on administrative expenditures. Although OPIC operating expenses in fiscal year 1981 were far below the budgeted amount overall, as described in chapter 1, improved expenditure criteria is needed to assure compliance with applicable restrictions. We attribute this need in part to a lack of well-defined OPIC operating policies and procedures, as well as a need for more active internal review and agency responsiveness to previously expressed audit concerns.

Specific instances which illustrate our perceived control weaknesses in OPIC administrative spending practices and lead us to this conclusion follow.

BUSINESS MEETING AND ENTERTAINMENT EXPENSES NOT CLEARLY DISTINGUISHABLE

We identified more than $16,000 as having been spent by OPIC during fiscal year 1981, for food and beverages in connection with business meetings and entertainment functions. Of this amount, just under $8,000 was charged against OPIC's representation allowance account. This allowance account was subject to a congressional limitation of $10,000 for entertainment. The balance of expenditures were treated by OPIC as business promotion expenses and were spread among six other accounts, with by far the highest concentration being in the "Other Contractual Services" account.

We found that some charges made to these accounts were not clearly distinguishable from entertainment, though OPIC had made a legal determination which set the two types of expenditures apart as to their nature or purpose. The Corporation distinguishes meals and refreshments incurred in the course of specific business activity as not being subject to the congressional ceiling, but rather considers it as business promotion and permits such business meeting expenses to be charged in an unlimited amount to general administrative accounts. However, the nature of certain activities and accompanying lack of narrative explaining how OPIC drew this distinction in accounting for some of these expenses made it difficult for us to determine whether or not the congressional limitation was exceeded.

According to OPIC policy guidelines concerning business meeting expenses (such as meals), the expenses must be business-related and approved in advance by a department head. The expenses of only one OPIC employee may be allowed for each visitor in attendance. Business meeting expenses are to be charged against the Other Contractual Services account, which the accounting manual defines as " * * * used to record costs incurred for services received under formal contract not otherwise specifically identified." Expenses which further OPIC's purpose but which are not connected with business meetings are considered entertainment expenses and are to be charged against the congressional limitation.

The food and beverage expenses that we identified as having been charged to the various accounts are shown in the schedule below:

Schedule of Food and Beverage Expenses
By Account, Fiscal Year 1981

Description	Representation	Other Contractual Services	Various administrative accounts
Receptions	$6,542	$2,185	$ 166
Business lunches	396	2,931	210
Board of directors meetings	215	975	274
Staff working lunches	-	134	753
Seminars and conferences	-	65	50
Ceremonies and observances	780	968	-
	$7,933	$7,258	$1,453

Certain of the charges in the schedule above did not have sufficient narrative explaining their purpose or whether they were business-related to permit us to verify whether or not the $10,000 ceiling on entertainment was exceeded. Moreover, we did not perform an exhaustive search which would assure that we identified all food and beverage expenses that may have been charged in connection with business meetings. OPIC acknowledged our concern and agreed to establish and maintain more formal and detailed policies and procedures regarding food and beverage charges. (See p. 25.)

OPIC's enabling legislation confers great discretion on the Corporation over how it may make expenditures, including specific authority to use its revenues for investment promotion expenses. However, one restriction that does apply is the ceiling on entertainment allowances contained in each foreign assistance appropriations act since 1971, the first year that funds were appropriated to OPIC. This restriction amounted to $10,000 in fiscal year 1981, and was lowered to $8,000 for fiscal year 1982.

The legislative history of the appropriation acts is virtually silent regarding the intended meaning of "entertainment allowances." The only reference we found to the provision was a brief exchange during a 1970 hearing on OPIC's first appropriation. At this hearing, the OPIC representative characterized the expenses to be covered from the entertainment allowance generally as those incurred for official functions involving the private business community.

The Congress may have intended OPIC to operate with the same flexibility as the private businesses it insures. However, there is no express support in the entertainment allowance provision for the distinction OPIC draws between meals and refreshments that constitute ordinary and necessary business promotion expenses chargeable to general administrative funds and those that constitute entertainment expenses payable from the limited annual entertainment allowance. Because there is some question as to what costs are intended by the legislation to be charged to "entertainment allowances" and how much discretion the Corporation has in accounting for such costs, OPIC's interpretation may not be consistent with what the Congress intended in imposing the ceiling.

RECOMMENDATION

To enable a determination on whether OPIC is adhering to the congressional spending limitation on entertainment, we recommend that the President of OPIC obtain clarification from the Congress regarding what costs constitute entertainment versus business meeting expense and thus is chargeable to the limited annual entertainment allowance.

CASH INCENTIVE AWARDS HIGH

In the past 2 years, OPIC has spent over $230,000 for cash incentive awards to its employees for sustained superior performance. The amount spent by OPIC, in relation to its payroll costs, was significantly higher than that suggested by the Office of Personnel Management (OPM) and that spent by other Federal agencies on the average. Further, not all awards were based on current written performance appraisals nor were they adequately publicized. We believe that this is necessary to assure program credibility and fairness. OPIC said that the awards recognized employee performance in enabling the Corporation to achieve or exceed its goals. It cited recordbreaking business volume and operating results in 1980 and 1981, despite being involved in a legislative reauthorization and a change in administrations.

Following the passage of the Civil Service Reform Act of 1978, OPM revised its guidelines to Federal agencies in May 1980 to give them greater flexibility to recognize employee achievements through their incentive awards programs. Among the significant changes were:

--Requiring that performance rewards must be linked to performance appraisals as a means of increasing awareness that deserving employees were being recognized.

--Permitting awards to be based on a percentage of base salary, 15 percent being the maximum allowed in any 52-week period on special achievement awards for sustained superior performance. (Formerly, OPM guidance limited awards for sustained superior performance to $350.)

Overall, OPM recommended that agencies allocate about 1 percent of payroll costs for sustained superior performance awards.

OPIC spent $99,000 and $132,550 for sustained superior performance awards for its employees in December 1980 and 1981, respectively, compared to $7,600 in 1979. These cash incentive awards constituted 2.53 percent of payroll costs in 1980 and 3.13 percent in 1981. In addition, in 1981, quality step increases were granted to 14 employees for their outstanding work throughout the year and merit pay of 2.4 percent of base salary was distributed to supervisors based on their performance. OPIC has no employees in the Senior Executive Service.

Cash awards were granted to 47 employees in 1980 and 45 employees in 1981. This represents awards to over one-third of OPIC's approximate permanent full-time staff of 125 both years, with average awards amounting to $2,106 in 1980 and $2,945 in 1981. In

1981, they ranged from a low of $600 to a high of $6,500. Twenty employees were recipients both years, including 9 employees (all with a base salary of over $50,000 annually) who accounted for $79,500, or 34 percent, of the total awards made. Eighty-three awards, or 90 percent, were $1,000 or greater in amount.

These figures are in sharp contrast to amounts spent by other Federal agencies. According to testimony presented in August 1980 before the Subcommittee on Compensation and Employee Benefits, House Committee on Post Office and Civil Service, an OPM official stated that only 7/10 of 1 percent of employees who received performance awards the preceding year (1979) received over $1,000. The average award was $266, exclusive of merit pay and Senior Executive Service bonuses. Although the official said he expected the amount of the average award to rise under OPM's new guidance (it did, to $322 in 1980; the 1981 figure was not yet available), only about 6 to 10 percent of eligible employees were expected to continue to get them. Overall, with respect to cash awards which amounted to only about 1/10 of 1 percent of the entire Federal civilian payroll, the OPM official commented that "* * * I have no illusions that actual expenditures will go to 1 percent [of payroll] in any foreseeable time if at all * * *."

OPIC takes the position that its staff recognition was not excessive when considered in light of the Corporation's accomplishments and was well within OPM's 15 percent of base salary ceiling. It notes that individual cash awards averaged only 7 percent of base salary in 1980 and 8 percent in 1981, about half the maximum permitted. With regard to the suggested overall allocation of 1 percent of payroll, an OPIC official said this was a guideline and not a requirement. He stated that in a small, highly professional organization such as OPIC which had, compared to other agencies

> "* * *no blue collar activity and relatively little lower level white collar activity [there was] a higher probability that a larger percentage of the staff will be better motivated and interested in pushing their performance beyond satisfactory than in most other agencies that are significantly more diverse in their composition. * * *"

Nonetheless, we believe that the number and amount of OPIC cash awards were high in relation to how we view the spirit and intent of the Federal program for performance-based incentive awards.

The cash awards made by OPIC in 1980 were not based on written job performance appraisals, as required by OPM. Rather, they were based on written nominations and oral evaluations presented by supervisors through department heads to a performance review panel chaired by the Executive Vice President and ultimately approved by the President. The awards for department heads were initiated by the Executive Vice President and President and approved by the President. We were told that the reason written appraisals were not prepared in 1980 was that OPIC's entire performance appraisal system had not been completed. Written performance appraisals were prepared for 1981. Still, we question their reliability and objectivity in at least some instances. For example, three sustained superior performance awards totaling $4,800 were granted in 1981 to three new employees, all with a base salary of over $50,000 annually, who had been with OPIC for less than 6 months at the time they received the award. By comparison, for Senior Executive Service appointees to be eligible for bonus awards, an executive's performance must have been sustained over a minimum of 12 months. Also, OPM guidance and the law imply that the executive's performance over several years should be taken into account.

Finally, we consider that the awards were not adequately publicized. Although ceremonies to honor awardees were held in 1980 and 1981 and a memorandum announcing the 1981 awardees was sent to the OPIC staff, the amount of the awards, either individually or collectively, was not stated. In addition, the 1981 announcement excluded any mention of the awards made to the three new employees, previously mentioned, and of two repeat recipients (also with a base salary of over $50,000), who were granted a total of $11,000 in 1981.

An OPIC official acknowledges that these five award recipients were not publicized but says the ommission was inadvertent because the executive special achievement award presentations were made subsequent to the memorandum to the staff announcing employee awards. Moreover, these recipients were presented their awards before their peers including the entire executive staff. This official states, however, that procedures will be implemented to assure that all recipients will be included in future general staff announcements.

While we believe that agencies should publicize individual award amounts and suggested to OPM in January 1981 that it develop and enforce a regulation to this effect, OPM does not require it. OPIC considers that such publicity

> "* * * may invite, even encourage, invidious comparison that could create unnecessary pressure on supervisors to be less objective in making discrete judgments between individual performances thereby seriously undermining the whole purpose of the awards system."

We take the opposite view. Full disclosure of award recipients and amounts can serve as both a preventive and incentive measure to enhance this important program. It tends to avoid (1) outright program abuse, such as what occurred at one agency where top management gave themselves large cash awards and (2) the skepticism of disgruntled employees who think that awards are based on favoritism. Further, full disclosure may increase employee incentive because they will be able to correlate specific performance with a specific monetary reward.

CONTRACT COST INCREASED FOR DEVELOPMENT OF PERFORMANCE MANAGEMENT SYSTEM

OPIC hired an expert consultant in May 1979 to assist top management in establishing and implementing a performance management system which would, among other things, be responsive to OPM's new requirement of linking incentive programs to employees' on-the-job performance. The hiring took place under a fixed price contract at a cost not to exceed $40,000, with completion scheduled for February 15, 1980. The contract was extended three times, to September 30, 1981, and increased in amount to $74,000 without the contract amendments stating that the work scope was being modified. We were told that the contract extensions, which involved 85 additional days of consulting at the billed rate of $400 per day, were necessitated by scheduling delays caused by OPIC through no fault of the contractor. An OPIC official acknowledged that the contract amendments did not reflect that a change in work scope had occurred, but stated that a change did in fact occur and OPIC placed a memorandum documenting the scope of work changes in the contract file.

CONCLUSIONS AND RECOMMENDATIONS

We believe that more needs to be done to improve OPIC's financial management controls. OPIC management should set forth, in writing, what its major operating and financial policies and procedures are so as to provide greater assurance that administrative and program expenditures are made in accordance with its own or other applicable criteria. Also, in the past, OPIC management has placed too much reliance on our financial examinations to disclose weaknesses in financial controls and inefficient or ineffective practices. We believe that periodic comprehensive reviews by the AID Inspector General should be an integral part of improved financial management controls. While OPIC's establishment of an automatic and fully integrated management information system should permit improved monitoring and review of Corporation financial management controls and practices, its value will be limited if it is not accompanied by clearly defined objectives and approaches that can be measured or evaluated in specific terms. For example, in order to properly evidence that the congressional ceiling on entertainment expenditures has not been exceeded, it is important that OPIC clearly define and document in sufficient detail the grounds upon which OPIC treats food and beverage charges as business promotion.

Accordingly, we recommend that the President of OPIC:

--Require operating policies, having significant financial or internal control implications, be in writing, and subject to review by the Board of Directors and independent auditors.

--Request the AID Inspector General to monitor OPIC financial and management policies and controls, and to conduct such reviews or inspections of administrative expenditures as often as he deems necessary, though not less frequently than once every 3 years.

AGENCY COMMENTS AND OUR ANALYSIS

OPIC attributed our observations in this chapter to a lack of documentation and said it provided no evidence to justify the implication that its management was not properly supervising administrative operating expenses. It asserts that senior management is involved in all expenditure matters and that, consequently, there is not the need to produce the same volume of formal policies and procedures as there might be in a larger agency with an extended chain of command.

Nonetheless, it agreed to prepare more formal and detailed policies and procedures for food and beverage charges in order to, among other things, allow us to more effectively carry out our review of these expenditures in future years. It believes congressional clarification of what constitutes entertainment versus business expense in OPIC's case is unnecessary. We disagree. OPIC operates under two legislative requirements--one which gives it great discretion to operate as a business entity and to incur unspecified investment promotion expenses, and another which sets a ceiling on what it may spend for entertainment. Based on previously published Comptroller General decisions, some expenses that OPIC considers business promotion we have traditionally viewed as "entertainment." Hence the need for congressional clarification.

OPIC contends that it has fully complied with both the letter and spirit of the law and regulations in its incentive awards program by implementing policies that have successfully motivated and stimulated improved employee performance. Nevertheless, based on available OPM guidance and other Federal agencies' practices, we think the awards were high and serve to illustrate the need for improved controls on agency expenditures.

Finally, OPIC stated that the OPIC Amendments Act of 1981 removed the internal audit function of the AID Inspector General, thus making the oversight responsibility recommended by the report to be outside the Inspector General's scope of authority. The Act removed the requirement that the AID Inspector General conduct internal audits because of a possible duplication with GAO audits. Under the law, the AID Inspector General retains authority to conduct reviews, investigations and inspections of OPIC finances. We view oversight of administrative controls and expenditures to be an integral part of this authority and has a direct bearing on the scope of our audits.

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D.C. 20548

FEB 17 1982

B-201607

To the Board of Directors
Overseas Private Investment Corporation

We have examined the balance sheets of the Overseas Private Investment Corporation as of September 30, 1981 and 1980, and the related statements of income, changes in capital and reserves, and changes in financial position for the years then ended. Our examinations were made pursuant to the Government Corporation Control Act (31 U.S.C. 841-871) and in accordance with generally accepted government auditing standards, and included such tests of the accounting records, internal accounting controls, compliance with the terms and provisions of laws and regulations, and other audit procedures as we considered necessary under the circumstances.

As explained in note 4 of the accompanying financial statements, Section 235(c) of the Foreign Assistance Act of 1961 (Act), as added by the Foreign Assistance Act of 1969 (22 U.S.C. 2195(c)), established an Insurance and Guaranty Reserve for the respective discharge of liabilities under the Corporation's insurance and guaranty contracts. At September 30, 1981, these reserves totaled $664 million. (See notes 5 and 6.) In addition, section 237(c) of the Act provides that the full faith and credit of the United States is pledged for the full payment and performance of the Corporation's insurance and guaranty liabilities. Thus, if claim settlements exceed available resources, the Congress would have to appropriate funds to fulfill this pledge. The standing authority for such appropriations is contained in section 235(f) of the Act.

In our opinion, the accompanying financial statements present fairly the financial position of the Overseas Private Investment Corporation as of September 30, 1981 and 1980, and the results of its operations, changes in its capital and reserves, and changes in its financial position for the years then ended in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Our study and evaluation of the Corporation's system of internal accounting controls disclosed no material weakness. Also, our tests showed that the Corporation was in compliance with terms and provisions of laws and regulations that could have materially affected its financial statements.

Charles A. Bowsher

Comptroller General
of the United States

OVERSEAS
PRIVATE
INVESTMENT
CORPORATION

1129 20th Street N.W.
Washington D.C. 20527
Telex-OPIC Wsh 89 2310

April 19, 1982

Mr. Frank M. Zappacosta
Senior Group Director
International Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Zappacosta:

The management of the Overseas Private Investment Corporation is responsible for preparation of the accompanying financial statements, including the notes thereto, for the fiscal years ended September 30, 1981 and 1980. The financial statements have been prepared in accordance with generally accepted accounting principles appropriate in the circumstances, based on our best estimates and judgments and giving due consideration to materiality.

The Corporation maintains internal accounting control systems that are designed to provide reasonable assurance that assets are safeguarded from loss or unauthorized use, that transactions are executed in accordance with management's authorization and are properly recorded, and that accounting records are adequate for preparation of financial statements and other financial information.

Management believes that the Corporation's internal accounting controls provide an appropriate balance between the cost and expected benefits of specific control measures.

Management further warrants that, to the best of its knowledge and belief, it has complied with the terms of applicable laws and regulations and made appropriate disclosure of contingent liabilities that could have a material adverse effect upon the Corporation's financial position or operations.

The Corporation's Board of Directors is responsible for prescribing, amending and repealing the rules and regulations governing the manner in which the business of the Corporation may be conducted and in which the powers granted it by law may be exercised and enjoyed. Under the general direction of the Board of Directors, management of the Corporation has been delegated power and authority to conduct the business of the Corporation. Management is responsible for assuring

Frank M. Zappacosta

that the financial statements of the Corporation have been prepared in conformity with law.

Sincerely yours,

Dale Duvall

C. Dale Duvall
Treasurer

Balance Sheet
Overseas Private Investment Corporation

At September 30	1981	1980
Assets		
Cash and investments:		
Cash	$ 79,195,307	$ 85,085,221
U.S. Treasury securities at cost plus accrued interest (Note 2)	577,187,221	498,564,605
	656,382,528	583,649,826
Direct Investment Fund loans outstanding less allowance for uncollectable loans of $5,097,288 in 1981 and $4,945,928 in 1980 (Note 3)	20,392,393	18,758,388
Accrued interest and fees	2,081,487	2,242,009
Accounts receivable	18,292,699	9,080,653
Prepaid reinsurance premiums	1,179,110	1,136,447
Furniture and equipment at cost less depreciation of $281,840 in 1981 and $213,996 in 1980	558,075	456,573
Leasehold improvements at cost less amortization of $420,782 in 1981 and $143,040 in 1980	764,512	953,235
Assets acquired in claims settlements	45,363,989	52,359,535
	$745,014,793	$668,636,666
Liabilities, Capital and Reserves		
Liabilities:		
Accounts payable and accrued expenses	$ 1,100,062	$ 1,439,797
Direct liabilities related to claims settlements	3,050,289	2,974,639
Participations in DIF loans	43,686	87,370
Unearned premiums	14,590,822	14,223,295
Fees held pending claims determinations	459,097	344,739
	19,243,956	19,069,840
Contingent liabilities (Notes 5 and 6)		
Capital and reserves:		
Capital held by U.S. Treasury (Note 3)	50,000,000	50,000,000
Insurance reserve (Notes 4 and 5)	530,954,045	452,707,754
Guaranty reserve (Notes 4 and 6)	133,390,969	123,592,606
Retained earnings (Note 7)	11,425,823	23,266,466
	725,770,837	649,566,826
	$745,014,793	$668,636,666

The accompanying notes are an integral part of this statement.

Statement of Income
Overseas Private Investment Corporation

For the year ended September 30	1981	1980
Revenues		
Political risk insurance premiums	$30,104,317	$31,317,787
Less premiums on shared risks	5,069,872	4,837,636
	25,034,445	26,480,151
Investment guaranty fees	2,138,692	1,812,283
Direct investment interest	2,495,976	1,779,543
Other income	109,805	61,690
	29,778,918	30,133,667
Interest	56,997,171	45,999,010
	86,776,089	76,132,677
Expenses		
Salaries and benefits	4,365,600	4,151,027
Loss (Gain) on claim settlements:		
Political risk insurance	1,753,709	2,397,418
Investment guaranties	201,638	(103,498)
Provision for uncollected DIF loans	1,000,000	1,600,000
Contractual services	1,129,824	471,794
Investment encouragement	361,816	258,894
Rent, communications and utilities	819,085	747,099
Travel	325,245	451,892
Printing and supplies	265,532	288,081
Depreciation and amortization	349,630	111,694
	10,572,079	10,374,401
Net income	$76,204,010	$65,758,276

The accompanying notes are an integral part of this statement.

Statement of Changes in Capital and Reserves
Overseas Private Investment Corporation

For the 2 years ended September 30, 1981	Capital	Insurance reserve	Guaranty reserve	Retained earnings	Total
Balance September 30, 1979	$50,000,000	$405,105,172	$113,489,108	$15,214,270	$583,808,550
Net income				65,758,276	65,758,276
Adjustment for (loss) gain on claim settlements		(2,397,418)	103,498	2,293,920	
Transfers from retained earnings		50,000,000	10,000,000	(60,000,000)	
Balance September 30, 1980	$50,000,000	$452,707,754	$123,592,606	$23,266,466	$649,566,826
Net income				76,204,010	76,204,010
Adjustment for (loss) on claim settlements		(1,753,709)	(201,638)	1,955,347	
Transfers from retained earnings		80,000,000	10,000,000	(90,000,000)	
Balance September 30, 1981	$50,000,000	$530,954,045	$133,390,969	$11,425,823	$725,770,837

The accompanying notes are an integral part of this statement.

Statement of Changes in Financial Position
Overseas Private Investment Corporation

For the year ended September 30	1981	1980
Source of Funds		
Net income	$76,204,010	$65,758,276
Depreciation and amortization	349,630	111,694
Provision for uncollectible DIF loans	1,000,000	1,600,000
	77,553,640	67,469,970
Increase (decrease) in:		
Unearned premiums	367,528	937,586
Fees held pending claims determinations	114,358	(52,269)
Direct liabilities related to claims settlements	75,650	(1,732,181)
Decrease (increase) in:		
Accrued interest and fees	160,522	880,517
Assets acquired in claims settlements	6,995,546	9,981,886
	85,267,244	77,485,509
Application of Funds		
Net disbursement on DIF loans	2,634,005	756,129
Acquisition of:		
Furniture and equipment	173,389	340,239
Leasehold improvements	89,020	985,741
Increase(decrease) in:		
Accounts receivable	9,212,046	(545,929)
Prepaid reinsurance premiums	42,663	65,638
Decrease (increase) in:		
Accounts payable and accrued expenses	339,735	(463,850)
Participations in DIF loans	43,684	43,684
	12,534,542	1,181,652
Increase in cash and investments	$72,732,702	$76,303,857

The accompanying notes are an integral part of this statement.

Notes to the Financial Statements

Overseas Private Investment Corporation

Note 1: Summary of Significant Accounting Policies

The significant policies are summarized below:

Revenue recognition: In accordance with generally accepted accounting principles, revenue from political risk insurance is recorded on a pro-rata basis over the contract period; all other revenue is recognized when earned. However, when interest income has become 90 days past due, related investments are placed on nonaccrual status, previously accrued interest, including that which has been capitalized, is reversed and interest income is recognized only when cash is received.

Valuation of assets acquired in claims settlements: Debt of a foreign government acquired in the settlement of a claim is valued at the lower of its present value or the cost of acquisition. All other assets acquired in claims settlements are valued at the lower of management's estimate of the present value of the recovery on the asset or the cost of acquisition. Present value is determined at the time of acquisition using the composite yield for all U.S. Government securities.

Depreciation and amortization: Furniture and equipment are depreciated on a straight-line basis over a 10-year life. Leasehold improvements are amortized over the life of the related lease.

Pending claims: OPIC follows a policy of recording investment insurance contract claims as financial liabilities only upon determination that a liability exists and where the amount of such liability can be reasonably estimated. In the case of most expropriation claims, the expropriatory action must continue for a period of one year before the claim matures. Formal applications for compensation are generally filed only with respect to mature claims and specify the particular events which have occurred and which, in the opinion of the investor, subject OPIC to liability.

Note 2: Investments in U.S. Treasury Securities

In conformance with Section 239(d) of the Foreign Assistance Act of 1961, as amended (FAA), investments in U.S. Treasury securities are limited to funds derived from fees and other revenues. The funds available for investment were $560,957,642 and $491,738,097 at September 30, 1981 and 1980, respectively. Of these funds $560,394,703 and $491,596,301, respectively, represent the original cost of investments included in the Balance Sheet.

Note 3: Direct Investment Fund

The FAA authorized the establishment of a Direct Investment Fund (DIF), that consisted of the $40,000,000 paid in as capital of the corporation, to make loans on terms and conditions established by OPIC. The DIF is charged with realized losses and credited with realized gains and such additional sums as determined by the Board of Directors. During 1976 OPIC increased the DIF by $10,000,000 in connection with the transfer of $10,000,000 from retained earnings to capital held by the U.S. Treasury. For each fiscal year beginning in 1982, OPIC is required to increase the DIF by, and make loans in the amount of, principal and interest repayments received during the previous year and at least ten percent of net income for the previous year. Such funds shall be used to make loans to eligible projects to the extent or in the amounts provided in Congressional appropriations.

The status of the DIF was as follows, in millions:

	September 30	
	1981	1980
Appropriated DIF capital	$40.0	$40.0
Transfer from earnings	10.0	10.0
Net losses including $5.1 allowance for uncollectable loans for 1981; $4.9 for 1980	(7.5)	(6.5)
Uncommitted funds	(7.8)	(14.5)
Outstanding commitments	34.7	29.0
Undisbursed portion	(9.2)	(5.4)
Net loans outstanding	$25.5	$23.6

Proceeds received from the sale of participations were credited to the DIF for further lending in accordance with Sections 231(c), 235(b) and 239(d) of the FAA. The figures above are net of such participations, which amounted to $43,686 and $87,370 at September 30, 1981 and 1980, respectively. Pursuant to provisions of Sections 239(d) and 234(b) of the FAA, OPIC has guaranteed full payment of the participated portion of DIF loans. This liability for outstanding participations is included in the amount of investment guaranties outstanding (Note 6).

Note 4: Statutory Reserves and Full Faith and Credit

Section 235(c) of the FAA established a fund with separate accounts known as the Insurance Reserve and the Guaranty Reserve for the respective discharge of liabilities under investment insurance and under guaranties issued under Section 234(b) of the FAA and similar predecessor guaranty authority.

Both Reserves may be replenished or increased by transfers from retained earnings or by new Congressional appropriations. Retained earnings at September 30, 1981, available for transfer to the Insurance or Guaranty Reserves, were $11,425,823.

Should funds at any time not be sufficient to discharge obligations arising under investment insurance or guaranties, as the case may be, Congress would have to appropriate funds to fulfill the pledge of full faith and credit to which such obligations are entitled. Standing authority for such appropriations is contained in Section 235(f) of the FAA.

All investment insurance issued by OPIC, all guaranties issued by OPIC in connection with the settlement of claims under investment insurance and all guaranties referred to in the first paragraph above constitute obligations of the United States of America. The full faith and credit of the United States of America is pledged for the full payment and performance of such obligations.

Note 5: Insurance Reserve

The Insurance Reserve at September 30, 1981 totaled $530,954,045. Charges against the Insurance Reserve could arise from contingent obligations under (A) guaranties issued in settlement of claims arising under investment insurance contracts, (B) pending claims under investment insurance contracts, and (C) outstanding investment insurance contracts. These three categories of contingent obligations are discussed in more detail in the balance of this Note.

(A) Claims Settlement Guaranties

Pursuant to Sections 237(i) and 239(d) of the FAA, OPIC has in some instances settled claims arising under investment insurance contracts by issuing payment guaranties of host government obligations. These claims settlement guaranties represent contingent obligations backed by the Insurance Reserve.

The contingent liability at September 30, 1981 under these guaranties, including liability as to interest, was $100,295,000. If the principal obligors default in full, and if OPIC does not exercise certain prepayment rights, OPIC would be liable during the following fiscal years for the following amounts, in thousands:

Fiscal year	Contingent liability
1982	$ 34,320
1983	31,905
1984	21,419
1985-8	12,651
	$100,295

Of the total contingent liability under claims settlement guaranties, $92,315,000 represents guaranties of obligations either incurred by the Government of Chile in compensation agreements with OPIC insureds or recognized by the Government of Chile in respect of debt previously insured by OPIC.

Also, in connection with the settlement of one claim, OPIC entered into an indemnity agreement with an insured in 1978 which could result in OPIC liability of up to $8 million.

(B) Pending Claims

At September 30, 1981, the total amount of compensation formally requested in connection with investment insurance contract claims for which no determination of liability has yet been made is approximately $17,000,000. There are 5 claims filed under inconvertibility coverage, 9 under expropriation, and 2 under war/revolution/insurrection.

In addition to requiring formal applications for claimed compensation, the contracts require investors to notify OPIC promptly of host government action which the investor has reason to believe is or may become an expropriatory action. Careful investor compliance with this notice provision will sometimes result in their filing notice of events that do not mature into expropriatory actions.

The highly speculative nature of these notices both as to the likelihood that the event referred to will constitute expropriatory action and the amount of compensation, if any, that may become due leads OPIC to follow a consistent policy of not recording liability related to such notices in its financial statements. Any claims that might arise from these situations are, of course, encompassed in management's estimate that maximum potential exposure, prior to reinsurance, under existing investment insurance contracts is $3.0 billion (Note 5C).

(C) Political Risk Investment Insurance

OPIC issues investment insurance under limits fixed by the legislative authorization in the FAA and prior authorities. The utilization of these authorized amounts at September 30, 1981 (excluding obligations under guaranties issued in settlement of claims) was as follows, in millions:

	Total	Uncommitted	Outstanding
Prior authorities	$1,890		$1,890
FAA Section 235	7,500	$3,991	3,509
	$9,390	$3,991	$5,399

Effective October 1, 1981, the FAA provides that OPIC can issue insurance coverage only to the extent or in the amounts provided in Congressional appropriation acts. OPIC, as did its predecessors, insures the same investment against three different risks (inconvertibility of currency; expropriation; and war, revolution or insurrection). Under some contracts issued by predecessors, theoretically an investor could make successive claims under more than one coverage with respect to the same investment, thereby collecting aggregate compensation exceeding any single coverage amount. The outstanding amount reflects this theoretical possibility and in addition includes provision for insurance as to which OPIC is not currently at risk, but is contractually obligated to provide upon the investor's future request to cover increases in retained earnings and accrued interest.

The outstanding amount pursuant to legislative authorizations is of little use in evaluating realistically the maximum exposure at September 30, 1981 to insurance claims, because it includes insurance for which OPIC is not currently at risk and because it is improbable that multiple payments would be made for each investment. Management believes that a more accurate representation of maximum potential exposure to future claims arising from existing investment insurance contracts can be obtained by assuming that only one claim would be brought under each contract and that the coverage under which the claim would be brought would be the coverage with the highest amount of current insurance in force. Based on this assumption, management believes the maximum potential liability of OPIC as to claims at September 30, 1981 is $3.0 billion.

Note 6: Guaranty Reserve

The Guaranty Reserve at September 30, 1981 totaled $133,390,969. Section 235 of the FAA requires OPIC to have, at the time OPIC commits itself to issue any guaranty under Section 234(b) of the FAA, a Guaranty Reserve equal to at least 25 percent of guaranties then issued and outstanding or committed under 234(b) and prior authorities. At September 30, 1981, the Guaranty Reserve exceeded by $54 million the required minimum reserve. (See Note 4 for description of the Guaranty Reserve and full faith and credit status of guaranties.) Guaranties under prior authorities and Section 234(b) of the FAA include guaranties of debt, equity, and participations in DIF loans. Effective October 1, 1981, the FAA provides that guaranties may be issued only to the extent or in the amounts provided in Congressional appropriation acts. The outstanding commitments at September 30, 1981 were as follows, in millions:

	Prior authority	FAA 234(b) and 235	Total
Legislative authorization	$ 9.9	$750.0	$759.9
Uncommitted	-	442.6	442.6
Total outstanding commitments	$ 9.9	$307.4	$317.3
Currently at risk, net of unfunded commitments	$ 9.9	$121.7	$131.6

Note 7: Return of Appropriated Funds

Commencing in fiscal year 1982, Section 240B of the FAA requires OPIC, in each fiscal year, to pay to the United States Treasury an amount equal to 25 percent of its net income after making suitable provisions for transfers to Reserve and Capital until the $106 million aggregate amount appropriated to OPIC has been repaid.

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