



United States Department of State  
and the Broadcasting Board of Governors

*Inspector General*

May 22, 2009

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TO: SCA - Richard Boucher  
Embassy Islamabad - Ambassador Anne W. Patterson  
ECA- C. Miller Crouch, Acting

FROM: OIG – Harold W. Geisel, Acting 

SUBJECT: Memorandum Report on the Limited-Scope Review of Management and Internal Controls over the J. William Fulbright Scholarship Fund in Pakistan  
Report Number MERO-I-09-07

**Background**

The United States Educational Foundation in Pakistan (USEFP) was established in 1950 by the Governments of Pakistan and the United States. USEFP is guided by a binational commission composed of an equal number of Pakistanis and Americans, and its Chairman alternates each year between a Pakistani and an American. USEFP receives support and counsel from the Governments of both Pakistan and the United States, but it is not an agency of either. USEFP supervises a variety of programs to send Pakistani scholars to American universities and to bring American scholars to universities in Pakistan. From 1951 through academic year 2008, USEFP has sent approximately 1,830 Pakistani grantees to the United States under various programs.

In FY 2008, USEFP received approximately \$10.5 million from the Higher Education Commission Pakistan (HEC), \$19.5 million from the U.S. Agency for International Development (USAID), and \$800,000 from the Department of State's Bureau of Educational and Cultural Affairs (ECA). For FY 2009, HEC may not make its annual contribution to USEFP, and USEFP and ECA are in the process of mitigating the impact of the potential \$10 million loss in contribution from HEC. Through yearly memoranda of agreement, USAID has delegated its responsibility for USEFP funding to ECA management.

The USEFP program has grown from eight graduate students in the 2004-2005 school year to 104 in the 2005-2006 school year and 141 in the 2008-2009 school year. Since FY 2005, USEFP has successfully handled the substantial increase in grantee students, ensured diversity of selected students, and made the program accessible to more potential students by establishing satellite offices in Karachi and Lahore. Based on statistics provided by USEFP, of the 104 graduate students in the 2005-2006 school year, 82 received advanced degrees, 20 are still attending universities, and two returned to Pakistan without completing advanced degrees.

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## **Results**

### **Financial Reporting and Accounting**

In its review, OIG found several weaknesses in USEFP's budgeting and financial reporting, as well as in ECA's oversight of USEFP's financial processes. ECA has oversight and monitoring responsibility over funds provided to USEFP. ECA has made numerous inquiries, requested information, and held discussions with USEFP concerning its financial reporting accuracy and timeliness. ECA has identified what it considers USEFP's failure to provide adequate and timely financial reporting.

From October 1, 2004, through September 30, 2008, USEFP has received approximately \$83.5 million in direct payments from the Department of State, USAID, and HEC. The Department also makes payments to the Institute of International Education (a U.S. non-profit organization) on behalf of USEFP. At the time of OIG's fieldwork, the Institute of International Education was unable to provide the cash amounts, as of September 30, 2008, it was holding on behalf of USEFP. As of September 30, 2008, USEFP had approximately \$58.3 million in a non-interest-bearing account in its New York bank. USEFP's unaudited internal financial statement (Balance Sheet) report for the period ending September 30, 2008, accurately reflects the cash balances reported by the bank. Based on OIG's comparison of unaudited financial statements with the bank statements, OIG found no instances of misuse of funds provided to USEFP.

Audited financial statements have not been completed in a timely manner. The last audited financial statement (annual report) covers USEFP's fiscal year ending September 30, 2006. The certified public accounting firm contracted to perform the annual audit reports only starts the next year's audit after the prior year's audit is approved by the USEFP Board. According to the certified public accounting firm, the USEFP Board has been slow to approve the annual report. USEFP also has not routinely provided quarterly unaudited financial statements (Income Statement, Statement of Cash Flow, and Balance Sheet) to ECA. This delay in receiving audited financial reports and the absence of quarterly unaudited financial statements has raised ECA's concerns about the proper use of funds provided to USEFP. USEFP stated it will begin providing quarterly unaudited financial statements to ECA.

USEFP does not have a controller or chief financial officer managing financial operations. Financial operations are currently managed by USEFP's Executive Director. However, proper segregation of duties dictates that recording, maintaining, and reporting of the organization's financial activities should be independent of overall program management.

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USEFP's current accounting system is not capable of maintaining assigned grant accounts by student. Individual student awards, budgets, and expenses are maintained separately on spreadsheets. The capital balances (cash and bank balances) reported to the balance sheet commingle encumbered and unencumbered grant funds. USEFP has no formal written accounting policies and procedures governing its accounting and budgeting practices. The absence of such policies means that USEFP can adjust or change student funding amounts without explanation and does not have sufficient historical records or data for audit and management oversight reviews. This absence of written policies also means USEFP can create budget estimates for students that extend beyond the grant period without formally deciding to extend the grant period and/or amount. As a result, USEFP budgeted amounts for grants are overstated. USEFP is in the process of revising its grant budget estimates.

In OIG's opinion, ECA's oversight of USEFP needs considerable improvement. ECA has not conducted an on-site review of USEFP, nor has ECA scheduled periodic on-site reviews. Further, ECA's FY 2005-2008 memoranda of agreement with USAID require ECA to request State OIG to "perform periodic program and financial audits of the use of funds." OIG notes that ECA's failure to perform or request OIG to perform on-site reviews has contributed to the breakdown in USEFP's system of internal controls.

Grantee Selection Process

USEFP does not have a defined, standardized, or consistent reviewing method to identify the best-qualified applicants seeking advanced university degrees. Applications for advanced university degrees are subject to a three-phase review process before USEFP submits its nominations, through ECA, to the FFSB for final selection. The Executive Director of USEFP conducts the first review of all incoming applications to determine the best-qualified candidates to be "short-listed" for further evaluation by a nomination review panel. Second, one of several nomination review panels interviews and evaluates "short-listed" candidates and recommends its nominations to the USEFP Board. Third, the USEFP Board reviews the panels' recommendations. The Board then makes final nominations to ECA to submit to the FFSB for final approval. The FFSB has sole authority to award grants under the Fulbright Program.

USEFP does not have a defined, standardized, or consistent scoring process to identify the best-qualified applicants. The Executive Director conducts the first review using a scoring sheet and point system. As a result of a change in scoring midway through the screening process, the total available points are not the same for all the scoring sheets. Although the points are supposed to total 100, OIG's review of 72 applications for the 2009 PhD program revealed 12 candidates with scoring sheets totaling 80 maximum points, and three candidates with sheets totaling 78 points. Thus, a candidate with a perfect score, but a maximum total of only 78 points would be at

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a disadvantage compared to a candidate scored on a 100-point scale. Further, points are recorded on scoring sheets for various academic categories, but USEFP has not documented or established a standardized method for assigning points to a particular category. For example, candidates can receive a maximum of 23 points for “Academic History,” a measure of the candidate’s grades weighted for the caliber of the university or universities attended. However, OIG could not verify the basis for assigning points to a candidate for “Academic History.” Without a standardized scoring process, consistent scoring and ultimately fairness to the grant applicants cannot be assured.

### **Conclusion**

In OIG’s opinion, USEFP’s management and internal controls need improvement. These controls should include written management and accounting policies and procedures; an accurate and verifiable integrated accounting system; timely audited and unaudited financial reporting; accurate grant budgetary projections; periodic internal and external operations, management, and financial reviews; and consistent grantee selection practices and procedures. This lack of management and internal controls is caused by the failure of USEFP management to follow FFSB policies and Department guidelines (FFSB Manual for Binational Commissions and Foundations, March 2005), and ECA’s failure to provide adequate oversight and monitoring of USEFP.

### **Management Comments and OIG Response**

Ambassador Patterson of Embassy Islamabad commented on a draft of this report in an attached letter dated April 21, 2009 (Attachment 1). In her letter, the Ambassador noted her appreciation for MERO’s prompt response to her request for a review. The Embassy has already begun to work with USEFP and its Executive Director to address comments made by the MERO team immediately following the review. The USEFP Board has passed an action plan with work scheduled for completion by the end of July 2009. Actions in the plan include contracting with an auditing firm, hiring a controller, developing a new accounting system, and training staff on its use. Further, the Board’s new Treasurer (USAID comptroller) visits USEFP weekly and regularly communicates with staff members. USEFP is providing quarterly unaudited financial statements to ECA. A proposal to place unexpended grant funds in an interest-bearing account has been made to the USEFP Board. USEFP is providing ECA with grant estimates by grantee. The Executive Director of USEFP is ensuring that written policies and procedures for applicant evaluation are followed. Finally, the Embassy has informed ECA of its support for on-site reviews by that bureau, as well as audits by State OIG.

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OIG commends the Embassy on its timely work with USEFP and ECA and encourages continuing cooperation to fully implement report recommendations.

ECA commented on a draft of this report in an attached memorandum (Attachment 2). ECA noted its appreciation for the assistance of OIG, and concurred with OIG's recommendations. ECA stated that it has communicated and reinforced the importance of these issues with USEFP Board members, including Embassy Islamabad representatives on the Board. ECA also suggested minimal administrative changes to OIG's recommendations, which have been incorporated as appropriate.

### **Recommendations**

Recommendation 1: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure the United States Educational Foundation in Pakistan follows the financial and management policies and procedures of the J. William Fulbright Foreign Scholarship Board and the Department of State. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 2: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure the United States Educational Foundation in Pakistan acquires a new accounting system capable of integrating general ledger, financial accounting, grant management, and budgeting, and ensure the United States Educational Foundation in Pakistan trains the accounting staff on the acquired accounting system. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 3: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure the Board Treasurer of the United States Educational Foundation in Pakistan monitors its financial operations by performing periodic reviews and reports the results of the reviews to ECA. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 4: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should provide the United States Educational Foundation in Pakistan with electronic funds transfer information made to the Institute of International Education on its behalf within 10 days of receipt of such payments by the Institute of International Education. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 5: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure the United States Educational Foundation in Pakistan

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provides ECA with quarterly unaudited financial statements (Income Statement, Statement of Cash Flow, Balance Sheet, and Fulbright Program Expenditures against Budget Information) and audited annual financial reports for the preceding fiscal year by April 1 of each year. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 6: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure the management office of the United States Educational Foundation in Pakistan is staffed with a controller to manage accounting, budgetary, and financial reporting processes. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 7: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure the United States Educational Foundation in Pakistan reviews and revises, as appropriate, in collaboration with ECA and cooperating agencies, grant estimates by individual grantee. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 8: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure the United States Educational Foundation in Pakistan places unexpended grant funds in an interest-bearing account. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 9: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should perform scheduled periodic on-site reviews of the operation of the United States Educational Foundation in Pakistan. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 10: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should fund and request State OIG to perform periodic on-site audits of the operations of the United States Educational Foundation in Pakistan, in accordance with U.S. Agency for International Development/Department of State memoranda of agreement; 10 FAM 236.4-2 (implementation of systematic program monitoring plans); and appendices 6, 7, and 8 of the J. William Fulbright Foreign Scholarship Board Manual for Binational Commissions and Foundations. (Action: ECA, in coordination with Embassy Islamabad)

Recommendation 11: The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure the United States Educational Foundation in Pakistan establishes and follows written policies and procedures for evaluating and selecting scholarship applicants, and administering scholarships, as outlined in the policies of the J. William Fulbright Foreign Scholarship Board and the Department of State. (Action: ECA, in coordination with Embassy Islamabad)

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*Embassy of the United States of America*

OFFICE OF THE AMBASSADOR

Islamabad, Pakistan

April 21, 2009

Mr. Nick Arntson  
Assistant Inspector General  
Middle East Region  
Office of the Inspector General  
Department of State  
Washington, D.C. 20520

Dear Mr. Arntson:

Thank you for the opportunity to comment on the draft report of the Office of Inspector General's Middle East Regional Office report on the Management/Internal Controls over the J. William Fulbright Scholarship Fund, Pakistan. We appreciated your office's prompt response to my request for a review, and we have worked closely with the Board of Directors of the United States Educational Foundation in Pakistan (USEFP) and its Executive Director to ensure quick action on the initial comments made by the inspection team. Their comments are addressed in the issues laid out in the draft report.

Immediately following the auditors' visit, we convened a board meeting of the USEFP, including the Executive Director, who had drafted an action plan attending to the verbal recommendations presented by the auditors. This action plan included contracting with an auditing firm and the hiring of a controller to address financial and management policies and procedures and developing a new accounting system and training the staff on its use. The plan was passed by the Board at that meeting. The Board's Finance Committee will make the accounting firm and controller selection on April 22, and this work is scheduled to be completed by the end of July.

The Board's new Treasurer, the USAID Islamabad Comptroller, visits the USEFP weekly, and communicates with staff on a regular basis via telephone and Email clarifying the auditors' verbal recommendations and assisting in all aspects of fiduciary responsibility.

The USEFP is now providing quarterly unaudited financial statements to ECA and continues to work with them to ensure they contain the information requested by them.

Recommendation Eight stated that USEFP should place unexpended grant funds in an interest-bearing account. This was researched and a proposal will be made to the Board on April 23.

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USEFP has revised grant estimates by individual grantee, and has updated that information in the time frame and format discussed by the auditors, and sent them to ECA. In addition, the Executive Director is in the process of ensuring written policies and procedures for all stages of scholarship applicant evaluation as outlined in FFSB and State Department policies are drafted and followed. The Board will discuss the status of this action at its monthly meeting with the Executive Director Thursday, April 23, with a final deadline of the following meeting in May.

Finally, I wish to ensure you that this post will make it clear to ECA that we support the periodic on-site reviews they may wish to perform on the USEFP operations, as well as State OIG periodic on-site audits of same.

Again, I wish to thank you for your office's assistance in this matter, ensuring you of the seriousness with which we take our responsibility in managing this extremely important aspect of our bilateral relationship with the Pakistani people, and our commitment to having a fruitful and cooperative relationship with ECA as we forge ahead with this endeavor.

Sincerely,

A handwritten signature in cursive script that reads "Anne W. Patterson".

Anne W. Patterson

Attachment 2

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**MEMORANDUM**

TO:           OIG – Harold W. Geisel, Acting

FROM:        ECA - Miller C. Crouch, Acting

SUBJECT:    Comments on Draft Recommendations: The Memorandum Report on the Limited-Scope Review of Management/Internal Controls over the J. William Fulbright Scholarship Fund, Pakistan Report Number MERO-I-09-07

ECA appreciates the assistance of the Office of the Inspector General (OIG) in identifying issues regarding financial and management oversight of the Fulbright Program in Pakistan and subsequent recommendations.

While ECA concurs with the OIG's recommendations and recognizes the Bureau's responsibility to see that they are carried out, ultimately the responsibility for success depends on the U.S. Embassy in Islamabad and the U.S. Educational Foundation in Pakistan (USEFP).

ECA has been in communication with USEFP Board members, including the Embassy representatives on the Board, to reinforce the importance of the issues highlighted in the OIG's recommendations. The binational agreement that established USEFP stipulates that the management and direction of the affairs of USEFP is vested in a Board.

ECA concurs with the OIG's recommendations with additional comments on the following recommendations:

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**Recommendation 5:** The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure USEFP provides ECA with quarterly unaudited financial statements (Income Statement, Statement of Cash Flow, and Balance Sheet) and audited annual financial reports for the preceding fiscal year by April 1 of each year. (Action: ECA, in coordination with Embassy Islamabad).

**Response:** ECA would suggest the following additional language (in bold): “...quarterly unaudited financial statements (Income Statement, Statement of Cash Flow, and Balance Sheet **and Fulbright Program Expenditures against Budget Information**) and audited annual financial reports for the preceding fiscal year by April 1 of each year,” in order to provide a complete description of what ECA requests in the quarterly report that ECA requires of all Commissions.

**Recommendation 7:** The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure USEFP reviews and revises, as appropriate, grant estimates by individual grantee. (Action: ECA, in coordination with Embassy Islamabad)

**Response:** ECA would suggest the following additional language (in bold): “...USEFP reviews and revises as appropriate, **in collaboration with ECA and cooperating agencies**, grant estimates by individual grantee”, in order to reflect the critical importance of consultation among all parties in determining grantee costs.

**Recommendation 11:** The Bureau of Educational and Cultural Affairs, in coordination with Embassy Islamabad, should ensure USEFP establishes and follows written policies and procedures for evaluating and selecting scholarship applicants as outlined in FFSB and Department of State policies. (Action: ECA, in coordination with Embassy Islamabad)

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**Response:** ECA would suggest the following additional language (in bold):  
“...follows written policies and procedures for evaluating, selecting, **and administering** scholarship applicants,” in order to reflect the need for written policies and procedures for the grantees’ entire grant period.

In addition, ECA would suggest adding a recommendation for USEFP to provide periodic program evaluations as requested by ECA and other funders of the Fulbright Program in Pakistan. Suggested recommendation language:

**Recommendation 12:** The Bureau of Educational and Cultural Affairs will request that USEFP provide periodic evaluations of program achievements in addition to financial, statistical, and narrative reports as outlined in Department of State policies (Fulbright Manual for Binational Commissions and Foundations).  
(Action: ECA)

Attachment:

Tab A – OIG Memo of 4/16/09

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