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

B-173240

February 26, 1979

[Financial Statements of The Overseas Private Investment Corporation For Fiscal Year 1978]

To the Board of Directors
Overseas Private Investment Corporation

AGC00171

We have examined the balance sheet of the Overseas Private Investment Corporation as of September 30, 1978, and the related statements of income, changes in capital and reserves, and changes in financial position for the year then ended. This examination was made pursuant to the Government Corporation Control Act (31 U.S.C. 841 et seq.) and in accordance with generally accepted auditing standards and included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We previously examined and reported on the Corporation's financial statements for fiscal year 1977.

The Corporation insures U.S. investors against loss of their overseas investments due to expropriation; currency inconvertibility; and war, revolution, or insurrection. Due to the uncertainties related to the Corporation's exposure under these coverages (see note 5 to the financial statements), we are not able to express an opinion on the adequacy of the amounts available for losses the Corporation may suffer because of its insurance and claim settlements.

Section 237(c) of the Foreign Assistance Act of 1961, as amended (22 U.S.C. 2197(c)), provides that the full faith and credit of the United States is pledged for the full payment and performance of obligations incurred by the Overseas Private Investment Corporation under its insurance contracts. Thus, if claim settlements exceed available resources, the Corporation would be required to either borrow funds from the U.S. Treasury or request supplementary funds from the Congress to pay the claims.

In our opinion, except for the adequacy of the amounts available for losses, the accompanying financial statements present fairly the financial position of the Overseas Private Investment Corporation at September 30, 1978, and 1977, 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 consistent basis.

Frederic B. Steele

Comptroller General
of the United States

Letter Report
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Overseas Private Investment Corporation

Statement of Income

For the year ended
September 30

1978 1977

	1978	1977
Revenues		
Political risk insurance premiums	\$31,069,931	\$30,153,633
Less premiums on shared risks	<u>5,195,973</u>	<u>5,727,463</u>
	25,873,958	24,426,170
Investment guaranty fees	2,353,192	2,295,910
Direct investment interest	1,331,872	1,356,603
Other income	<u>306,211</u>	<u>333,368</u>
	<u>29,865,233</u>	<u>28,412,051</u>
Interest	<u>30,589,449</u>	<u>26,421,833</u>
	<u>60,454,682</u>	<u>54,833,884</u>
Expenses		
Salaries and fringes	3,468,561	3,435,741
Provision for doubtful DIF loans	1,600,000	1,600,000
Contractual services	1,789,362	1,171,442
Rent, communications and utilities	451,818	428,943
Travel	256,189	223,574
Printing and supplies	143,699	134,042
Depreciation and amortization	<u>33,062</u>	<u>28,098</u>
	<u>7,742,691</u>	<u>7,021,840</u>
Net income	<u><u>\$52,711,991</u></u>	<u><u>\$47,812,044</u></u>

The accompanying notes are an integral part of this statement.

Balance Sheet

	At September 30	
	1978	1977
Assets		
Cash and investments:		
Cash	\$ 71,498,541	\$ 59,329,922
U.S. Treasury securities at cost plus accrued interest, which approximates market (Note 2)	372,159,782	315,053,410
	443,658,323	374,383,332
Direct Investment Fund loans outstanding less allowance for doubtful loans of \$3,600,000 in 1978 and \$2,000,000 in 1977 (Note 3)	17,920,837	21,126,915
Accrued interest and fees	1,256,284	1,802,613
Accounts receivable	6,078,135	5,738,897
Prepaid reinsurance premiums	1,172,301	787,814
Furniture and fixtures at cost less depreciation of \$157,348 in 1978 and \$137,858 in 1977 and amortized leasehold improvements	155,775	171,693
Assets acquired in claims settlements	5,521,820	6,336,820
	\$475,763,475	\$410,348,084

The accompanying notes are an integral part of this statement.

Balance Sheet

	At September 30	
	1978	1977
Liabilities, capital and reserves		
Liabilities:		
Accounts payable and accrued expenses	\$ 1,011,837	\$ 1,892,052
Direct liabilities related to claims settlements (Notes 5 and 6)	5,521,820	6,336,820
Participations in DIF loans	680,988	1,559,047
Unearned premiums	15,553,119	13,420,085
Fees held pending claims determinations	2,442,739	2,178,542
	<u>25,210,503</u>	<u>25,386,546</u>
Contingent liabilities (Notes 5 and 6)		
Capital and reserves:		
Capital held by U.S. Treasury (Note 3)	50,000,000	50,000.00
Insurance reserve (Notes 4 and 5)	283,005,916	229,947,973
Guaranty reserve (Notes 4 and 6)	99,965,476	100,143,976
Retained earnings	17,581,580	4,869,589
	<u>450,552,972</u>	<u>384,961,538</u>
	<u>\$475,763,475</u>	<u>\$410,348,084</u>

Statement of Changes in Capital and Reserves

For the 2 years ended
September 30, 1978

	<u>Capital</u>	<u>Insurance reserve</u>	<u>Guaranty reserve</u>	<u>Retained earnings</u>
Balance September 30, 1976	\$50,000,000	\$204,949,185	\$82,191,147	\$36,057,545
Net income				47,812,044
Payments on claims settlements		(46,172,625)	(1,047,171)	
Recoveries on prior years' claims settlements		11,171,413		
Transfers from retained earnings		60,000,000	19,000,000	(79,000,000)
Balance September 30, 1977	50,000,000	229,947,973	100,143,976	4,869,589
Net income				52,711,991
Payments on claims settlements		(69,340)	(1,249,305)	
Recoveries on prior years' claims settlements		14,127,283	70,805	
Transfers from retained earnings		39,000,000	1,000,000	(40,000,000)
Balance September 30, 1978	<u>\$50,000,000</u>	<u>\$283,005,916</u>	<u>\$99,965,476</u>	<u>\$17,581,580</u>

The accompanying notes are an integral part of this statement.

Statement of Changes in Financial Position

	For the year ended September 30	
	1978	1977
Source of funds		
Net income	\$52,711,991	\$47,812,044
Depreciation and amortization	33,062	28,098
Provision for doubtful DIF loans	1,600,000	1,600,000
	54,345,053	49,440,142
Decrease in accrued interest and fees	546,329	59,368
Increase in fees held pending claims determinations	264,197	1,942,422
Net reduction (increase) in DIF loans	1,606,078	(521,216)
Increase (decrease) in unearned premiums	2,133,034	(444,950)
Net recoveries (payments) on claims settlements	12,879,443	(36,048,383)
	71,774,134	14,427,383
Application of funds		
Decrease (increase) in:		
Participations in DIF loans	878,059	1,284,309
Accounts payable and accrued expenses	880,215	(49,047)
Increase in:		
Accounts receivable	339,238	760,592
Prepaid reinsurance	384,487	131,792
Additions to furniture and fixtures	17,144	33,295
	2,499,143	2,160,941
Increase in cash and investments	\$69,274,991	\$12,266,442

The accompanying notes are an integral part of this statement.

Notes to the Financial Statements

Note 1: Summary of significant accounting policies

The significant policies are summarized below:

Income recognition: Revenue from political risk insurance is recognized ratably over the contract year. All other revenue is also recognized when earned in accordance with generally accepted accounting principles.

Payments to investors on claims settlements: Payments to investors on claims settlements are charged directly to the applicable Insurance or Guaranty Reserve at the time a payment is made or the payment obligation is irrevocably established. Recoveries made in the course of liquidating assets acquired in the settlement of claims are credited to the Reserve against which the related claims were charged.

Assets and direct liabilities related to claims settlements: As a result of claims settlements, OPIC owns or has an interest in certain assets arising from interests in future payments due under certain promissory notes guaranteed by OPIC under claims settlements and its guaranty authority. OPIC will have to make payments under these guaranties prior to receipt of payment from the obligors. These assets are reflected at the amount of future payments required prior to reimbursement by the obligors. OPIC's payment obligations are reflected in the liability section of the Balance Sheet and their due dates are shown in Notes 5 and 6.

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

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 \$364,043,736 and \$310,068,937 at September 30, 1978 and 1977, respectively. Of these funds \$364,043,185 and \$309,590,750, 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 initially of the \$40,000,000 paid in as capital of the corporation, to make loans in United States dollars repayable in dollars or loans in foreign currencies. 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 U.S. Treasury.

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

	September 30	
	1978	1977
Appropriated DIF capital	\$40.0	\$40.0
Transfer from earnings	10.0	10.0
Net losses	(3.3)	(1.7)
Uncommitted funds	(15.0)	(15.4)
Outstanding commitments	31.7	32.9
Undisbursed portion	(10.9)	(11.3)
Net loans outstanding	\$20.8	\$21.6

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 \$.7 million and \$1.5 million at September 30, 1978 and 1977, 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 guaranty 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, 1978, available for transfer to the Insurance or Guaranty Reserve, were \$17,581,580.

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 given by OPIC, all guaranties given 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, 1978 totaled \$283,005,916; and OPIC has cash and U.S. Treasury securities in excess of this amount. Claims against the Insurance Reserve could arise from certain liabilities shown on OPIC's Balance Sheet and certain contingent liabilities.

Direct liabilities related to claims settlements and chargeable against the Insurance Reserve amount to \$3,076,820 at September 30, 1978. OPIC will be required to make payments to discharge these liabilities in fiscal years 1980 to 1982.

Contingent obligations which could give rise to future additional claims on the Insurance Reserve include obligations under (A) guaranties issued in settlement of claims arising under investment insurance contracts, (B) pending claims under investment insurance contracts, (C) unresolved disputed claims and (D) outstanding investment insurance contracts. These four categories of contingent claims 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, 1978 under these guaranties, including liability as to interest, was \$180,372,000. 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
1979	\$ 24,286
1980	23,065
1981	30,344
1982	36,494
1983	32,269
1984-8	33,914
	\$180,372

Of the total contingent liability under claims settlement guaranties, \$166,624,000 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.

(B) Pending claims

OPIC follows a policy of recording investment insurance contract claims as financial liabilities only upon determination that a liability exists and 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.

The total amount of compensation requested in connection with formal applications for which no determination has yet been made is \$14.8 million. Included in this amount is \$6.8 million arising from seven claims—three of which are under expropriation coverage, one under inconvertibility, one under war/revolution/insurrection, and two under expropriation and/or inconvertibility—for which no determination of liability has yet been made, and \$8.0 million arising from one claim—under expropriation coverage—for which the amount of liability, if any, cannot yet be reasonably estimated.

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 making no reference to such notices in its financial statement. 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 \$3,169 million (Note 5D).

(C) Unresolved disputed claims

The claim of Revere Copper and Brass Incorporated (Revere) for expropriatory action arising from an investment in Jamaica, which, in accordance with the insurance contract had been submitted to arbitration for a final decision, was decided on August 24, 1978. Two of three neutral arbitrators found OPIC liable to Revere. The arbitrators finding liability set compensation at \$1,131,144 plus expenses of arbitration, rather than the more than \$90 million claimed by Revere. On September 26, 1978 Revere filed a motion in federal district court in the District of Columbia to modify or vacate that portion of the arbitral award fixing the amount of compensation. By order dated December 8, 1978, the court denied Revere's motion. On December 29, 1978, Revere filed notice of its intention to appeal.

A request by an investor whose claim had been paid in 1972 for approximately \$4.4 million of asserted excess salvage is being evaluated. There are no other unresolved disputed claims.

(D) 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, 1978 (excluding obligations under guaranties issued in settlement of claims) was as follows, in millions:

	Total	Uncommitted	Outstanding
Prior authorities	\$ 2,609		\$2,609
FAA Section 235	7,500	\$4,503	2,997
	<u>\$10,109</u>	<u>\$4,503</u>	<u>\$5,606</u>

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, 1978 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 to claims at September 30, 1978 is \$3,169 million.

Note 6: Guaranty Reserve

The Guaranty Reserve at September 30, 1978 totaled \$99,965,476; and OPIC has cash and U.S. Treasury securities in excess of this amount. 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, 1978, the Guaranty Reserve exceeded by \$66,357,487 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 participation in DIF loans. The outstanding commitments at September 30, 1978 were as follows, in millions:

	Total	Prior authority	FAA 234(b) and 235
Legislative authorization	\$777.1	\$27.1	\$750.0
Uncommitted	642.7		642.7
Total outstanding commitments	<u>\$134.4</u>	<u>\$27.1</u>	<u>\$107.3</u>
Currently at risk, net of repayments	\$123.2	\$27.1	\$ 96.1

The table above and the Balance Sheet include a direct liability of \$2,445,000 chargeable to the Guaranty Reserve and payable in semiannual principal installments of \$407,500 plus six percent interest through June 30, 1981. As installments are paid, an undivided interest is acquired in notes. The debt evidenced by the notes has been rescheduled.

Note 7: Recoveries on claims settlements

OPIC does not recognize recoveries with respect to claims settlements until the proceeds are received. However, pursuant to various settlement arrangements, certain foreign governments have an obligation to pay OPIC the following amounts, in thousands:

Fiscal year	Principal	Interest
1979	\$13,410	\$ 5,922
1980	13,073	5,304
1981	10,029	4,047
1982	8,753	3,273
1983	8,841	2,732
1984-8	<u>25,294</u>	<u>5,866</u>
	\$79,400	\$27,144

Of these amounts, \$74,836,000 in principal and \$24,197,000 in interest are obligations of the Government of Chile. A portion of Chile's debt to OPIC was rescheduled in connection with Chile's general rescheduling of international debt. The Government of Chile has to date made timely payment of all installments due in accordance with the new schedule. There has been no repudiation or default with respect to any foreign government obligations held or guaranteed by OPIC, and all governments are current in their payments.