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# Memorandum

TO : Mr. Thomas C. Niblock, Director  
USAID/Indonesia

DATE: August 26, 1980

FROM : Geoffrey G. Fritzler, B/AAG/EA

SUBJECT: Memorandum Audit Report No. 2-497-80-19  
Rural Works - Indonesia  
Loan Nos. 497-T-035 & 497-T-036 497-0002/  
Grant No. 497-0285

## BACKGROUND

More than 110 million Indonesians (80%) live in rural areas and attempt to make a living from agriculture and related activities. However, continuing pressure on these farmlands to support a population growth of more than 2% per year is forcing more and more families to seek off-farm employment to meet basic subsistence needs. Current estimates place the labor force at more than 40 million, and increasing at a rate of 1.4 million people per year.

Why  
Help  
is  
Needed

In recent years the Government of Indonesia (GOI) has become more aware of the problems of the rural population and has been experimenting with, and developing programs to increase food production, employment opportunities and more equitable income distribution.

After three years of experimenting with some small rural projects using PL 480 Title II commodities as wages, the GOI in 1969 instituted an extensive Food-for-Work or Padat Karya Gaya Baru (PKGB) program for Repelita I (GOI's 5-Year Plan). The program was an effort to overcome the most critical aspects of rural poverty and assigned highest priority to employment and improvement in the living standards of the poorest rural people. The Food-for-Work program was limited to food deficient areas.

Early  
Solutions

This program, which terminated in 1973, was considered a big success, both from the standpoint of the distribution of food to the really needy, as well as the value of the

Project

History

completed projects themselves. In the early 1970's Congress presented the "New Mandate" for foreign aid, according to which U.S. aid was to be concentrated in the lowest income groups, especially in the rural areas. In its search for qualified projects applicable to this segment of the population, AID turned to the PKGB program, a project singularly responsive to the wishes of Congress. The current Rural Works loan project is a direct descendant of the PKGB Food-for-Work program, the main difference being that the contribution is U.S. dollar funded instead of being food-funded. The project was proposed in late 1973 and authorized in 1974.

Cost

Sharing

Explained

The GOI has undertaken to continue to implement the PKGB program for the years 1974 through 1978 and budgeted an amount equivalent to \$20 million (about Rps. 8.3 billion for it). AID has made a dollar loan of \$6.8 million, of which \$300,000 was to be used to pay for two U.S. technical advisors, and the remainder was used to reimburse 38 percent of the estimated cost of approved and successfully completed projects for Indonesian Fiscal Years 74/75 through 77/78. The appropriated Indonesian funds are allotted by the Department of Manpower in Jakarta (DMP) to the poorest Kecamatan (counties), with an initial installment of about Rp. 13 million (\$21,000) to each Kecamatan. These specific Kecamatan select and design, with the assistance of the local Public Works technicians, a project or projects costing about this amount. The project's stipulations include a "65 percent of total cost" labor intensity requirement and an economic benefits prerequisite (no schools, mosques, etc.). Most projects fall into either the flood or irrigation canals or village roads categories. All activities funded by the initial loan are completed.

Recent

Developments

A subsequent four-year follow-on project, Rural Works II, has been in effect since April 1979. Beginning with Indonesian Fiscal Year (IFY) 1978/79 subprojects, and ending with IFY 1982/83, it will ultimately provide a technical assistance grant of up to \$3.0 million (\$1.5 million obligated to date). Concurrently, loans totaling \$25 million, will assist with the financing of up to 1,800 regular padat Karya subprojects, construction of a new training center, and training of staff (both in-

country and overseas). USAID/Indonesia reimbursement is expected to be about 35% of the cost of accepted subprojects. The GOI input is expected to be at least \$46 million. USAID/Indonesia reviews the designs and inspects completed work in the field, to determine the eligibility of subprojects for USAID reimbursement. The Mission employed an Indonesian staff of four engineers, for this purpose. Factors affecting eligibility for reimbursement include socio-economic benefits of the subprojects, as well as adequate design and construction. The subprojects must be fully functional.

Elsewhere, in the foreign donor community, the Royal Netherlands government (RNG) has agreed to provide loans of up to \$13,600,000 for reimbursing PKGB subprojects beginning with IFY 1977/78. Total consolidated donor input will not exceed 60 percent of approved subproject costs so that the GOI is the largest contributor.

<u>Other</u>	USAID	35%
<u>Donor</u>	RNG	<u>25%</u>
	Total Foreign Donors	60%
<u>Participation</u>	GOI	<u>40%</u>
	Total	100%

The RNG will use the same subproject acceptance criteria and reimbursement procedures as USAID in order to promote uniform standards of subproject selection, design and construction.

In addition, the RNG has agreed to provide DMP with technical assistance similar to that funded by USAID. Two technicians are on board and based in Surabaya, and two foreign national engineers will probably be hired to work with the USAID/Indonesia direct hire foreign national engineers.

A USAID-funded three-year host-government \$1.2 million contract between DMP and The New TransCentury Foundation was signed on April 19, 1979. It provides for six long-term specialists and several short-term consultants to work in close cooperation with GOI counterparts at Central headquarters and at four provincial (Kanwil) offices. The six long-term specialists arrived in Indonesia to begin two-year assignments in June and August 1979.

USAID/Indonesia obligations and expenditures through July 31, 1980 are as follows:

		<u>Obligated</u>	<u>Expended</u>
<u>Financial</u>	Loan 497-T-035	\$ 6,800,000	\$6,770,933
	Loan 497-T-056	25,000,000	-0-*
<u>Status</u>	Grant 497-0285	1,500,000	232,007

\* 502 subprojects, constructed in 1979/80, subject to potential USAID reimbursement of about \$6.0 million, are currently being inspected by Mission personnel.

### SCOPE OF AUDIT

Our audit of the Rural Works Project was designed to determine whether: (1) AID loan and grant funds were spent in accordance with AID regulations; (2) the program was managed in an efficient and economical manner; and (3) the objectives of the project were being achieved.

Our review included an examination of selected documents and correspondence, interviews were held with concerned USAID/Indonesia officials, contractor representatives and GOI officials. We inspected project sites in East Java and Bali.

The Rural Works Project was included in a 1976 audit of the USAID/Indonesia programs. The report included no specific recommendations pertaining to Rural Works.

The draft report has been discussed with Mission officials and their comments were considered and included in the report as appropriate.

### STATEMENT OF FINDINGS AND RECOMMENDATIONS

#### Progress and Implementation

Since the start of the project, there has been extraordinarily fast progress in the numbers of construction of subprojects. Since 1974, the Pèdat Karya Gaya Baru (PKGB, or Rural Works) has constructed 1,897 regular subprojects. USAID/Indonesia, between 1975 and 1979, participated in the funding of 839 of the subprojects and Mission personnel are currently inspecting the final construction of the 502 (included above) subprojects built by the PKGB in 1980. Between 1976 and 1979 USAID/Indonesia accepted for reimbursement 789, or 77%, of the 1,020 subprojects built by PKGB for this project and inspected by the Mission.

During the same time-frame, and in addition to the 1,897 regular subprojects, the PKGB, with GOI funds, built an additional 854 emergency subprojects, and 240 minor irrigation canals.

The PKGB Rural Works projects, with very modest funding (about \$21,000 per subproject), have produced remarkable achievements. One of the primary purposes of the project is to provide employment for the rural under-unemployed. To date, the project has funded about 60 million person-days of employment. The average cost per mile for construction of roads or canals is a very modest \$5,400.

There are reports of, and we observed, irrigation canals built in former one-crop areas that now raise three crops per year. There are additional reports of roads built a few years ago that are well maintained, while some others are not so well maintained. In some instances the GOI has, a few years after the PKGB built a basic all-weather road, upgraded it to a hard surface road.

The project is not without problems: The other elements of the project have not been nearly as successful as the pace of construction portion of the project.

Virtually all project problems relate to the extensive delays on the part of the GOI to provide the required technical inputs as well as the delay in purchasing the site for the training center.

Some problems are caused by the GOI's frequently delayed release of project funds. Such problems are by no means unique to the GOI, with AID/Washington having had similar problems, in the past. However, current year funds were made available in a timely manner, thus eliminating the need for formal recommendation on this subject.

The overall level of funds being provided by the GOI is more than adequate. The GOI would like to substantially increase the numbers of subprojects built each year, however it recognizes its lack of technical capabilities, and has agreed to limit the numbers of subprojects pending development of additional technical capabilities.

#### Delays in GOI Technical and Management Inputs

The GOI has not provided the number of employees or the types of

employees required to satisfactorily implement the project. Furthermore, the GOI has not even acquired the site for the training center that was to have been constructed and functioning by March 1980.

Six years ago (1974), when the project began, PKGB personnel consisted of six professional employees at headquarters and the provincial staff. Today there are still only six professional employees at headquarters. In 1974 PKGB constructed about 193 subprojects, whereas in 1978 they built 655 subprojects, with the same number of professional staff. Although this is a commendable accomplishment it points out the need to reexamine headquarter's professional staffing requirements.

Six years ago the PKGB did not have the capability to properly select, survey, design, prepare cost estimates, construct or evaluate a subproject. Today, with the possible exception of the construction element, the situation remains virtually the same.

Our positive conclusion concerning the improvement in the construction element of the project relates primarily to the PKGB's qualitative ability to construct 655 subprojects last year. That ability is directly related to the one successful recruitment and training program at the PKGB addressing the subproject construction foreman (PLP). Each subproject is headed by a PLP. The PKGB has hired a large number of additional PLP's, and has, through the coordinated efforts of the Ministry of Public Works and the AID grant-funded consultants, provided training for each PLP. Yet, inspite of impressive volume-related results the quality of construction remains marginal. The AID-funded training advisor has revised the training manual for PLPs whose active use should start this year. Its efforts are directed toward improving the quality of construction.

Most of the current problems relate to the selection, survey, design, cost estimates, inspection and evaluation of the subprojects. USAID/Indonesia, in commenting on that conclusion, and elaborating on its resolution, provided the following verbatim perspective:

"The AID funded contractor has begun to address the problem of subproject selection. A short term consultant worked in-country from July through December 1979. He reviewed in the field 52 PKGB subprojects from

various years and of different types. He also conducted interviews with subproject beneficiaries and PKGB staff throughout the country. As a result he identified certain factors that seemed to lead to a successful (beneficial) subproject, and developed surveys to be used by PKGB staff in choosing future subprojects. The surveys were subsequently revised based on their review during the workshop, and were field tested by the short term consultant in March and April 1980. In May 1980 PKGB central and province level staff were trained in the use of the subproject selection surveys by contractor personnel. They have in turn trained district level staff in the 5 major provinces in the use of the surveys. This represents the initial effort to solve subproject selection problems. The system will be reviewed and, if necessary, revised after the selection of the 1981/82 projects, a process underway at the time of this report."

To date, the Ministry of Public Works (PW), has performed, on a reimbursable basis, all survey and design functions for the PKGB. The PKGB does not intend to attempt to develop its own capabilities to do the work presently done by PW; however, the PW has an extensive program of its own and for that reason often finds itself in the position of being unable to respond to workload in either a timely or professional manner.

The lack of technical capabilities prevents the PKGB from effectively reviewing the surveys and designs prepared by PW. If the PKGB would have the competence, it would be able to screen out and reject all poorly conceived or poorly designed projects prior to the start of construction. USAID/Indonesia indicated that PKGB, the Contractor and the Mission are attempting to address this problem through the recruitment and training of PKGB "technicians", i.e. individuals who have demonstrated expertise as construction supervisors (PLPs) who will be given enough additional technical training to allow them to adequately review PW surveys and designs and reject poorly conceived or designed subprojects. The first seven technicians have been selected, given a one week intensive training course by the contractor, PKGB and PW personnel, and have been undergoing on-the-job training, since mid-July 1980. The training period will last about two years.

The PKGB, in coordination with PW, takes the various quantitative data presented in the project design, and applies PKGB-established wage rates and productivity factors to the total subproject cost estimate on which AID's reimbursement is based. To date, PKGB lacks the capabilities to prepare reasonably accurate estimate of cost. Subproject cost estimates are more related to the total rural works budget than to the accurate cost of the specific subproject. For instance, if there is a total budget of \$10 million for 500 subprojects each subproject will be allowed about \$20,000. In future, estimates should be subproject-specific. Even more importantly: We probed the abuse potential of the current methodology and satisfied ourselves that a number of safeguards, such as unit cost controls, have been installed and are operational.

For the sake of perspective, one should remember that initially, a primary purpose of the project was to provide wages for the rural poor. Within that first priority the broad and general method of estimating subproject cost was initially considered to be not too important. However, this initial relative lack of concern is no longer acceptable, with each subproject now being based on its own merits. Such a merit test includes a realistic cost estimate to do the job.

Historically, PKGB did not have, nor has it since acquired, the capability to inspect or evaluate the quality of construction, or to verify the socio-economic benefits of a subproject. This handicap has been acknowledged by both the GOI and USAID/Indonesia. When reviewing the Project Identification Document (PID) for the proposed loan, AID/W expressed specific concern over PKGB's lack of such capabilities. STATE 159529 of July 9, 1977 indicated . . . "Critical consideration here will be the pace at which Directorate of Manpower increases its own administrative effectiveness and oversight of subprojects, thereby permitting USAID to reduce inspection coverage to random sample. If major investment in staff time still required, USAID should consider reduction of AID financing to minimum necessary to consolidate gains being made in conceptual managerial improvement of Padat Karya program."

In response to AID/W's concern, USAID/Indonesia stated in the Project Paper that the Mission provides five direct project engineers (one US and four foreign national) for the purpose, and confirming the adequacy of that staff, adding further that by 1980, USAID/Indonesia would field-inspect less than 50% of the subprojects.

The Action Memorandum for the Administrator, dated January 17, 1979, urging the Administrator to approve the \$25.0 million loan, indicated "The DMP has significantly increased its capability to carry out the rural works program by increasing its staff, creating a central monitoring and evaluation unit, training local construction supervisors, and improving procedures for subproject selection, design and maintenance."

Clearly, this is not the case, because only on the sub-topic of "construction supervisors" and recent (May 1980) seminars on "subproject selection" have any of the problem been addressed. From May 1975 through 1980 USAID/Indonesia inspected virtually 100% of the subprojects, and rejected 23% of those inspected for AID financing. Through at least 1982, USAID/Indonesia will have to inspect 100% of each year's subprojects, thus necessitating, for the foreseeable future, a continued "major investment in staff time." The volume of subprojects is now so great, that the four USAID/Indonesia engineers do not have the time to properly review each subproject design, or to visit each site during construction.

USAID/Indonesia acknowledges that "the problem of PKGB's lack of an evaluation and inspection capability is being addressed only now. Padat Karya, the contractor and the USAID have developed a scope-of-work for a short-term consultant, scheduled to arrive in mid-October, who will plan a permanent in-house PKGB evaluation system. The system will be designed to evaluate subproject selection, construction and socio-economic benefits annually and feed the results back into PKGB's overall program management. The consultant will also develop a staffing pattern and training programs for a permanent evaluation section within DMP to operate the evaluation system. If successful, this section is intended to eventually assume the subproject inspection role presently held by USAID and the contractor's monitoring, evaluation and feedback roles."

### Training Center

The training center was scheduled to be constructed and functioning by March 1980; to date, the GOI has not even acquired the site for the training center. As a result, use of the training center will be delayed at least until early 1982.

Lack of a training center and lack of a training staff at PKGB have adversely impacted upon the AID grant-funded training advisor's ability to do his job and to contribute towards a

successful project implementation.

Recommendation No. 1

USAID/Indonesia require Padat Karya Gaya Baru to present a definitive and realistic plan to immediately address the inter-related problems of staff, staff capabilities, and training center construction.

Outstanding Advance to Padat Karya

In January and July 1977, USAID/Indonesia advanced \$388,420 of loan funds to the PKGB. By December 1977 PKGB was to submit to the USAID a detailed financial accounting of expenditures. Any unexpended amount or amounts determined to be inappropriate for AID financing were to be refunded to AID or deducted by AID from subsequent reimbursements. However, the GOI has not provided the required financial accounting of expenditures and the advance remains unliquidated.

The Mission, in April 1979, requested that PKGB submit these accountability statements; however, they have not been provided.

Recommendation No. 2

USAID/Indonesia require, prior to the release of additional loan funds, that Padat Karya Gaya Baru provides full accountability for the advance.

## REPORT RECIPIENTS

### USAID/Indonesia

Director 5

### AID/W

Deputy Administrator 1

#### Bureau for Asia:

Assistant Administrator 1

Deputy Assistant Administrator (Audit Liaison  
Officer) 1

Office of the Indonesia and South Pacific/  
Asian Affairs (ASIA/ISPA) 1

#### Bureau of Development Support:

Office of Development Information and  
Utilization (DS/DIU) 4

#### Office of the Auditor General:

Auditor General (AG) 1

Executive Management Staff (AG/EMS): 12

Plans, Policy & Programs (AG/PPP) 1

#### Area Auditor General:

AAG/W 1

AAG/Africa (East) 1

AAG/Egypt 1

AAG/Near East 1

AAG/Latin America 1

Office of the Legislative Affairs (LEG) 1

Office of Financial Management (FM) 1

Office of the General Counsel (GC) 1

### OTHER

Auditor General, Inspections and Investigations  
Staff (AG/IIS/Manila) 1