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**AUDIT OF
CANAL CITIES WATER AND SEWERAGE PROJECT
USAID/EGYPT PROJECT NO. 263-0048
Audit Report No. 6-263-85-5
July 25, 1985**

memorandum

DATE: July 25, 1985

REPLY TO
ATTN OF: Harold R. Gill, RIG/A/CairoSUBJECT: Audit Of Canal Cities Water And Sewerage Project
USAID/Egypt Project No. 263-0048
Audit Report No. 6-263-85-5

TO: Mr. Frank B. Kimball, Director USAID/Egypt

The subject report discusses the results of our audit of USAID/Egypt's Canal Cities Water And Sewerage Project. The audit objectives were to evaluate project progress, and to determine compliance with Agency regulations.

Accounting for AID-financed equipment and materials valued at \$75 million needed improvement. In addition, water and sewerage tariffs were not sufficient to maintain and operate the systems.

We recommended that \$75 million of project equipment and materials be accounted for, and that the GOE implement water and sewerage tariff reforms. Subsequent to our audit, your staff reported that the Government of Egypt initiated actions to increase tariffs and that on July 1, 1985 the Suez Canal Authority raised its water tariffs for residential use to a level set in the June 1985 National Tariff Plan. We accept this positive action to increase tariffs and will consider Recommendation No. 2 closed when the report is issued.

Other matters discussed were: disposal of project vehicles without USAID/Egypt approval; a non-competitive procurement awarded without a waiver; the provision of lump-sum payments under a cost plus fixed-fee contract; and the construction of a \$11.7 million pipeline that did not contribute to the project purpose.

Written comments received from USAID/Egypt have been reviewed and incorporated into the report. Management comments are presented in the body of the report and included in their entirety in Appendix 1.

Please advise us within 30 days of the actions taken or planned to close the recommendations. Thank you for the courtesies extended to my staff during the audit.

EXECUTIVE SUMMARY

The Regional Inspector General for Audit in Cairo has completed an audit of USAID's \$169 million Canal Cities Water And Sewerage project (263-0048) to upgrade the water and sewer systems in the Egyptian cities of Port Said, Ismailia and Suez. Our audit was made to determine if project objectives were being achieved, and if the project was in compliance with Agency regulations. The audit covered activities from project inception in September 1978 through March 1984.

At March 31, 1984, project expenditures were \$77 million. The funds were used for the procurement of materials, equipment, design of the works, and oversight of construction and rehabilitation.

The Government of Egypt through its implementing agencies, the Suez Canal Authority and the National Organization for Potable Water and Sanitary Drainage, agreed to provide the equivalent of \$114 million in Egyptian Pounds for the project to finance engineering services and construction.

The project is scheduled for completion in 1987.

With the exception of the findings summarized below and reported in detail in Part II of this report, we found nothing to indicate that the project is not making progress toward achieving its purpose of providing urgently needed improvements to water and sewer systems in the Canal Cities.

AID financing of equipment and materials for the project exceeded \$75 million. The Government of Egypt's inventory system did not assure that all items financed by AID were received in good condition, accounted for and used as intended. Receiving reports were either incomplete or not prepared at all, claims were unresolved, and transfers from port to warehouses and the construction contractors were not documented.

Revenues from user charges for water and sewerage services provided only a small percentage of the funds needed to maintain and operate the systems. In 1978, when the project was designed, rates for water usage had not changed for almost 60 years; sewerage services were provided free. Accordingly, covenants were included in the project agreements to rationalize rates. The Government had not implemented the covenants. In fact, the Mission increased funding for the project in 1979 and again in 1983 and each time agreed to further postponement of rate reforms. Increases in water rates originally scheduled for 1978 are now scheduled for 1986. Plans for future introduction of wastewater tariffs were due from the Government of Egypt in January 1984 but had not been submitted. Subsequent to our audit field work USAID/Egypt management reported that the Government approved a National Tariff Plan in June 1985.

A project contractor donated 10 used vehicles financed by AID to the Government's customs authorities for resale. Proceeds from the sale should be returned to AID.

Other matters discussed in the report are:

(1) The award of a \$5.4 million procurement of pipe without benefit of competition;

(2) USAID/Egypt's approval of a \$3.284 million lump sum work order which eliminated the potential review of costs, exceeded limitations on overhead established in the original contract, and authorized payment on the passage of time without regard for level of effort; and

(3) The construction of an \$11.7 million pipeline to a cement plant which does not contribute to the stated project purpose of providing water and wastewater facilities to the three Canal Cities.

Office of the Inspector General
Office of the Inspector General

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CANAL CITIES WATER AND SEWERAGE PROJECT
USAID/EGYPT PROJECT NO. 263-0048**

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PART I - INTRODUCTION

A. Background

The water and sewer systems of the three Suez Canal Cities, Ismailia, Port Said and Suez suffered heavy damage during the 1967-73 war years and deteriorated due to non-use during this period when the cities were virtually abandoned. As a result, the systems were incapable of providing satisfactory services. Water pressure fell to unsafe levels during periods of peak demand and water disinfection was erratic. Sewage backed up into dwellings and onto streets, polluting surface waterways and lakes. AID-financed studies recommended upgrading and reconstruction of the systems.

At the request of the Government of Egypt (Government), the Agency For International Development provided financial assistance to the Canal Cities water and sewer rehabilitation program. In Fiscal Year 1978, AID provided a \$60 million loan and a \$36 million grant to finance technical assistance, equipment and materials. In Fiscal Year 1983, AID granted an additional \$73 million for construction, the continuation of consulting services, and additional equipment and materials. As of March 31, 1984, AID's obligations for the Canal Cities Water and Sewerage project were \$169 million; project expenditures totalled \$77 million.

The Government of Egypt budgeted the equivalent of \$114 million in Egyptian Pounds for engineering services and construction.

The Suez Canal Authority (SCA) and the National Organization for Potable Water and Sanitary Drainage (NOPWASD) were the GOE implementing agencies for the project. The SCA was responsible for design, construction, operation and maintenance of the water systems in the three Canal Cities. NOPWASD was responsible for the design and construction of the sewer systems in the three cities and for the construction of the Southwest Main, a 60 kilometer water pipeline from Suez city to a cement plant.

Contract services for design and construction supervision were provided by Canal Cities Consultants (CCC), a joint venture of three U.S. firms: Hazen & Sawyer; Metcalf & Eddy International, Inc.; and Pirnie-Harris International. The contracts were for up to \$18.7 million.

Most of the \$169 million AID-financing was for the procurement of equipment and materials. The largest segment of the equipment

and materials procured was pipe which represented 80 percent of total procurement.

The project is scheduled for completion in 1987.

B. Audit Objectives And Scope

The objectives of the audit were to determine if the project purpose was being achieved, and to determine compliance with Agency regulations.

We visited project sites, examined project records, and interviewed project personnel at USAID/Egypt, the Suez Canal Authority, the National Organization for Potable Water and Sanitary Drainage, and the contractor (Canal Cities Consultants). Our audit was made during the period January through May 1984 and covered project activities from September 12, 1978 through March 31, 1984.

A major element of our review was the examination of Government records relating to the procurement of \$75 million in equipment and materials because our audit survey indicated poor internal controls over procurement. We examined procurement records at the offices of NOPWASD and the SCA in Cairo, Ismailia, Port Said and Suez. In February and March 1984, we inventoried a sample of pipe valued at \$21 million in the three Canal Cities.

We did not audit dollar costs of the technical assistance contracts because supporting documentation was maintained at the contractor's U.S. headquarters and was not available in Egypt.

Our audit was made in accordance with generally accepted government audit standards.

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PART II - RESULTS OF AUDIT

A. Findings And Recommendations

1. Accounting For AID-Financed Equipment And Materials Should Be Improved

AID financed equipment and materials costing \$75 million for the project. The GOE and its consultant agreed to establish and maintain an inventory system to track these commodities from point of shipment through end use. To assure that all AID-financed commodities were actually received and used as intended, system controls need to be strengthened. System weaknesses included incomplete and missing receiving reports, unresolved claims against suppliers, undocumented transfers of commodities to construction contractors, and procurement of equipment that was unsuited to the needs of the project.

Recommendation No. 1

We recommend that USAID/Egypt:

- a. have the Suez Canal Authority and the National Organization for Potable Water & Sanitary Drainage account for all AID-financed equipment and materials;
- b. ensure that all claims against suppliers are resolved; and
- c. have the National Organization for Potable Water and Sanitary Drainage develop plans to use or transfer AID-financed equipment valued at \$166,000 to another USAID project.

Discussion

The standard provisions of the project agreements require the Government of Egypt to maintain records and controls on the receipt, storage, issue and use of goods and services. Section B-5 of the Standard Provisions states that the grantee will "maintain or cause to be maintained, in accordance with generally accepted accounting principles and practices consistently applied, books and records relating to the Project and to this Agreement, adequate to show, without limitation, the receipt and use of goods and services acquired."

Also, the Consultant contracts included a requirement to "Review ... procedures for documenting and controlling receipt, storage and issuance of all equipment and materials for conformance with AID's requirements, and advise as necessary." (Sections 3.2.3 and 6.2.3 of the Scopes of Work.)

System Controls Need To Be Strengthened

Receiving The SCA and NOPWASD did not match commodities received at Egyptian ports with amounts billed and shipped by suppliers. Receiving reports were not prepared or were incomplete. Thus, there was no assurance that all commodities paid for by AID were actually received in good condition.

AID financed \$36.4 million of equipment and materials for the Suez Canal Authority. Records at the port included invoices and bills of lading. However, receiving reports did not document whether or not quantities invoiced were actually received. Pipe was a particular problem. Total pipe procured involved 26,963 pieces at a total cost of \$21.6 million. Each invoice for pipe showed total length shipped, cost per meter, number of pieces and total cost. Receiving reports showed number of pieces received but did not show total length. We measured a sample of pipe and found that the length was not standard; individual pieces varied by as much as one meter. SCA would have had to measure the individual pieces to assure that total meters of pipe billed were actually received.

The National Organization for Potable Water and Sanitary Drainage (NOPWASD) received \$39.2 million of AID-financed equipment and materials. The Organization documented actual receipts for only one of eight shipments. The purchasing department had copies of suppliers' invoices and packing lists, but in the absence of receiving reports had no basis for determining if all items paid for had been received in good condition. According to Organization officials, not a single shortage or damage claim had ever been filed on the \$39.2 million of commodities received.

A construction contractor, Petrojet, received \$11.7 million of NOPWASD's \$39.2 million of commodities directly from the port for the construction of the Southwest Main pipeline. The contractor did not prepare receiving reports or inventory records. We attempted a physical inventory of two line items, 400 and 500 millimeter pipe invoiced at \$3.9 million. Our inventory analysis included a count of pipe in storage and estimates of the length of pipe already installed at the time of our review. Although imprecise because of the estimates of pipe installed, our analysis showed that about \$55,000 had been paid to suppliers for pipe that could not be accounted for. However, our analysis relied heavily on NOPWASD's incomplete records. In addition, pipe valued at \$58,000, that should have been received by Petrojet, was missing at the construction site (See Exhibit 1).

Claims The Suez Canal Authority (SCA) filed claims for short shipments and damaged materials totaling \$107,855 during the period June 28, 1982 to December 31, 1983 (See Exhibit 2). None of these claims had been resolved. On the other hand, NOPWASD had not filed a single claim for shortages or damages on its AID-financed shipments costing \$39.2 million. SCA's experience and common sense would indicate that not all of the thousands of individual items consigned to NOPWASD arrived in good condition.

Undocumented Transfers The Suez Canal Authority had good records at its Central Warehouse showing in detail the commodities shipped to intermediate storage yards in the Canal Cities. The National Organization for Potable Water and Sanitary Drainage had no such records. The Organization could not document shipments to Petrojet or to storage yards in the Canal Cities. Petrojet had no receiving reports or inventory records. At the time of our visit to the Petrojet construction site, we found 233 pieces of pipe costing \$130,000 scattered in the desert along 60 kilometers of completed construction (See Exhibit 1). The pipe was not needed for construction and should have been collected and returned to a controlled storage area. Storage yards in the Canal Cities for commodities consigned to both SCA and NOPWASD had incomplete receiving reports and inventory records. Commodities were stored in disorderly heaps in the open, at numerous locations.

Our best effort to inventory 2105 pieces of pipe NOPWASD shipped to the Canal Cities showed 71 pieces of pipe valued at approximately \$213,000 missing (See Exhibit 1). Even if our physical count was accurate, there was no assurance that the pipe billed by the supplier and shipped to storage areas in the Canal Cities was received. The supplier billed and was paid for length of pipe rather than by pieces of pipe.

Unsuitable Equipment Governorates are responsible for maintaining the sewer systems in the three Canal Cities. NOPWASD procured and turned over to the governorates equipment that the governorates were not using; a \$122,000 TV system for inspecting sewer lines and three pickup trucks costing \$44,000. Governorate personnel told us that the TV system could not be used in the Canal Cities' sewer lines, and the pickups were not used because the eight cylinder engines used too much gasoline.

Construction of water and sewer systems is now underway in the three Canal Cities and construction contractors are removing commodities from storage areas. Lapses in inventory control need to be corrected to ensure that all AID-financed equipment and materials are received, claims are resolved and the commodities are used as intended.

Management Comments

USAID/Egypt Management agreed that even though improvements had been made, inventory procedures need to be improved. According to USAID/Egypt, the Canal Cities Consultants inventoried Suez Canal Authority (SCA) and the National Organization for Potable Water and Sanitary Drainage (NOPWASD) equipment that arrived over the past year. However, USAID/Egypt said it was impossible at this stage of the project to make an exact inventory of large quantities of equipment and materials that have already been installed at construction sites. Management also stated that accounting for equipment incorporated into construction will have to wait to completion of construction.

In addition Management stated that (a) follow-up would be made on all outstanding claims to see that all claims are settled and (b) effective use will be made of the equipment valued at \$166,000.

Office Of The Inspector General Comments

We believe a full accounting of the \$75 million AID-financed equipment and materials should be made. All equipment and materials in country should be reconciled with GOE records of receipt. An inventory would obviously not be impossible. As a minimum, there should be a physical inventory of yet-to-be installed equipment and materials. This inventory (a) would provide the basis for current control and (b) added to inventory on the as-built drawings, would be the basis for determining what was delivered.

2. Water And Sewerage Tariffs Were Too Low

With the exception of changes for certain industrial users and ships transiting the Suez Canal, rates for water usage have not been increased since 1926 and provide less than half the revenues required for operation and maintenance of water facilities. Sewerage service is provided free of charge. Unless tariffs are raised as required by the project agreements, revenues will be insufficient to maintain and operate the AID-financed systems.

Recommendation No. 2

We recommend that USAID/Egypt arrange for the Government of Egypt to implement water and sewerage service tariff reforms.

Discussion

The September 1978 project paper characterized the then existing condition of finance for the Egyptian water and wastewater sector as chaotic. Rates for water had not changed since 1926 and in 1978 were equivalent to 9.5 U.S. cents per 1000 gallons. (By comparison, 1977 Fairfax County, Virginia rates were 87.5 U.S. cents per 1000 gallons.) Tariffs were not charged at all for sewerage services. Accordingly, clauses were included in the project agreements whereby the Government of Egypt (Government) covenanted to:

- No later than April 30, 1978, set SCA tariffs at a level high enough to produce a reasonable rate of return on average net fixed assets in operation, appropriately valued and revalued from time to time. (Project loan agreement for \$60 million dated September 30, 1978.)
- No later than April 30, 1980, set SCA tariffs at a level high enough to produce a reasonable rate of return on average net fixed assets in operation, appropriately valued and revalued from time to time. (Project Grant Agreement for \$36 million dated June 27, 1979.)
- No later than January 1986, SCA tariffs shall be set at a level sufficient to cover operation and maintenance, depreciation and debt repayment. In addition, GOE and NOPWASD were to provide by January 1, 1984 and at six month intervals thereafter plans for introduction of wastewater tariffs including schedules and levels of such tariffs. (First amendment to project grant agreement, dated September 12, 1983, increasing the total grant to \$109 million.)

In addition to the above covenants, the Government and USAID signed a memorandum of understanding on April 1, 1984. The two parties agreed to implement a \$1.2 billion funding program for water and sewerage in Egyptian cities, including the Canal

Cities. Funds were to be provided during the calendar years 1982 through 1987 subject to U.S. Congressional approval. The two parties also agreed to the need for management and administrative actions including tariff increases adequate to cover the cost of water and wastewater operations, maintenance, debt service and routine improvements. Also the Government was to provide appropriate increases in the size of the operations, maintenance and investment budgets to fund the sector. The memorandum anticipated that the construction program would be completed by July 1, 1989 with the action on tariffs and GOE financing to be phased in and fully in place by that time.

In summary, AID periodically committed additional millions of dollars to water and sewer programs in Egypt during the 1978-1984 period, and each commitment of U.S. funds further postponed implementation of the tariff reforms needed to establish the financial integrity of the AID-financed systems. Water tariffs to be in place by October 1978 are now to be in place by July 1989.

At the time of our audit, the Government of Egypt had not implemented the covenants. Water tariffs originally covenanted for implementation by April 30, 1978 and then by April 30, 1980, had not been increased. Even the plan for sewerage tariff reform due on January 1, 1984 had not been submitted.

During our discussions of the draft report in June 1985, USAID/Egypt personnel told us that the Government had initiated action to increase water and sewerage rates. The increased rates, however have yet to be implemented.

With over \$750 million obligated for water and sewer projects for the Canal Cities and other locations in Egypt and additional funding anticipated, USAID/Egypt needs to elicit action from the Government of Egypt to rectify conditions that have changed little since 1978.

Management Comments

In their written response to our draft report, USAID/Egypt stated that the Government of Egypt approved a National Tariff Plan in June 1985. The plan calls for increases in residential water tariffs and the implementation of a 10 percent surcharge on water bills to cover a portion of wastewater system operation and maintenance costs. USAID/Egypt Management also pointed out that on July 1, 1985, the Suez Canal Authority raised its water tariffs for residential use to a level set in the National Tariff Plan.

Office Of Inspector General Comments

As reported by USAID/Egypt, the Government of Egypt initiated actions to correct the tariff situation. Because of this positive action to increase tariffs, the recommendation will be closed upon issuance of this audit report.

3. Project Vehicles Were Disposed Of Without USAID/Egypt Approval

The Canal Cities Consultants transferred 10 Government of Egypt titled project vehicles to the Government's Customs Department for disposal. The vehicles (See Exhibit 3), were in need of repair, and neither SCA nor NOPWASD wanted the vehicles. The project agreement standard provisions required that use of project vehicles for other than project purposes must receive the written approval of USAID/Egypt. The 10 vehicles were not disposed of in accordance with the project agreement.

Recommendation No. 3

We recommend that USAID/Egypt determine the disposition of the ten vehicles given to the Government of Egypt's Customs Department, and if the vehicles have been sold, recover the proceeds.

Discussion

The Consultant disposed of 10 AID-financed vehicles without USAID/Egypt's approval.

Standard provisions of the project agreements state that any resources financed by AID will be used on the project until the completion of the project, and thereafter will be used to further the objectives sought in carrying out the project. USAID/Egypt must approve any waiver of the provisions. If a commodity is used for unauthorized purposes the borrower/grantee may be required to refund to AID the entire amount reimbursed for the transaction.

If the Consultant transferred the 10 vehicles to SCA or NOPWASD, payment of custom duties was required because the vehicles did not have permanent government plates. The consultant requested information from the Government on how to dispose of the vehicles and was advised to turn the vehicles over to the Customs Department.

At the time of our audit, the consultant did not know the status of the vehicles, but advised that the vehicles would be sold and the proceeds used to offset custom duties on the vehicles. If the vehicles have been sold, USAID/Egypt should seek a refund of the sale price because the project agreements preclude the payment of customs duties on AID-financed commodities.

Management Comments

Management agreed to follow the audit recommendation to determine the exact disposition of the vehicles. Management also stated that it would attempt to recover proceeds if the Customs Department has sold the vehicles.

B. Compliance And Internal Control

Compliance

USAID/Egypt's Canal Cities Water and Sewerage Project (No. 263-0048) was authorized to provide assistance for the construction and rehabilitation of the Canal Cities water and sewerage systems. The project operated within the provisions of Handbook 3 (Project Assistance) and within agreements between USAID/Egypt, the Government of Egypt and a contractor. Water and sewer systems tariff rates had not increased as prescribed in project agreements' covenants (page 7). Also project vehicles were disposed of without USAID/Egypt's approval (page 9).

Internal Control

All obligations and commitments were recorded on USAID/Egypt financial records, and were supported by adequate obligating documents. However, we did note that management of \$75 million of AID-financed equipment and materials needed improvement (page 3).

C. Other Pertinent Matters

1. Non-Competitive Procurement Awarded Without A Waiver

On September 26, 1983, the Suez Canal Authority amended a 1981 supply contract increasing the quantities and increasing the dollar value by \$5.4 million. USAID/Egypt approved the amendment for AID financing on January 2, 1984, although formal competitive procedures were neither followed nor waived as required by the rules of AID Handbook 11, Country Contracting.

The Handbook sets out rules to be followed in country contracting. The rules are either derived from U.S. Government statute or based on AID's experience in carrying out its responsibility for stewardship of U.S. Government funds. In certain cases, rules may be waived by an authorized AID official based on a written justification (Handbook 11, Chapter 3, Section 1.3). Rule 2.2 sets out requirements for formal competitive procedures and requires that waivers be sought if procurement is to be negotiated with a single source:

- Contracts for equipment and materials are normally awarded on the basis of formal competitive bids (Rule 2.2.1).
- Informal procedures, including advertising requests for quotations may be used when (a) it is impossible to develop adequate specifications for use in an invitation for bids, (b) when proprietary procurement is justified or (c) when adherence to formal procedures would impair project objectives (Rule 2.2.3).
- Competition may be waived and negotiation with a single source authorized if (a) an emergency situation exists, (b) when proprietary procurement is justified or (c) when competitive procedures would impair U.S. objectives. A waiver in these circumstances may be authorized only by the AID Administrator if the value of the procurement exceeds \$500,000 (Rule 2.2.6).

The USAID/Egypt Director determined that the \$5.4 million procurement could be awarded without competition; a waiver was neither sought nor justified. The Director approved the award on the basis of a clause in the contract that allowed a change in the contract quantities by plus or minus 20 percent and on the Mission's assumption that tenderers to the original contract knew that a 20 percent variation in quantity was possible at a date subsequent to contract award. A further consideration was the contractor's offer to provide the materials at the same price included in the original 1981 contract. USAID/Egypt officials assumed that re-advertising would result in higher prices.

The clause allowing a 20 percent variation in quantity was included in a 1981 invitation for tenders and stated that "The Purchaser (SCA) shall have the right at the time of contract award to increase or decrease the quantity of any item by 20% plus any fraction necessary to equal a whole number of the quantity tendered upon the unit price offered." (Underscoring added.)

The USAID/Egypt legal staff concluded on October 16, 1983 that the terms of the 1981 tender did not permit an amendment; the 20 percent increase or decrease could be made only at the time of award of the original contract. (The original contract was awarded on October 26, 1981, for \$29 million.) The legal staff concluded that USAID/Egypt must either obtain the Administrator's waiver for non-competitive procurement or enter into a formal competitive procedure.

On December 18, 1983, the legal staff modified its position, stating that:

"If the bidders knew or should have known from the facts and circumstances apparent at the time of the original IFB that the competition included the possibility of up to 20% additional order at a negotiated price with the additional quantity to be based on completion of the Project design, then the Legal Office concurs that this would be adequate competition for the follow-on order and concurs that the follow-on order does not constitute a new procurement amendment requiring further competition before it can be financed by AID. The question that has caused us so much trouble is determining whether the facts adequately support such a determination. Of course, we do not ultimately decide this point. The determination as to the reasonableness of this interpretation of the facts and of the language the IFB must rest with the Mission official who approves the financing of the host country contract, in this case, the Mission Director."

The legal staff also noted that, if the contract was AID-direct instead of host country, the issue would be more clear-cut against making the award.

On January 8, 1984 the USAID/Egypt Director approved the non-competitive amendment for an additional \$5.4 million on the basis that, in 1981, tenderers knew that design was not finalized and that changes in the range of 20 percent were possible.

Management Comments

According to USAID/E, the legality of proceeding with AID funding of the add-on was reviewed by AID legal staff and appropriate management officials; the decision to proceed was fully cleared at that time.

Office Of Inspector General Comments

We recognize USAID/Egypt's position concerning non-competitive procurement, but also recognize that the legal staff's position was modified. The original conclusion of USAID/Egypt's legal staff did not permit the \$5.4 million non-competitive procurement after the award of the original contract. We believe that AID rules for country contracting were not followed. USAID/Egypt should have either obtained the Administrator's waiver or followed formal competitive procedures on this \$5.4 million procurement.

2. Lump Sum Payments Approved Under A Cost Plus Fixed Fee Contract

In June 1983, USAID approved a \$3.284 million lump sum work order under Canal Cities Consultants' Contract with the Suez Canal Authority. The work order converted a cost plus fixed fee contract to lump sum and as a result: (a) eliminated the potential review of costs; (b) exceeded limitations on overhead established in the original contract; and (c) authorized payment based solely on the passage of time without regard for level of effort. Also, the period of the lump sum work order coincided with a \$4.0 million cost reimbursement plus fixed fee work order issued in March 1983 under Canal Cities Consultants' contract with the National Organization for Potable Water and Sanitary Drainage. Both contracts are financed under the project. Both work orders provided construction supervision and consulting services to the two GOE Agencies; the language of the scopes of work was almost verbatim.

The position titles of contractor employees are, with few exceptions, identical for both work orders. At least four employees were to be concurrently shared between the two work orders. Concurrent lump sum and cost reimbursement work orders created the possibility that AID payment would exceed 100 percent of costs incurred by the contractor. Cost data used to justify the lump sum included questionable amounts of at least \$91,000, (See page 17) plus liberal allowances for air fares and per diem.

AID guidance on Country Contracting (Handbook 11) sets out criteria for determining which type of contract; cost reimbursement, time rate, or lump sum is most appropriate. Cost reimbursement contracts are advisable when uncertainties in the amount of work, or conditions under which the work must be performed make accurate determination of the costs involved impossible. Time rate contracts are useful when services are tied to schedules whose duration and timing are uncertain, but the type of skills is known. Lump sum, fixed price contracts should be used whenever the scope and duration of services to be performed may be defined in advance with sufficient precision to enable both contracting parties to determine with reasonable accuracy the personnel and other requirements for the performance of the contract. A fixed price contract is most suitable when the work is precisely defined and the contract period is sufficiently short to minimize contingencies covered in the price.

Background In September 1979, Canal Cities Consultants and GOE agencies executed two cost plus fixed fee contracts, both contracts were AID-financed under the Canal Cities Water and Sewerage Project. The first contract was with the General Organization for Sewerage and Sanitary Drainage (later renamed the National Organization for Potable Water and Sanitary Drainage) to provide engineering and advisory services. The total estimated contract cost, including amendments and work orders, was \$11.6 million. The second contract was with the Suez Canal Authority; also for engineering and advisory services. The total contract cost, including amendments and work orders, was \$7.08 million. In addition to the dollar costs, the GOE provided local currency to finance local costs of the contractor.

In March 1983, Canal Cities Consultants and the National Organization for Potable Water and Sanitary Drainage executed work order number two for supervision of construction and installation of equipment and other services at an estimated cost reimbursement plus fixed fee of \$4 million.

In June 1983, work order number one was issued under the contract with the Suez Canal Authority. The work order provided Canal Cities Consultants an AID-financed lump sum of \$3.284 million to supervise construction and the installation of AID-financed equipment. The award of a lump sum for these services conflicts with Handbook 11 guidance and eliminates cost controls incorporated in the basic contract.

Review Of Contractor Costs Estimated costs provided by the Contractor in support of the lump sum amount included salaries, overhead, travel and other costs plus fee. Actual costs incurred are no longer subject to voucher examiner review or post audit. The contractor gets paid the lump sum whether or not estimated costs are actually incurred. Also, four to six contractor employees are to be shared with the National Organization for Potable Water and Sanitary Drainage cost reimbursement contract.

Support costs for shared employees appear in both the cost justification for the lump sum work order and in the budget for the cost reimbursement work order. The Project Director's travel costs for example:

Project Director
Travel Per Diem and Related Costs
36 Month Period

	<u>Included in Lump Sum Estimate</u>	<u>Included in Reimbursement Budget</u>	<u>Total</u>
Round trips for family of 3:	\$ 6,000	\$12,000	\$18,000 <u>1/</u>
Ground Transport	225	450	675 <u>1/</u>
Stopover days	600	1,200	1,800 <u>1/</u>
Medical Processing	750	750	1,500
Excess Baggage	600	2/	600
Relocation Allowance	800	800	1,600
Personal Effects in/out of Storage	2,750	2,750	5,500
Personal Effects Storage Per Month	2,850	3,610	6,460 <u>3/</u>
Air Freight	4,800	2,100	6,900 <u>4/</u>
Sea Freight	5,200	2,600	7,800 <u>5/</u>
Settling In Cost	1,000	1,000	2,000
	<u>\$25,575</u>	<u>\$27,260</u>	<u>\$52,835</u>
	=====	=====	=====

1/ One round trip under lump sum, two round trips under reimbursement.

2/ None Listed

3/ \$190 per month for 34 months.

4/ \$8.00 per pound under fixed price, \$3.50 per pound under reimbursement.

5/ \$2.00 per pound under fixed price, \$1.00 per pound under reimbursement.

It appears that payment of certain categories of support costs for shared employees under the National Organization for Potable Water and Sanitary Drainage (NOPWASD) reimbursement contract work order, effects in/out of storage for example, would result in AID paying more than 100 percent of the costs because they have already been included in the lump sum Suez Canal Authority (SCA) contract work order.

Overhead Both the SCA and NOPWASD contracts contained clauses to the effect that actual overheads would in no event exceed ceiling rates specified in the contracts. Overhead rates allowed under the contracts' work orders exceeded the maximum established by the underlying contracts. Also, calculation of the overhead in both work orders was inflated because the rates were developed using a 40 hour per week labor base. The rates so developed were then applied to salaries and personnel costs based on a 45 hour per week labor base. The error should be corrected on NOPWASD's work order when provisional rates are audited and adjusted to actual. Under the lump sum work order, however, the error is locked in there is no provision for adjustment.

Payment Based On Passage Of Time Each month, the contractor receives a percentage of the lump sum regardless of level of effort. Thirty-six monthly payments were scheduled as follows:

<u>Month</u>	<u>Monthly Factor</u>	<u>Cumulative Percentage</u>
1 through 12	2 percent	24 percent
13 through 30	3.5 percent	87 percent
31 through 35	2 percent	97 percent
36	3 percent	100 percent

As noted above, the work order is primarily for supervision of construction and equipment installation. The contractor's level of effort should therefore be controlled by the contract award process and subsequent progress of the construction and equipment installation contractors, not by the passage of time.

Questionable Cost Estimates Items costing \$91,000 included in the June 1983 lump sum work order are questionable. NOPWASD under its cost reimbursable contract absorbs half of the sea and air freight costs for CCC personnel. Although SCA absorbed the same costs under its cost reimbursable contract with CCC, the lump sum work order shifted the return sea and air freight costs to the dollar side financed by AID.

Lump Sum Work Order
Inflated Freight Estimate

	<u>SCA Weight Allowance (LB)</u>	<u>NOPWASD Weight Allowance (LB)</u>	<u>Difference in Weight (LB)</u>	<u>\$ Cost Per LB</u>	<u>Difference in Costs</u>
Air Freight	15,200	7,450	7,750	\$4.00	\$31,000
Sea Freight	73,400	36,300	37,100	1.00	37,100
Total					\$68,100
					=====

(Current air freight rates from Cairo to Washington D.C. are LE2.75 per kilogram or about \$1.51 per pound at the LE.83 = \$1 rate.)

Also, the lump sum estimates include \$6,890 for air fares and ground transportation for 26 R&Rs; yet only an estimated 9 employees and family members are scheduled to be assigned to the contract for more than 15 months each. The overcharge is about \$4,500 (\$6,890 x 17/26 = \$4,505). In addition, two round trips to the States are provided for the 9 employees and dependents scheduled for 24 month assignments. Only one round trip appears justified. The overcharge is \$18,000 (9 round trips at \$2,000 each). Per diem for 146 stopover days en route was \$100 per day for adults and \$50 for minors or an average of \$95 per day; most stopover points in Europe have rates lower than \$95 per day.

Air fares for 66 adult round trips were included in the cost estimates at \$2,000 each. While some trips from the western United States may approach this amount, \$2,000 per trip is undoubtedly very liberal.

It appears that USAID officials approved this lump sum work order with little, if any, review of the cost estimate justifying the lump sum.

Management Comments

According to USAID/Egypt, the complete details on contract negotiations between CCC and SCA were not available to USAID, and they should be reviewed to determine the justification of the lump sum costs. Management also stated that the lump sum contracting mode should not be discarded without a thorough evaluation of both the advantages and disadvantages.

3. Construction Of The \$11.7 Million Southwest Main Pipeline Did Not Contribute To Project Purpose

A \$11.7 million pipeline to supply potable water to the AID-financed Suez Cement Plant was funded from this project. The pipeline will not contribute to the achievement of the project purpose.

According to AID's Handbook 3, a development project should provide assistance to accomplish a result directly related to a discrete development problem. The discrete development problem in USAID's Water and Sewerage project was the provision of water and wastewater facilities for the Canal Cities.

The Southwest Main is a 60 kilometer pipeline extending from the Suez water treatment plant through the desert to the AID-financed portland cement plant constructed for the Suez Cement Company. The project paper and its amendments provided little justification for the pipeline. The project paper stated only that the pipeline with its associated pumping stations and storage tanks would serve the cement plant and the developing area between Adabiyah and Ein Sukna. The pipeline would also supply water for Adabiyah port and cold storage facilities as a means to develop the Port of Suez. There was no analysis in the project paper as to number of communities to be served by the pipeline or their projected rate of water consumption.

Management Comments

In response to our draft report, USAID/Egypt Management stated that the Southwest Transmission Main was part of the Water and Wastewater Master Plans developed for the Canal Cities in 1977/78, and was described in the plans as one of the most critical Phase I projects.

**AUDIT OF
USAID/EGYPT'S
CANAL CITIES WATER AND SEWERAGE PROJECT
PROJECT NO. 263-0048**

PART III - EXHIBITS AND APPENDICES

EXHIBIT 1

Canal Cities Water And Sewerage Project
Project No. 263-0048
Shortages, Losses And Non-Use Of Pipe Procured By
The National Organization
For Potable Water And Sanitary Drainage

SOUTHWEST MAIN PIPELINE

<u>Unaccounted For Pipe At NOPWASD</u>	<u>Value</u>
7 pieces 900 millimeter pipe	\$ 10,458
22 pieces 800 millimeter pipe	26,971
13 pieces 500 millimeter pipe	7,370
25 pieces 400 millimeter pipe	9,974
	<u>\$ 54,773</u>
	=====

Unaccounted For Pipe At Petrojet Construction Site

109 pieces of 500 millimeter pipe	\$ 58,401
	=====

Pipe Found At Construction Site Not Used

17 pieces of 800 millimeter pipe	\$ 20,841
5 pieces of 600 millimeter pipe	3,678
127 pieces of 500 millimeter pipe	71,995
84 pieces of 400 millimeter pipe	33,512
	<u>\$130,026</u>
	=====

CANAL CITIES SEWERAGE SYSTEM

Unaccounted For Pipe

	<u>Pieces</u>	<u>Average</u> <u>Cost</u>	
Pipe Billed and shipped to Canal Cities	2,105		
Auditor's Physical Count	<u>2,034</u>		
Unaccounted For Pipe	71	\$3,000	\$213,000
	=====	=====	=====

Canal Cities Water And Sewerage Project
Project No. 263-0048
The Suez Canal Authority
Claims Against Suppliers

<u>Quantity</u> <u>Short or</u> <u>Damaged</u>	<u>Pipes</u>	<u>Value</u>
9	800 millimeter	\$ 9,675
43	600 millimeter	38,566
7	400 millimeter	337
5	300 millimeter	151
5	200 millimeter	243
	 <u>Other Materials</u>	
1	400 mm Socket 450 Bend	408
1	20x12 " Flange Reducer 20" LG	780
1	24 " FF Pipe DI 53/47 5.95M	5,820
2	16 " Flange 22 1/3 Bend DID	1,349
1	48 " Fastite Pipe CL 52/65	295
1	12 " Fastite Pipe CL 52/37	292
3	Accessories for Tapping & Drilling Machines	49
72	Accessories for Tapping & Drilling Machines	2,742
1	48 " Pipe Damage 10% of \$3,318	332
1	Connection with Flange & Tail 16"	1,764
5	Connection with 7 Flanges, length 300c M/16"	2,708
1	Connection with Flange and Tail 14"	394
1	Connection with 2 Flanges, length 90 CM/16"	799
2	Boxes Spare Parts for Vehicles	5,449
83	Fire Hydrants	35,409
1	400 MMX 300 Double Socket Taper 260 MM LG DI 64KG.	293
1	500 MM/FST wall castings DI/750 MM W/C Center 426KG	not known
	TOTAL	<hr/> \$107,855 *****

Canal Cities Water And Sewerage Project
Project No. 263-0048
Vehicles Turned Over To GOE Customs By U.S. Contractor

<u>MODEL</u>	<u>SERIAL NO.</u>	<u>YEAR OF PURCHASE</u>	<u>LICENSE PLATE NO.</u>	<u>END USER</u>
CHEVROLET NOVA	147257	1980	11728	CCC SCA
CHEVROLET NOVA	146961	1980	12151	CCC SCA
CHEVROLET MALIBU	463067	1980	10375	CCC SCA
CHEVROLET MALIBU	463296	1980	10352	CCC SCA
CHEVROLET MALIBU	181449737	1980	10119	CCC SCA
CHEVROLET MALIBU	81448967	1980	13321	CCC SCA
CHEVROLET SUBURBAN	168104555	1980	11579	CCC NOPWASD
CHEVROLET MALIBU	181449568	1980	10713	CCC NOPWASD
CHEVROLET MALIBU	438602	1980	17072	CCC NOPWASD
PONTIAC PHEONIX	163256	1980	17631	CCC NOPWASD

memorandum

DATE: July 11, 1985

REPLY TO
ATTN OF: DIR, Frank B. KimballAPPENDIX 1SUBJECT: Draft Audit Report on Canal Cities Water and Sewerage Project
(263-0048)

TO: RIG/A, Harold R. Gill

JUL 15 RECD

Attached is the Mission's response to the subject Audit Report

clrs:

OD/UAD:FZobrist AD/DR:GRvanRaalte (Draft) OD/FM/FA:HJamshed DD:AHandly

- 1 -

USAID/CAIRO RESPONSE TO AUDIT REPORT
CANAL CITIES WATER AND SEWERAGE PROJECT

USAID/Cairo has reviewed the Draft Audit Report on the Canal Cities Water and Sewerage Project. The following Mission views and comments on this draft report are first directed at the overall presentation of the report and then directed at the report's specific findings and recommendations.

A. Overall Presentation of Audit Report

1) The report states that the audit's objectives were to determine if the project purpose was being achieved and to determine compliance with Agency regulations. Yet there is very little, if any, discussion of whether the project's purpose of providing urgently needed improvements to water and wastewater systems in the Canal Cities is being achieved. The report should provide a thorough evaluation of the project's progress in developing Master Plans and facility designs, procuring equipment and implementing the construction projects. 1/

2) The tone of the report is overly negative and ignores project accomplishments. For example, the section on low water and wastewater tariffs does not accurately reflect Mission and GOE efforts to date to increase tariffs and, in light of these efforts, the use of the word chaotic to describe the tariff situation is unjustified. Other examples of this negative reporting style are cited in our comments on specific findings and recommendations. 2/

3) This Audit Report is aimed at ensuring compliance of specific project activities with AID and Mission policies, procedures and regulations without evaluating the possible need to revise policies, procedures and regulations that have caused project implementation problems. For example, the report clearly shows that the GOE implementing agencies have problems with the inventory of equipment and materials. Rather than just focusing on the inventory problems of two specific organizations, we feel that the report should also examine, and possibly make recommendations on, the broader issue of whether equipment in large construction contracts should be purchased by the owner or the construction contractor.

1/ RIG/A/C added a statement on project progress to the Executive Summary on page 1 of this report. It should be noted that audit resources for the detailed review were focused on the problem areas noted during the audit survey. In accordance with prescribed audit standards, we did not make, nor did we intend to make, a thorough evaluation of aspects of the project when problems were not evident.

2/ Subsequent to receipt of USAID/Egypt comments, the report was revised to reflect progress on tariffs. Reporting of non-competitive procurement and the lump sum contract award were revised as appropriate.

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B. Comments on Findings and Recommendations

1) Accounting for AID-Financed Equipment Should Be Improved

Since this audit was completed over a year ago we would like to update the project's inventory situation:

The project's construction supervision consultant, Canal Cities Consultants (CCC), has inventoried all Suez Canal Authority (SCA) and National Organization for Potable Water and Sanitary Drainage (NOPWASD) equipment that has arrived over the past year. CCC is not allowed to clear equipment through customs. However, they do jointly inventory equipment with the SCA once unopened boxes arrive in SCA's warehouse in Port Said. Missing or damaged equipment is noted and claims are initiated. NOPWASD equipment is jointly inventoried by CCC and Harbert - Jones, the construction contractor, as soon as it is delivered to Harbert-Jones storeyards. Detailed inventory reports are prepared and CCC assists NOPWASD in making claims against suppliers. Over the past four months NOPWASD has initiated claims against four suppliers and three of these claims are near resolution.

Despite these improvements in the inventory of project's equipment USAID does agree that NOPWASD's and, to a lesser extent, SCA's, inventory procedures need to be improved. We will continue to encourage them to upgrade these procedures and to consider USAID assistance in inventory control under the existing Canal Cities project or the proposed Canal Cities Phase II project.

Finally we would like to comment on statements regarding the measurement of pipe:

- Paragraph 2 of page 7 contains a statement that pipe length was not standard and that individual pieces varied by as much as one meter. This is quite normal. Industry standards set the nominal laying length of ductile iron pipe at either 18 feet (5.5 meters) or 20 feet (6.1 meters). These standards permit a maximum of 20 percent of the total number of pipe specified in an order to be furnished by as much as 24 inches (610 mm) shorter than the nominal laying length, and an additional 10 percent may be furnished by as much as 6 inches (152 mm) shorter than the nominal laying length.
- The report states that SCA would have to measure each piece of pipe received to determine if they received the correct amount. It is not common practice for the inspector to measure the actual length of each section of pipe received by the owner; however, an inspector would be expected to measure the running length of installed pipe including joints, fittings, etc. Obviously, the installed length of bell and spigot pipe will be slightly less

than the sum of the lengths of the individual pipe sections due to the fact that a portion of the plain-end extends into the bell section (for 16-inch or 400 mm diameter pipe this would result in a loss of approximately 3 1/2 inches or 89 mm per pipe section). Pipe purchasers always order an additional amount of pipe to take into account variance in length, damages during handling and installation, the need to cut pipe to accommodate valves and fittings etc. and magnitude and nature of the job. 3/

Our comments on specific recommendations are as follows:

a) The SCA and NOPWASD Account For All AID-Financed Equipment and Materials

New equipment that will not be incorporated into the construction of new facilities (such as tools, spare parts etc.) should not be difficult to inventory. However it is impossible at this stage of the project to make an exact inventory of large quantities of equipment and materials that have already been installed at construction sites. Construction contractors do not keep accounts of exact amounts of pipe and fittings installed. We do know that NOPWASD and the SCA ordered an adequate amount of materials and equipment to complete the project taking into account a need for extra equipment to cover a normal amount of damage and unforeseen design changes. Accounting for equipment incorporated into construction will, most likely, have to await completion of construction when USAID can ascertain that water and wastewater systems are properly functioning (and therefore the proper amount of equipment was installed) and that there is a reasonable amount of "extra" equipment.

b) Ensure That All Claims Against Suppliers Are Resolved

USAID shares the Audit Report's concern that claims against suppliers remain unresolved and will continue to press SCA and NOPWASD to resolve these claims.

c) NOPWASD Develop Plans to Use or Transfer AID-Financed Equipment Valued at \$166,000 to Another USAID Project

The equipment referred to consists of \$122,000.00 of TV inspection equipment for sewer lines and three pick-up trucks valued at \$44,000.00.

COC and NOPWASD plan to use the TV inspection equipment in their upcoming training program for wastewater collection system personnel in the three Canal Cities. We will further evaluate the use of this equipment upon completion of the training program.

3/ Management response in this section does not address the issue whether \$75 million of AID-financed equipment and materials were actually received and accounted for.

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The three pick-up trucks are 8-cylinder vehicles. These trucks were purchased before the GOE's ban on the use of 8-cylinder vehicles for Government use due to high operation costs. It may be difficult to transfer these vehicles to another AID-financed project since most GOE agencies will not accept 8-cylinder vehicles. We will continue to press NOPWASD and the Governorates to develop a plan for the use of these vehicles before any new project vehicles are financed by AID.

2) Water and Sewerage Tariffs Were Too Low

The tariff situation has changed considerably since the audit was performed. An update of this situation follows:

Since the inception of the water and wastewater program, USAID has recognized that water and wastewater tariffs in Egypt are too low. All of USAID's urban water and wastewater projects contain covenants calling for increases in tariffs. In 1983 USAID recognized that covenants in project agreements were not an effective way of gaining GOE implementation of increased tariffs and other reforms in the sector and initiated a direct water and wastewater policy dialogue with the GOE to press for reforms. In January 1984 AID and the GOE signed a Memorandum of Understanding (MOU) in which the GOE and the United States jointly agreed to the need for tariff increases adequate to cover the cost of water and wastewater operations, maintenance, debt service and routine improvements. The GOE also agreed to increases in the size of operations, maintenance and investment budgets to fund the sector. The signing of the MOU was followed by two Annual Reviews of AID-funded water and wastewater projects attended by both USAID and GOE representatives. At the second Annual Review, held in February 1985, the GOE agreed to benchmarks for implementation of reforms in the water and wastewater sector. The tariff benchmark for 1985 was the National Assembly's approval and implementation of rates that would cover 35% and 10% of water and wastewater O&M costs respectively. The GOE also agreed to increase tariffs annually to meet a goal of covering 100% of water supply O&M costs and 50% of wastewater system O&M costs by the year 2000.

The GOE approved a National Tariff Plan in June 1985. This plan calls for the implementation of residential water tariffs of 30 millimes/m³ for the first 30m³ of water and 50 millimes/m³ for all quantities of water greater than 30 m³. The plan also calls for the implementation of a 10% surcharge on water bills to cover a portion of wastewater system O&M costs.

On July 1, 1985 the Suez Canal Authority raised its water tariffs for residential use to the level set in the National Tariff Plan. The SCA has also informed USAID that it will impose a 10% surcharge on

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water bills and attempt to raise water tariffs each year with the goal of covering 100% of water system costs by 1990. Water tariffs for other categories of water use were significantly increased by the SCA earlier this year. USAID will continue to monitor tariff increases in the Canal Cities at both the project and policy level.

Because water and wastewater tariff issues have been addressed at a policy, rather than a project specific level since 1983 USAID feels that it is inappropriate to include a review and recommendation on tariffs in the Canal Cities Audit Report. If RIG/A does not accept our view that discussion of tariffs should be removed from the Audit Report, we request that the audit recommendation be closed based on USAID's and the GOE's success in implementing tariff reforms in the Canal Cities.

3) Project Vehicles Were Disposed of Without USAID/Egypt Approval

USAID has verified that ten project vehicles were transferred to the GOE's Customs Department without USAID approval. We plan to follow the audit recommendation that USAID determine the exact disposition of these vehicles and to attempt to recover proceeds if the Customs Department has sold the vehicles.

C. Other Pertinent Matters

1) Non-Competitive Procurement Awarded Without a Waiver

The Mission notes that the Auditors take issue with the add-on of 20% of pipe, at a value of \$5.4 million, to a Host Country Contract. The Mission's only comment on this situation is that the legality of proceeding with AID funding of the add-on was reviewed by AID legal staff and appropriate management officials; the decision to proceed was fully cleared at that time. No purpose seems served by retroactively debating the issue.

2) Lump Sum Payment Approved Under a Cost Plus Fixed Fee Contract

USAID feels that the negative tone of this section, which implies that OCC is "cheating" the GOE, is unwarranted unless complete details were collected on Canal Cities Consultants contract negotiations with the SCA. This negative tone could be damaging to future contract negotiations between the GOE and AID-financed contractors.

When lump sum contracts are negotiated, the Contracting Agency and the contractor often concede to higher costs in one budget category in order to reduce costs in another budget category. The final aim of the negotiation process is to arrive at a lump sum price that both

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parties agree is adequate to accomplish the work. Since SCA's contract with CCC is a Host Country Contract, we do not have a record of negotiation. Without knowledge of what transpired at negotiations we feel the Audit Report's treatment of this issue should be more even-handed. The GOE has a preference for lump sum contracts for design and construction supervision. We do not feel that this contracting mode should be hastily discarded without a thorough evaluation of both the advantages and disadvantages. We recommend that the Auditors either perform a complete analysis of contracting approaches or delete this section of the report.

We would also like to point out that:

- The statement (p. 27) that CCC's lump sum work order included inflated freight costs of \$70,900.00 is erroneous. CCC's cost reimbursement contract with NOPWASD also has an LE allowance for air freight and sea freight based on LE 3.2 per pound for air freight and LE 1.0 for sea freight. At a conversion rate of LE 83 = \$1.00 the cost per pound for air freight is nearly the same in both of CCC contracts and the cost per pound for sea freight is higher in CCC's cost reimbursable contract.
- The contractor's air freight rates should not be compared with those of the U.S. Embassy in Cairo. Rates obtained from TWA by the Embassy are extremely low because we are one of their best freight customers. Contractors with small, sporadic shipments are charged a much higher rate.
- The title of this section is confusing. Lump sum payments are now being paid under a lump sum contract. We suggest a new title: Use of Lump Sum Contracts for Construction Supervision Contracts

3) Construction of the \$11.7 Million Southwest Transmission Main Pipeline Did Not Contribute to Project Purpose

USAID does not agree that the construction of the Southwest Transmission Main does not contribute to the project purpose.

The Canal Cities Water and Sewerage Project is an outgrowth of AID-financed Water and Wastewater Master Plans that were developed for the Canal Cities in 1977/78. All Master Plans for the three cities recommended phased construction programs to meet the cities' water and wastewater needs up to the year 2000. The Suez Water Facilities Master Plans makes recommendations for projects that should be implemented immediately to meet existing needs (Phase I) and projects that should be implemented to meet water supply needs in the year 1990 and 2000 (Phase II). Section 10.5, Priorities and

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Implementation, of the Water Facilities Master Plan discusses how priority determinations were made and lists the construction of the Southwest Transmission Main as one of the most critical Phase I projects.

ID#0191D

LIST OF RECOMMENDATIONS

	<u>Page</u>
<u>Recommendation No. 1</u>	3
We recommend that USAID/Egypt:	
a. have the Suez Canal Authority and the National Organization for Potable Water & Sanitary Drainage account for all AID-financed equipment and materials;	
b. ensure that all claims against suppliers are resolved; and	
c. have the National Organization for Potable Water and Sanitary Drainage develop plans to use or transfer AID-financed equipment valued at \$166,000 to another USAID project.	
<u>Recommendation No. 2</u>	7
We recommend that USAID/Egypt arrange for the Government of Egypt to implement water and sewerage service tariff reforms.	
<u>Recommendation No. 3</u>	9
We recommend that USAID/Egypt determine the ultimate disposition of the ten vehicles given to the Government of Egypt's Customs Department, and if funds have been generated, recover these funds from Customs.	

APPENDIX 3

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