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AUDIT OF
FEEDER ROADS MAINTENANCE AND
IMPROVEMENT PROJECT IN BANGLADESH
PROJECT NO. 338-0056

AUDIT REPORT NO. 5-388-87-1
December 23, 1986

memorandum

DATE: December 23, 1986
REPLY TO: *James W. Widdows*
ATTN OF: James W. Widdows, RIG/A/Singapore, Acting
SUBJECT: Audit of the Feeder Roads Maintenance and Improvement Project
in Bangladesh (Project No. 338-0056)
TO: Dr. John Westley, Director, USAID/Bangladesh

This report presents the results of audit of the Feeder Roads Maintenance and Improvement Project in Bangladesh. The audit was a program results audit with the specific objectives to evaluate (1) program accomplishments against the project objective and goal, (2) the Government of Bangladesh compliance with the terms and conditions of the Project Agreement, and (3) the adequacy of USAID/Bangladesh management of the project.

After five years and \$7.8 million in AID expenditures, little measurable accomplishments were made toward the project objective to institutionalize an effective program of routine annual maintenance and development of roads or toward the project goal of increased agricultural production. The Government of Bangladesh did not comply with critical elements of the Project Agreement. USAID/Bangladesh did not effectively manage project implementation to ensure compliance with the terms and conditions of the Project Agreement and the proper use of AID funds.

The audit disclosed five problem areas. First, several important components which were essential to the success of the project were not achieved. A second was the Government of Bangladesh did not make its required contributions to the project. Two others were questionable payments to the technical assistance contractor and to the Government of Bangladesh. The fifth problem was delays in the procurement of equipment.

Despite the limited success of the project, USAID/Bangladesh and the Government of Bangladesh amended the grant agreement on August 31, 1986. This amendment extended the project for four more years with an expected additional AID obligation of \$12.5 million.

We are making five recommendations requiring 22 separate actions by USAID/Bangladesh. These actions should resolve problems encountered in the project implementation and preclude similar problems occurring during the project extension. The recommendations include (1) limiting additional AID funding until specific actions are taken, (2) establishing periodic reporting requirements on critical elements essential to the effective and efficient implementation of the project, (3) establishing procedures to ensure that the Government of Bangladesh complies with the terms and conditions of the Project Agreement, and (4) recouping questionable payments made to the technical assistance contractor and the Government of Bangladesh.

USAID/Bangladesh's written comments were considered in finalizing this report. The comments generally concurred with the intent of the audit recommendations. However, the comments did not indicate that there were any plans to implement some of the recommended actions. The status of the 22 actions recommended is: 9 remain open because the comments did not indicate appropriate action to be taken, 11 are considered resolved and will be closed upon completion of the planned corrective actions, and 2 are considered closed upon issuance of this report. The comments are discussed in appropriate sections of the report, and are included as an appendix to the report.

Please advise me within 30 days of the actions taken or planned to implement the recommendations that were not closed upon issuance of this report. We appreciate the cooperation and courtesy extended our staff during the audit.

EXECUTIVE SUMMARY

The purpose of the Feeder Roads Maintenance and Improvement Project (formerly Zilla Road Maintenance and Improvement Project) in Bangladesh was to improve farm-to-market roads by institutionalizing an effective program of routine annual maintenance and development of roads under the jurisdiction of three districts in Bangladesh. Major emphasis was to be placed on developing an annual road maintenance program. The goal of the project was to increase agricultural production -- particularly food grains. The project was approved on August 20, 1981 and had an anticipated completion date of August 31, 1986. The total estimated cost of the project was \$13.8 million, with AID and the Government of Bangladesh providing \$9.2 million and \$4.6 million, respectively. AID had expenditures of \$7.8 million as of September 30, 1986.

On August 31, 1986, USAID/Bangladesh and the Government of Bangladesh signed an amendment to the grant agreement which extended the project completion date to June 30, 1990. The amendment also reassigned responsibilities within the Government of Bangladesh for project implementation. AID planned to obligate an additional \$12.5 million and the Government of Bangladesh was expected to contribute an additional \$3.1 million.

The Office of the Regional Inspector General for Audit/Singapore made a program results audit of the project activities from inception of the project on August 20, 1981 to September 30, 1986. The audit objectives were to evaluate (1) program accomplishments against the project objective and goal, (2) the Government of Bangladesh compliance with the terms and conditions of the Project Agreement, and (3) the adequacy of USAID/Bangladesh management of the project.

After five years and \$7.8 million in AID expenditures, little measurable accomplishments were made toward the project objective to institutionalize an effective program of routine annual maintenance and development of roads or toward the project goal of increased agricultural production. The Government of Bangladesh did not comply with critical elements of the Project Agreement. USAID/Bangladesh did not effectively manage project implementation to ensure compliance with the terms and conditions of the Project Agreement and the proper use of AID funds.

The audit disclosed five problem areas. First, several important components which were essential to the success of the project were not achieved. A second was the Government of Bangladesh did not make its required contributions to the project. Two others were questionable payments to the

technical assistance contractor and to the Government of Bangladesh. The fifth problem was delays in the procurement of equipment.

The Project Agreement and project design included several important components which were essential to the success of the project. The components included the (1) reorganizing and fully staffing the Government of Bangladesh institutional structure responsible for a road maintenance and improvement program, (2) developing a comprehensive road inventory, (3) performing economic feasibility and impact studies, and (4) performing annual project evaluations. None of these components were achieved under the project. The required criteria for prioritizing road maintenance and improvement activities were also not developed. A basic cause for these deficiencies was that USAID/Bangladesh did not have established policies and effective procedures to ensure that the Government of Bangladesh complied with the project covenants and that other critical components of the project were performed. The failure to accomplish these components resulted in AID spending \$7.8 million with little measurable accomplishments of the project objective or goal. The project objective was to institutionalize an effective program of routine annual maintenance and development of roads. The project goal was to increase agricultural production. This report recommends several specific actions prior to significant funding for the project extension. USAID/Bangladesh, in commenting on the draft report, generally concurred with each of the recommended actions; however, its comments in some cases were not responsive to actions recommended.

The Project Agreement required the Government of Bangladesh to contribute a stipulated amount of local currency. The Agreement also required, in accordance with the Foreign Assistance Act, that the contribution had to be at least 25 percent of total project costs. The Government did not provide the required amount of local currency -- only 16 percent of total project costs was provided. The shortfall in the Government's contribution was about \$1.1 million. The shortfall resulted in little road maintenance work performed and precluded any chance of establishing an effective road maintenance program which was the primary focus of the project. USAID/Bangladesh did not know the amount of Government of Bangladesh contributions because it did not have procedures to ensure that the Government provided the required contributions. This report recommends establishing procedures to ensure that the Government provides its required contributions and to resolve the problem of the shortfall. USAID/Bangladesh claimed that the Government's shortfall was less than that identified but agreed to establish the recommended procedures for future use and to resolve the problem of the shortfall.

AID Handbook 11 stipulated that only costs incurred that were allowable (reasonable and allocable) for the required work under host country contracts were reimbursable to the contractor. The claims made by the technical assistance contractor for the project were clearly questionable for at least a seven-month period when there was little productive work required under the project. USAID/Bangladesh payments to the contractor for costs claimed during this period amounted to \$466,500. These payments were made without a USAID/Bangladesh evaluation of the allowability of the labor hours and other technical aspects of costs billed by the contractor. This report recommends an evaluation on allowability of costs claimed and recoup questionable payments made to the contractor. USAID/Bangladesh commented in its response to the draft report that it had already determined the costs were allowable as part of the voucher approval process and did not agree to perform the recommended evaluation.

The construction contracts awarded by the Government of Bangladesh under the project included provisions for assessing penalties against the contractors for work not completed on time. The Project Agreement stipulated that the Government of Bangladesh would be reimbursed by USAID/Bangladesh for payment to the contractors. The penalty provisions were not routinely enforced by the Government of Bangladesh. USAID/Bangladesh payments would probably have been reduced by more than \$100,000 had the penalties been enforced. The Government of Bangladesh was also submitting reimbursement claims to USAID/Bangladesh for payment to construction contractors. These claims included amounts which were retained by the Government for a specific period of time. This practice resulted in USAID/Bangladesh making improper cash advances to the Government, and in unnecessary interest costs to the U.S. Government during the past three years of about \$32,000. The outstanding advances as of September 1986 amounted to about \$110,000. USAID/Bangladesh did not have procedures to ensure that the Government of Bangladesh enforced the penalty provision. Concerning the improper cash advances, USAID/Bangladesh relied on the certification by the technical assistance contractor and did not know that the advances were made or the status of the advances. This report recommends actions for improved internal controls over reimbursement claims submitted for construction activities and to recoup questionable payments made to the Government of Bangladesh. USAID/Bangladesh agreed to implement the actions recommended.

Office of the Inspector General

AUDIT OF
FEEDER ROADS MAINTENANCE AND
IMPROVEMENT PROJECT IN BANGLADESH
PROJECT NO. 338-0056

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PART I - INTRODUCTION

A. Background

The purpose of the Feeder Roads Maintenance and Improvement Project (formerly Zilla Road Maintenance and Improvement Project) in Bangladesh was to improve farm-to-market roads by institutionalizing an effective program of routine annual maintenance and development of roads under the jurisdiction of three districts in Bangladesh: Faridpur, Rangpur and Sylhet. Major emphasis was placed on developing a management capability within each district which would result in implementing an annual road maintenance program. The goal of the project was to increase agricultural production -- particularly foodgrains.

The Government of Bangladesh was responsible for overseeing all aspects of project implementation. The primary responsibility for implementing the road maintenance and construction was to reside with each district. A technical assistance contractor was to develop and train district technical personnel in improved rural roads maintenance and construction practices. USAID/Bangladesh was to monitor project implementation to ensure compliance with the terms and conditions of the Project Agreement and the effective and proper use of AID funds.

The project was approved on August 20, 1981 and was to be completed by December 1, 1984 which was extended to August 31, 1986. The total estimated cost of the project was \$13.8 million, with AID and the Government of Bangladesh providing \$9.2 million and \$4.6 million, respectively. AID had expenditures of \$7.8 million as of September 30, 1986.

On August 31, 1986, USAID/Bangladesh and the Government of Bangladesh signed an amendment to the grant agreement extending the project completion date to June 30, 1990. The amendment also reassigned responsibilities within the Government of Bangladesh for project implementation. AID planned to obligate an additional \$12.5 million and the Government of Bangladesh was to contribute an additional \$3.1 million.

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B. Audit Objectives and Scope

The Office of the Regional Inspector General for Audit/Singapore made a program results audit of the project activities from inception of the project on August 20, 1981 to September 30, 1986. The audit was done during the period June 29, 1986 through September 30, 1986. The audit covered AID expenditures of \$7.8 million.

The objectives of the review were to evaluate (1) program accomplishments against the project objective and goal, (2) the Government of Bangladesh compliance with the terms and conditions of the Project Agreement, and (3) the adequacy of USAID/Bangladesh management of the project.

Audit work included a review of project files and records and interviews with responsible officials of USAID/Bangladesh, the Government of Bangladesh and the technical assistance contractor. In addition, selected roads improved under the project were inspected. The audit was made in accordance with generally accepted government auditing standards.

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PART II - RESULTS OF AUDIT

After five years and \$7.8 million in AID expenditures, little measurable accomplishments were made toward the project objective to institutionalize an effective program of routine annual maintenance and development of roads, or toward the project goal of increased agricultural production. The Government of Bangladesh did not comply with critical elements of the Project Agreement. USAID/Bangladesh did not effectively manage project implementation to ensure compliance with the terms and conditions of the Project Agreement and the proper use of AID funds.

The audit disclosed five specific problem areas. First, several important components which were essential to the success of the project were not achieved. A second was the Government of Bangladesh did not make its required contributions to the project. Two others were questionable payments to the technical assistance contractor and to the Government of Bangladesh. The fifth problem was delays in the procurement of equipment.

We are recommending that USAID/Bangladesh resolve problems encountered in the project implementation, and preclude similar problems occurring in the future. The recommendations include (1) limiting additional AID funding until specific actions are taken, (2) establishing periodic reporting requirements on critical elements essential to the effective and efficient implementation of the project, (3) establishing procedures to ensure that the Government of Bangladesh complies with the terms and conditions of the Project Agreement, and (4) recouping questionable payments made to the technical assistance contractor and the Government of Bangladesh.

A. Findings And Recommendations

1. Little Was Accomplished Under the Project

The Project Agreement and project design included several important components which were essential to the success of the project. The components included (1) reorganizing and fully staffing the Government of Bangladesh institutional structure responsible for a road maintenance and improvement program, (2) developing a comprehensive road inventory, (3) performing economic feasibility and impact studies, and (4) performing annual project evaluations. None of these components were achieved under the project. The required criteria for prioritizing road maintenance and improvement activities were also not developed. A basic cause for these deficiencies was that USAID/Bangladesh did not have established policies and effective procedures to ensure that the Government of Bangladesh complied with the project covenants and that other critical components of the project were performed. The failure to accomplish these components resulted in AID spending \$7.8 million with little measurable accomplishments of the project objective or goal. The project objective was to institutionalize an effective program of routine annual maintenance and development of roads. The project goal was to increase agricultural production.

RECOMMENDATION NO. 1

We recommend that USAID/Bangladesh limit funding to necessary technical assistance until:

- a. the Government of Bangladesh establishes and fully staffs the organizations assigned responsibility for project implementation;
- b. the Government of Bangladesh agrees to provide quarterly reports on the status of staff in the organizations responsible for project implementation;
- c. criteria are developed for the selection and scheduling of road improvement and maintenance activities;
- d. a road inventory which classifies the condition of the roads covered by the project and type of work required is developed and used in the selection and scheduling of road maintenance and improvement activities;
- e. an economic feasibility study is initiated for potential road maintenance and improvement activities to be included under the project;

- f. an economic impact study is initiated for roads already improved under the project;
- g. procedures are developed to ensure that USAID/Bangladesh approves road maintenance and improvement activities based on established criteria for the selection and scheduling of those activities;
- h. procedures are developed for semi-annual review and reporting on the status of meeting the project covenants; and
- i. a specific policy is established that the required project evaluations be made and reported to the Director of USAID/Bangladesh.

Discussion

This section of the report discusses four important components of the project that were essential to the success of the project. The failure to achieve these components resulted in the lack of measurable accomplishments under the project.

Institutional Structure - The Project Agreement required the Government of Bangladesh to establish at the district level organizations which were to be responsible for road maintenance and development in the three districts. The technical assistance contractor was to assist in the development of these organizations. Establishing the maintenance organizations was specifically provided for as a project covenant. Another covenant required the Government of Bangladesh to increase the staffing of the maintenance and development organizations when required for the proper implementation of the project.

In October 1983, the technical assistance contractor developed a proposed organizational structure with increased staffing levels for the maintenance and improvement organizations. This proposal was never approved by the Government of Bangladesh because the Government decided to decentralize all development activities to a level of government below the district. This decentralization eliminated the three district organizations which were the project's institutionalization target.

The technical assistance contractor concluded in its draft project completion report that large parts of its organizational and management studies were rendered completely invalid due to the reorganization and redelegation of responsibilities instituted by the Government of Bangladesh. The contractor also stated in its monthly

progress report for May 1986 that the full picture of the scope and responsibilities of the new organizational structure implemented by the Government had still not been clarified.

USAID/Bangladesh did not examine the impact of the Government's institutional change on project implementation or assess the continued validity of the project objective until the design for the project extension was initiated in November 1985. USAID/Bangladesh merely allowed the project to continue at the expense of time and costs.

In August 1986, the Project Agreement was amended to extend the project for another four years with basically the same objective, i.e., to institutionalize an effective system of annual routine maintenance and improvements of roads. The institution question was the primary issue of the negotiations for the project extension.

Initially, USAID/Bangladesh maintained that the project should be implemented at the district level of the 14 new districts. The new districts were created out of the three old districts covered by the original project. USAID/Bangladesh believed the local governments below the district level were not capable of implementing the project. On the other hand, the Government of Bangladesh wanted the responsibility for project implementation at the level below the district. This resulted in a compromise agreement that in 11 of the 14 new districts, the district organizations to be established would implement both road maintenance and construction activities. In the remaining 3 districts, these district organizations would implement only the road construction program. Responsibilities for road maintenance activities would be assigned to 19 local government entities below the district level.

The persistence on the part of the Government of Bangladesh on this issue casts doubt upon their commitment to institutionalize an effective road maintenance and improvement program at the district level. A top Government of Bangladesh official responsible for road maintenance and construction activities made it clear that the Government would transfer the functions of farm-to-market road maintenance and improvement from the districts to the lower level local governments by the end of the project. He also said there would be no need for the technical expertise at the districts after the project is ended. This position was contrary to the objective of the project -- institutionalization of a program of road maintenance and improvement at the district level.

We believe that the significance of problems experienced in project implementation and the questionable commitment by the Government of Bangladesh to institutionalize an effective road maintenance and improvement program warrants increased management attention to ensure there is timely progress to establish and staff the organizations assigned responsibility for project implementation during the project extension.

Road Inventory - The original project design and the technical assistance contract provided that the technical assistance contractor would develop a road inventory which classified the road networks by priority and the type of maintenance or improvement required. A reliable inventory was considered essential for developing an effective annual road maintenance and improvement program. The project design and the AID regional bureau wanted the initial inventory to be completed by October 1983 and updated annually.

The data for the inventory, which was based on field inspections made in 1983 and 1984, was not compiled until November 1984. The final road inventory was not completed until June 1985.

The inventory was not used in the selection and scheduling of road maintenance and improvement activities under the project. At least 17 of the 21 road networks improved under the project were selected before the inventory work was started and no maintenance activities were scheduled and started under the project after the inventory was completed. In addition to being late, the inventory did not provide the required classification for maintenance or improvement work required on each road segment. Further, the inventory was not complete -- 3 of the 21 roads improved under the project were not included in the inventory.

USAID/Bangladesh officials thought that a current and comprehensive road inventory classifying the road networks by priority and type of maintenance or improvement required had been developed. This assumption was based on their discussions with the technical assistance contractor and Government of Bangladesh officials.

The importance of a comprehensive road inventory for the development of an effective road maintenance and improvement program was emphasized in numerous reports and other documents we reviewed. For example:

- The technical assistance contractor's progress report for December 1984 stated that a comprehensive road inventory updated periodically is the basic foundation for selecting road maintenance and improvement activities based on technical considerations.

- The design approved by USAID/Bangladesh in May 1986 for the project extension stated that a road inventory was necessary for the development of a road maintenance program.
- A report issued in June 1986 by a contractor for a project administered by the Asian Development Bank stated that details of various features of individual road sections including their conditions constitute the essential basis for the development of a detailed road maintenance program.

In our opinion, a reliable road inventory should be developed prior to AID funding of road maintenance and improvement activities. Without the inventory, USAID/Bangladesh cannot ensure that the roads developed and maintained under the project will result in the most cost effective and beneficial use of AID funds.

Economic Study - The Project Agreement required that economic impact assessments be performed to monitor the specific economic benefits achieved under the project. The project design wanted these assessments performed throughout project implementation. These assessments were also to provide data for evaluating the economic feasibility of the project. The project design stated that the assessments were considered crucial to the review and refinement of selection criteria for roads to be maintained or improved. The assessments were also considered essential for quantitative assessment of benefits achieved under the project.

There were serious delays in performing the assessments. The contract to perform a baseline study was not awarded until July 1985. This was four years after the initially planned start date for the study. A draft report on the study was submitted to the Government of Bangladesh in July 1986. The delay was due mainly to disagreement between the Government of Bangladesh and USAID/Bangladesh in the selection of the contractor to do the work. The delay precluded the study from being used in the selection of roads to be maintained or improved under the project. Therefore, there was no basis to determine that the roads selected would produce the most economic benefits to the Government and people of Bangladesh.

Also, the scope of the study was substantially reduced to include only the collection of baseline data on road links already selected for improvement under the project. As a result of the reduced scope, the study did not assess the economic benefits achieved under the project.

The design for the project extension did not consider an economic study important for the selection of road improvement and maintenance activities under the project. The design only provided for baseline data to be collected on selected road links already designated for improvement under the project. The design also provided that in two or three years, comparative data would be collected and analyzed. This analysis would provide USAID/Bangladesh valuable information about the social and economic impact of road improvement and maintenance activities in Bangladesh.

Two or three more years is too long to wait to determine if this project is economically feasible. An economic study should be made not only for assessing economic impact of the project but also should be used in the selection of road maintenance and improvement activities to be funded by the project. This would give USAID/Bangladesh some assurance that activities selected would result in the effective use of AID funds and the most economic benefits to the Government and people of Bangladesh.

Project Evaluations - The Project Agreement included a covenant that USAID/Bangladesh in conjunction with the Government of Bangladesh would perform evaluations during the project implementation. These evaluations were to (1) evaluate progress toward attainment of the project objectives, (2) identify problem areas or constraints which may inhibit such attainment, (3) assess how the information developed may be used to help overcome such problems, and (4) evaluate the overall development impact of the project.

The AID regional bureau directed that annual evaluations be performed. The bureau determined that the difficulty in bringing about the institutional change at the three districts and the related financial and development problems justified establishing an annual evaluation program under the project. Specific benchmarks were established to form the basis of the evaluations. In November 1982, USAID/Bangladesh also sent a letter to the Government of Bangladesh setting forth the requirement for the annual evaluations.

Concerning the 28 specific benchmarks which the AID regional bureau directed USAID/Bangladesh to evaluate against, little or no progress had been achieved in meeting at least 13 of the benchmarks. This included 6 of 10 benchmarks which were to be achieved by the end of the first year. Exhibit 1 lists the benchmarks that were not met.

None of the required project evaluations were performed. USAID/Bangladesh officials stated that they had attempted an in-house evaluation of this project in April 1985, but due to the shortage of the staff personnel and other priorities, the work was terminated after very little effort.

The evaluations would have highlighted the significance of the failure to accomplish essential components of the project and the need for corrective action.

The amendment to extend the project required that the Government of Bangladesh, in cooperation with the technical assistance contractor, develop and implement a system of data collection and analysis. The results of this effort were to be reported to USAID/Bangladesh on a quarterly basis. The project design also provided that USAID/Bangladesh, in coordination with the Government of Bangladesh and the technical assistance contractor, develop mutually agreed indicators for evaluating the information and measuring the project activities. The design called for a "rapid appraisal" during the first three months of the extension period to evaluate project status and accomplishments. It also called for a series of case studies during the second year of the extension period regarding the progress in institutionalizing an effective maintenance and improvement program. An end of project impact evaluation was also to be conducted.

In our opinion, based on the failure to perform the required annual evaluations during the initial four years of project implementation, USAID/Bangladesh should devote an increased management attention to the adequate and timely implementation of the evaluations provided for in the design for the project extension.

Lack of Measurable Accomplishments - The design approved by USAID/Bangladesh in May 1986 for the project extension recognized that little was accomplished in achieving the objective of the project. The design stipulated that the four year extension period would include working with the Government of Bangladesh in generating information (manpower, equipment, material and financial requirements) for the appropriate structure for the organizations responsible for maintaining and improving the roads under the project. This was precisely the same objective and primary scope of the original project.

Concerning the specific area of road maintenance, there was little accomplished. For example, USAID/Bangladesh and Government of Bangladesh records showed that only about \$180,000 was spent on approved road maintenance activities compared to \$1.5 million intended under the project design. In July 1985 - a month after the Government of Bangladesh considered the project ended - the technical assistance contractor reported that there had been little effort devoted to the creation of an effective road maintenance program.

There was also little measurable accomplishments to develop an effective road improvement program. The project did enhance the road networks in the districts by developing about 70 miles of roads and constructing numerous bridges and culverts. However, the roads improved under the project were selected without the support of any analysis to show that they would result in economic benefits to the Government and people of Bangladesh. The economic benefits produced by the improved road networks could not be determined because data essential to make an evaluation was never developed under the project as required by the Project Agreement. There was also little basis to ensure that the most cost effective and prudent road improvement activities were included under the project. As of September 30, 1986, AID and the Government of Bangladesh expenditures for road improvement activities under the project were about \$2.7 million and \$1.0 million, respectively.

The economic benefits of at least some of the roads improved under the project were questionable. An example was the 19 miles of improved road segments the audit staff physically inspected. The audit staff was accompanied during the inspection by officials from the Government of Bangladesh, USAID/Bangladesh and the technical assistance contractor. These roads segments were separated by a 2.4 mile segment of badly deteriorated surface. The deteriorated segment of road was practically unusable to vehicles. Our four-wheel jeep could not safely proceed at a speed in excess of five miles per hour. This may have contributed to the fact that there was not much vehicle usage in the entire length of road excluding the vehicles used by the auditors and project officials. During our two-hour inspection trip, we saw only two oil trucks and several ox carts and bicycles. AID spent approximately \$1.1 million -- or about 39 percent of total AID expenditures for road improvement activities under the project -- to improve these 19 mile segments of roads. (See Exhibit 2 for photographs of the improved and deteriorated surfaces.)

Another example of questionable economic benefits was a 2.7 mile segment of road which was improved to a bituminous pavement. The work was started in July 1983 and completed in August 1984. The contractor who performed a socio-economic study about a year after the work was completed on this road reported that this paved segment of road is motorable all the year round, but is primarily utilized by non-power vehicles. The contractor also reported that the remaining 7 miles of this road network was earth and was not serviceable at anytime of the year due to the presence of numerous road gaps not yet bridged. AID spent approximately \$135,000 to improve this 2.7 miles of road.

Some road segments improved possibly should have been maintained instead of improved -- especially since the major emphasis of the project was the implementation of an annual road maintenance program. For example, the road inventory prepared by the technical assistance contractor indicated that some road segments improved under the project were in a condition that would have warranted maintenance work -- not improvement. There was also no evidence that the relative costs to maintain or improve a road segment was considered. This should have been an important factor because USAID/Bangladesh estimated that the average cost to maintain and improve a one-mile segment of road was \$1,250 and \$52,000, respectively.

A basic problem in the selection process of roads to be improved and maintained was the lack of established criteria to prioritize the roads in terms of effective use of AID funds and the most benefits to the Government and people of Bangladesh. The technical assistance contractor reported that to obtain the greatest benefits from available funds, criteria must be developed for selecting and programming road maintenance and improvement activities. The criteria should consider such things as budget limits, identified urgency of needs, route continuity, cost-benefit analysis to maintain or improve the road, and the ultimate social and economic benefits of road use. The lack of criteria problem was compounded because the decision on which roads were included under the project was unilaterally made by the Government of Bangladesh.

The technical assistance contractor officials said they worked for the Government of Bangladesh and were not in a position to question the Government's selection of road segments to be included under the project. USAID/Bangladesh said they did not evaluate the selection in terms of whether the roads selected for improvement were the most cost effective and beneficial roads to develop under the project or whether maintenance should have been performed instead of improvement.

The accomplishments toward the project goal of increased agricultural production could not be measured because economic data essential to make an evaluation was never developed under the project as required under the Project Agreement.

Conclusion

After five years and \$7.8 million in AID expenditures, little measurable accomplishments were made against the project objective and goal. There was also little basis to ensure that the roads improved and maintained resulted in the most

effective and beneficial use of AID funds. A basic problem was that USAID/Bangladesh did not have adequate policies and procedures to ensure that the Government of Bangladesh complied with the project covenants and that other essential components required under the project were performed. Unless USAID/Bangladesh improves its management of this project, AID funds will continue to be spent with little assurance that the project objective and goal will be accomplished.

Management Comments

USAID/Bangladesh thoroughly acknowledged implementation problems discussed in the report. However, it took issue with the statement that after five years and \$7.8 million in AID expenditures, little measurable accomplishments were made toward the project objective to institutionalize an effective program of routine annual maintenance and development of roads. USAID/Bangladesh claimed that the statement was unsubstantiated.

USAID/Bangladesh also stated that the audit was conducted in the project officer's absence. USAID/Bangladesh commented that had the audit been conducted while the project officer was present, many of the inaccuracies and misunderstandings contained in the report could have been avoided.

Office of Inspector General Comments

USAID/Bangladesh comments did not provide any evidence or direct reference that there were measurable accomplishments toward the project objective to institutionalize an effective program of routine annual maintenance and development of roads. The report supports that there were little measurable accomplishments toward the objective or toward the project goal of increased agricultural production.

We do not understand the USAID/Bangladesh comment that the audit was conducted in the project officer's absence. This comment is not correct. The audit work was initiated when the project officer was on leave, but, for that very reason, the audit staff went back to Bangladesh at a later date to complete the audit when the project officer was present. In addition, the initial draft report which included each of the findings in this report was provided to the project officer for the purpose of confirming the facts presented in the report. The audit staff also fully discussed each finding with the project officer. The one case of a misunderstanding cited by USAID/Bangladesh in its comments was corrected in finalizing this report.

Management Comments

USAID/Bangladesh agreed to limit funding to necessary technical assistance until (1) the Government of Bangladesh establishes and fully staffs the organizations assigned responsibility for project implementation, (2) the Project Agreement is revised to require that the technical assistance contractor report in its regular progress reports on the status of staff in the responsible organizations and (3) a mission order is issued requiring reviews and reporting on the status of planned evaluations and the Government of Bangladesh adherence to the project covenants.

Office of Inspector General Comments

USAID/Bangladesh actions initiated or planned are responsive to parts (a), (b), (h) and (i) of the recommendation. These parts are considered resolved and will be closed upon completion of the corrective actions.

Management Comments

USAID/Bangladesh concurred with the recommended action to develop criteria for the selection and scheduling of road improvement and maintenance activities. USAID/Bangladesh further commented, however, that two systems of criteria had been established in 1978 and 1982, respectively.

Office of Inspector General Comments

USAID/Bangladesh comments were not responsive to the recommended action. Therefore, part (c) of the recommendation remains open. Although USAID/Bangladesh concurred with this part of the recommendation to develop criteria for the selection and scheduling of road activities, it did not indicate what corrective action was planned. USAID/Bangladesh instead implied that the required criteria already existed. These criteria were not identified to the audit staff during the audit. USAID/Bangladesh apparently did not consider the criteria important because its comments noted that the road segments improved were only recently assessed to determine if they conformed to the criteria of one of the two systems. USAID/Bangladesh did not comment on whether or not the criteria under one or both of the systems were adequate for the selection and scheduling of road improvement and maintenance activities. Furthermore, the existing criteria referred to in the comments did not include several factors identified in the report that should be considered to obtain the greatest benefits from available funds.

Management Comments

USAID/Bangladesh concurred with the recommended action to develop a comprehensive road inventory and use the inventory in the selection and scheduling of road maintenance and improvement activities. USAID/Bangladesh further commented that the first revision of the road inventory was completed in the spring of 1986. The comments stated that the technical assistance contractor will provide a detailed analysis of the scores given in the inventory and describe how this relates to the development of a composite feeder road maintenance plan.

Office of Inspector General Comments

USAID/Bangladesh comments were not responsive to the recommended action. Therefore, part (d) of the recommendation remains open. USAID/Bangladesh did not indicate that the work to be done by the technical assistance contractor was to include road improvement activities. In addition, USAID/Bangladesh commented that the first revision of the inventory was completed in the spring of 1986. The only inventory identified to the audit staff and discussed with responsible project officials was the initial inventory completed in June 1985. This initial inventory was also referred to in a cable sent on October 8, 1986 from USAID/Bangladesh to the audit staff on roads that were improved or planned for improvement which had not been inventoried. The cable noted that several roads planned to be improved had not been inventoried but would be during the first few months of the project extension which began August 31, 1986.

Management Comments

USAID/Bangladesh generally concurred with the recommendation that an economic feasibility study be initiated for potential roads to be included under the projects. USAID/Bangladesh agreed to perform the studies on new road segments to be improved prior to any AID investment; but, it did not believe that studies were required for road segments on which improvements had already begun and would be continued under the project extension. USAID/Bangladesh made reference to a phase II of a rural roads study. This study reportedly concluded that an economic evaluation on five roads indicated that the procedures employed in "defining the road network" proved effective as all five roads were considered in terms of economic impact to be excellent candidates for an improvement investment.

Office of Inspector General Comments

USAID/Bangladesh comments were not fully responsive to the recommended action. Therefore, part (e) of the recommendation remains open. We believe that an economic analysis should be undertaken not only on new roads to be included in the project, but also on roads previously improved where sizable investments are planned. The cost of previous improvements on some roads was minimal in relation to the work planned. For example, work done on one road in 1983 cost less than \$6,000. The estimated cost of the planned work is about \$400,000. Concerning the reference to a phase II of a rural roads study, this study was not identified to the audit staff during the audit.

Management Comments

USAID/Bangladesh stated that it concurred with the recommended action to initiate an economic impact study for roads already improved under the project. However, USAID/Bangladesh took issue with the timing of the study. The initial economic baseline study was performed September 1985 to May 1986. USAID/Bangladesh stated that it was standard practice to wait at least two years before comparative data is collected to judge the economic impact of road construction and maintenance activities. On this basis, USAID/Bangladesh plans to collect comparative data in early 1988 and then again in 1990. The USAID/Bangladesh comments emphasized that the analysis of the data collected would be directed toward the impact of road maintenance activities. No mention was made of plans to assess the impact of road improvement activities.

Office of Inspector General Comments

USAID/Bangladesh comments were not responsive to the recommended action. Therefore, part (f) of the recommendation remains open. The recommended action was for economic impact studies on roads already "improved" under the project. Many of these activities were completed several years ago. As stated in this report, these impact studies were considered in the project design to be crucial to the review and refinement of selection criteria for roads to be maintained or improved. We do not believe that USAID/Bangladesh should proceed to spend an additional \$12.5 million in AID funds under this project before it determines the economic impact of roads already improved under the project.

Management Comments

USAID/Bangladesh concurred with the recommended action to develop procedures to ensure that it approves road maintenance and improvement activities based on criteria to be developed for the selection and scheduling of those activities. USAID/Bangladesh further explained that the review process in place provided for final approval by USAID/Bangladesh of individual road activities.

Office of Inspector General Comments

USAID/Bangladesh comments did not indicate that corrective action was planned and, therefore, were not responsive to the recommended action. As a result, part (g) of the recommendation remains open. We do not question the existence of the review process which provides USAID/Bangladesh the right to approve or refuse AID funding of activities proposed by the Government of Bangladesh. A primary point of our concern, however, is that the existing review process is not effective to ensure that the approval of road activities is based on appropriate criteria for selecting and scheduling road activities under the project. Accordingly, there is no reasonable assurance that the roads selected are the most cost effective and economically sound. We believe that all road improvement and maintenance activities approved by USAID should be based on the specific criteria to be developed.

2. The Government of Bangladesh Did Not Make Its Required Contributions

The Project Agreement required the Government of Bangladesh to contribute a stipulated amount of local currency. The Agreement also required, in accordance with the Foreign Assistance Act, that the contribution had to be at least 25 percent of total project costs. The Government did not provide the required amount of local currency -- only 16 percent of total project costs was provided. The shortfall in the Government's contribution was about \$1.1 million. The shortfall resulted in little road maintenance work performed and precluded any chance of establishing an effective road maintenance program which was the primary focus of the project. USAID/Bangladesh did not know the amount of Government of Bangladesh contributions because it did not have procedures to ensure that the Government provided the required contributions.

Recommendation No. 2

We recommend that USAID/Bangladesh:

- a. take actions to ensure the Government of Bangladesh provides the amount of the shortfall in its contributions to the project;
- b. establish procedures to ensure that the Government of Bangladesh provides its required contributions; and
- c. require that the Government of Bangladesh provide quarterly reports on the status of the Government's contributions.

Discussion

The Project Agreement required the Government of Bangladesh to contribute a stipulated amount in local currency. The Agreement also required, in accordance with Section 110 of the Foreign Assistance Act, that in no case should the Government of Bangladesh contributions be less than 25 percent of total project costs.

The Government of Bangladesh did not provide the required amount of local currency. The Government provided only about \$1.5 million of the total project costs of \$9.3 million -- or about 16 percent of the total project costs. The shortfall in meeting the minimum 25 percent required by the Project Agreement and Foreign Assistance Act amounted to about \$1.1 million.

The shortfall was attributed to a devaluation of the local currency and the failure by the Government of Bangladesh to provide the amount of local currency stipulated in the Project Agreement. The exchange rate during project implementation went from 15 Taka at inception of the project to 30 Taka for \$1. To accommodate for the devaluation and maintain the required percentage of total project costs, either AID's level of funding should have been reduced or the Government of Bangladesh contribution of local currency increased. Neither of these action was taken.

The Project Agreement required the Government to contribute 69 million Taka in local currency. Based on the level of AID expenditures, the Government should have contributed about 58.9 million Taka as of September 30, 1986. However, the Government only contributed about 33.4 million Taka. The shortfall of 25.5 million Taka was at the time of our audit equivalent to about \$850,000. (See Exhibit 3 for a breakdown of the shortfall by cost categories.)

The local currency shortfall was primarily in the funding of road maintenance work under the project. Based on the level of AID funding to the project, the Government of Bangladesh should have contributed about 19.7 million Taka to the maintenance fund as of September 30, 1986. However, the Government contributed only about 1.6 million Taka -- or about 8 percent of the required contribution. Using the exchange rate as of September 30, 1986, the shortfall of 18.1 million Taka was equivalent to about \$600,000.

In terms of dollar equivalent of the Government's actual contribution for maintenance work and what was intended under the project design, the Government contributed only \$54,000 of the \$1.5 million originally intended. The difference between these amounts (\$1.46 million) and the \$600,000 shortfall noted above was attributed to the devaluation of the local currency. However, this larger amount was not considered for report purposes as a shortfall because, although the project design intended to have the Government contribute 33 percent of total project costs, the Project Agreement required that the contribution not be less than 25 percent. Therefore, the overall shortfall of the Government's contribution was calculated on the 25 percent requirement.

The shortfall of Government of Bangladesh contributions to the maintenance fund resulted in little maintenance work performed. The monthly progress reports prepared by the technical assistance contractor on approved maintenance activities repeatedly discussed the problems of cancellations and delays in maintenance work due to the shortage of Government of Bangladesh contributions. For example, the

progress report for March 1985 identified that maintenance work was cancelled or being delayed in at least 9 of the 17 roads included in the maintenance program at that time.

The absence of a routine maintenance program resulted and will continue to result in substantial waste of AID and Government of Bangladesh funds because of the excessive deterioration of roads. The technical assistance contractor reported that if proper road maintenance is not practiced, road distress will be accelerated which, in turn, will lead to premature need for rehabilitation of the road.

In September 1984 USAID/Bangladesh allowed AID funds allocated for the road improvement component of the project to be used for routine road maintenance to encourage progress toward obtaining its original objective to implement an annual maintenance program. This would not have been necessary had the Government of Bangladesh provided its required contributions to the road maintenance program. Furthermore, the Project Agreement stated that the financing of road maintenance work under the project would be the "sole responsibility" of the Government of Bangladesh. As of September 30, 1986, AID expenditures for maintenance work amounted to \$126,945.

The Government of Bangladesh provided USAID/Bangladesh documentation in September 1986 that showed the Government did fund additional road maintenance and improvement activities under separate programs in each district. These programs, which were required by the Project Agreement and confirmed by Project Implementation Letter Number 6, were to fund only "approved" maintenance activities under the project. However, activities funded under these programs were neither approved nor monitored by USAID/Bangladesh or the technical assistance contractor to ensure that road maintenance work and not road improvement work was actually performed. In fact, Government of Bangladesh records showed that essentially all funds spent under these programs were for road improvement activities which was in direct conflict with the Project Agreement and the basic objective of the project.

The deficiency in the Government of Bangladesh contributions was due to the general lack of monitoring by all responsible parties. The Government of Bangladesh did not monitor the level of its contribution as required by the Project Agreement. The technical assistance contractor did not monitor and report on the Government of Bangladesh contributions as required by the contract. USAID/Bangladesh did not closely monitor the course of project implementation including the quantity of project inputs as intended by the project design.

Government of Bangladesh and USAID/Bangladesh officials stated that they simply failed to monitor the level of Government of Bangladesh contributions in terms of what was specifically required under the Project Agreement. Technical assistance contractor officials said they did not realize it was their responsibility to monitor and report on the level of contributions.

The shortage of the Government of Bangladesh overall contributions -- especially for the road maintenance program -- indicated serious questions concerning its commitment to develop an effective road maintenance program, and whether it had the ability to finance continuation of project activities when AID participation is completed. In fact, it appeared the Government of Bangladesh had little commitment or ability to finance the project activities if AID participation was phased out. The USAID/Bangladesh project officer noted in a memorandum of a meeting with the Government of Bangladesh officials in February 1986 that the Government of Bangladesh considered the project ended as of June 30, 1985. The memorandum also noted that the Government of Bangladesh did not provide funding for the project in its Fiscal year 1986 budget (July 1, 1985 through June 30, 1986), and that this lack of funding resulted in unfinished road improvement activities.

The design for the project extension recognized the constraints on the Government of Bangladesh ability to contribute funds to the project. Therefore, USAID/Bangladesh reduced the required level of the Government's contribution to 20 percent. In an attempt to ensure that the Government does provide its required contributions, the amendment for the extension provided that AID funds would not be disbursed for each year's road maintenance and improvement activities until the Government of Bangladesh provided evidence that it has budgeted and will disburse the amounts required for these activities. Neither the design nor the amendment stipulated what type of evidence is required to show that the Government has budgeted and more importantly will disburse the funds.

We concluded that the problems associated with the shortage of Government of Bangladesh contributions to the project warrants immediate action by USAID/Bangladesh to ensure that the required contributions are made in accordance with the Project Agreement and the Foreign Assistance Act.

Management Comments

USAID/Bangladesh agreed to the substance of the three parts of the recommendation. However, it suggested that parts (a) and (b) be modified. USAID/Bangladesh also claimed that the amount of Government of Bangladesh contributions was more

than the amount in the audit report. Most of the increased amount was for road maintenance activities.

USAID/Bangladesh identified that the Government's contribution "to date" was Taka 58 million which was still short of the Taka 69 million stipulated in the original Project Agreement. This shortfall in local currency was equivalent to about \$370,000. USAID/Bangladesh stated that a schedule of annual contributions to be made by the Government will be developed. The schedule will incorporate the amount of the shortfall with the level of contributions already stipulated in the Agreement for the remaining four years of the project. USAID/Bangladesh believes that as long as the Government of Bangladesh contributions equal the total amount of local currency stipulated in the Agreement, the Government will be in compliance with the Agreement.

Office of Inspection General Comments

The modifications to parts (a) and (b) suggested by USAID/Bangladesh were incorporated in this report. USAID/Bangladesh actions planned are responsive on parts (b) and (c) of the recommendation. These parts are considered resolved and will be closed upon completion of the planned actions.

Part (a) will remain open until several actions are completed. One action is for USAID/Bangladesh to provide evidence to support the increased amounts of contributions and that the additional contributions were spent for approved activities -- especially maintenance activities. As stated in this report, documents provided by the Government of Bangladesh to USAID/Bangladesh in September 1986 showed that essentially all the additional funds reported in these documents were for road improvement activities. USAID/Bangladesh should also develop a revised schedule of Government of Bangladesh contributions because the schedule currently included as part of the Project Agreement does not provide for the amount of the shortfall. This revised schedule should be made part of the Project Agreement. In addition to ensuring that the Government contributes the stipulated amount of local currency, USAID/Bangladesh should also ensure that the Government provides at least 25 percent of the total project costs (excluding the contributions and costs stipulated in the amendment for the project extension) as required by the Project Agreement and the Foreign Assistance Act.

3. Questionable Payments Were Made to the Technical Assistance Contractor

AID Handbook 11 stipulated that only costs incurred that were allowable (reasonable and allocable) for the required work under host country contracts were reimbursable to the contractor. The claims made by the technical assistance contractor for the project were clearly questionable for at least a seven-month period when there was little work under the project. USAID/Bangladesh payments to the contractor for costs claimed during this period amounted to \$466,500. These payments were made without a USAID/Bangladesh assessment of the allowability of the labor hours and other technical aspects of costs billed by the contractor.

Recommendation No. 3

We recommend that USAID/Bangladesh:

- a. perform a technical evaluation on the allowability of the labor hours and other technical aspects of costs billed by the technical assistance contractor; and
- b. take action to recoup questionable costs claimed by the technical assistance contractor.

Discussions

The contract between the Government of Bangladesh and the technical assistance contractor was amended twice to extend the contract from November 30, 1985 to August 31, 1986. The USAID/Bangladesh authorized the first of these amendments for the contractor to procure and arrange for delivery of project equipment and to monitor road improvement activities. The second amendment required the contractor to monitor "scheduled works being carried out" by the Government of Bangladesh and to provide continuity for the proposed follow-up phase of the project. AID Handbook 11 stipulated that only costs incurred that were allowable (reasonable and allocable) to perform the work under host country contracts for authorized project purposes were reimbursable to the contractor. United States statute 31 U.S.C. section 82C prohibits payments for unallowable costs claimed by contractors.

This review did not include a financial audit to determine the allowability of all costs claimed by the contractor, but there were obvious questions concerning at least the \$466,500 of costs claimed by the contractor and paid by USAID/Bangladesh for the seven-month period ended June 30, 1986.

During most of this seven-month period in question, the only work authorized by USAID/Bangladesh was for the contractor to assist the Government of Bangladesh procure and arrange for delivery of 31 equipment items to the districts and to monitor five small road improvement activities. The work required to assist in the procurement and delivery of the equipment did not appear to be a large effort. The 31 items were to be procured under six contracts. As of November 30, 1985, two of the contracts had already been awarded, and the procurement documents had been prepared for two other contracts. Very little was accomplished during the seven-month period on the award of the remaining two contracts. Concerning the delivery of equipment to the districts, only six of the 31 items had been received during the seven-month period and those had not been delivered to the districts as of August 30, 1986. Ten of the remaining 25 equipment items were in transit from the United States, and the contracts for the remaining 15 had not been awarded.

The work required to monitor the five active road improvement activities also did not appear to be a large effort. The actual cost of each activity was between \$19,500 and \$36,200. Furthermore, all five activities should have been completed by July 1985. See Exhibits 4 and 5 for a listing and status of the equipment items and improvement activities during the seven-month period.

Notwithstanding the minimal work required under the contract, the contractor claimed monthly salary costs for between 60 and 64 persons during the first six months of the seven-month period. The number of persons reportedly working under the contract appeared to be excessive considering the little work that was required.

The contractor also reported in his monthly progress report for January 1986 that much of the staff time during this period was for work outside the scope of the contract. For example, the report stated that since November 1985, a good deal of staff effort was expended in the preparation of an amendment to the expired contract between the contractor and the Government of Bangladesh. Thus, the contractor had reported that much of the staff time for at least two months was spent on work beneficial to the contractor's interests and not within the scope of work required under the contract. The contractor claimed costs for this two-month period of \$151,000.

USAID/Bangladesh officials had little direct knowledge on how many people were actually working under the technical assistance contract or what they were doing during the seven-month period ended June 30, 1986. This was because the responsible USAID/Bangladesh officials had not visited the

contractor's district offices or project sites during that period. The project officer's administrative approval of the Contractor's vouchers for work under the contract was based on discussions with the Government of Bangladesh officials.

The contractor had submitted the required monthly progress reports to USAID/Bangladesh through May 1986. However, as of September 30, 1986, no progress reports were submitted for the months of June through August 1986. When we asked the responsible USAID/Bangladesh official why no reports were submitted for this three month period, he stated that there was no progress to report.

The U.S. Defense Contract Audit Agency performed a series of audits during 1985 on the financial systems and procedures of the technical assistance contractor and its major subcontractors. The Agency reported that U.S. Government technical evaluations had not been performed to determine the propriety and the necessity of the labor hours and other technical aspects of costs claimed by the contractor or the subcontractors. The Agency concluded that such an evaluation may result in disapproved costs.

We believe based on the issues discussed in this section that there is a need for a technical evaluation on the allowability of labor hours and other technical aspects of all costs billed under this project by the technical assistance contractor and its subcontractors. This evaluation should be made to ensure that all costs claimed by the contractor and its subcontractors were reasonable, allocable, and allowable to perform the work authorized by USAID/Bangladesh and required under the contract. At a minimum, there should be an analysis for at least the seven-month period in question in addition to any claims made for July and August 1986 of labor hours and other costs required for the contractor to monitor the road improvement activities and to assist in the procurement and delivery of equipment.

Management Comments

USAID/Bangladesh did not concur with the recommendation. It maintained that the vouchers submitted by the technical assistance contractor were reviewed by USAID/Bangladesh and determined that the costs incurred were allowable in accordance with the terms and conditions of the contract. Therefore, it did not believe it was in the best interest of the U.S. Government to perform a technical evaluation beyond the review performed in approving the vouchers. USAID/Bangladesh stated that the Defense Contract Audit Agency retained the authority to audit costs under the contract. USAID/Bangladesh also stated that substantive work

was performed by the technical assistance contractor during the seven-month period. No analysis or description was given on what work was specifically done.

Office of Inspector General Comments

USAID/Bangladesh did not provide any additional evidence that would resolve the finding or recommendation. This recommendation remains open. Concerning USAID/Bangladesh's position that the vouchers were reviewed and the costs incurred were determined to be allowable, this report states that USAID/Bangladesh officials had little direct knowledge on how many people were actually working under the contract or what they were doing during the seven-month period ended June 30, 1986. This was because the responsible USAID/Bangladesh officials had not visited the contractor's district offices or project sites during that period. USAID/Bangladesh stated that the Defense Contract Audit Agency retained the authority to audit costs under the contract. Our report identifies that the Agency performed a series of audits during 1985 on the financial systems and procedures of the technical assistance contractor and its major subcontractors. The Agency reported that U.S. Government technical evaluations had not been performed to determine the propriety and the necessity of the labor hours and other technical aspects of costs claimed by the contractor or the subcontractors. The Agency concluded that such an evaluation may result in disapproved costs. We believe it is in the best interests of the U.S. Government to perform a technical evaluation as recommended. We also believe that the payments for unallowable costs should be recouped from either the contractor or the Government of Bangladesh.

4. Questionable Payments Were Made to the Government of Bangladesh

The construction contracts awarded by the Government of Bangladesh under the project included provisions for assessing penalties against the contractors for work not completed on time. The Project Agreement stipulated that the Government of Bangladesh would be reimbursed by USAID/Bangladesh for payments to the contractors. The penalty provisions were not routinely enforced by the Government of Bangladesh. USAID/Bangladesh payments could have been reduced by more than \$100,000 had the penalties been enforced. The Government of Bangladesh was also submitting reimbursement claims to USAID/Bangladesh for payment to construction contractors. These claims included amounts which were retained by the Government for a specific period of time. This practice resulted in USAID/Bangladesh making improper cash advances to the Government, and in unnecessary interest costs to the U.S. Government during the past three years of about \$32,000. The outstanding advances as of September 1986 amounted to about \$110,000. USAID/Bangladesh did not have procedures to ensure that the Government of Bangladesh enforced the penalty provision. Concerning the improper cash advances, USAID/Bangladesh relied on the certification by the technical assistance contractor and did not know that the advances were made or the status of the advances.

Recommendation No. 4

We recommend that USAID/Bangladesh:

- a. require the Government of Bangladesh to enforce the penalty clause in the completed construction contracts when there were unjustified delays in completing the work;
- b. recoup from the Government of Bangladesh the amount of penalties assessed;
- c. establish procedures to ensure the Government of Bangladesh routinely enforce the penalty clause in construction contracts;
- d. instruct the Government of Bangladesh and the technical assistance contractor that claims are only to be made for actual payments made by the Government and authorized by USAID/Bangladesh;
- e. review the Government of Bangladesh records to ensure a proper accounting of the advance payments to the Government for construction activities; and

- f. recoup outstanding advances retained by the Government of Bangladesh.

Discussion

In accordance with AID Handbook 11, Chapter 2, the construction contracts awarded under this project included provisions for assessing penalties against contractors for work not completed on time. The penalty could not exceed ten percent of the estimated contract cost. These penalties would be considered as reasonable compensation without reference to whether or not any damage or loss was sustained. If the contractor was unavoidably hindered in its execution, the contract required the contractor to submit a written request to the Government of Bangladesh explaining why an extension was justified. The construction contracts also provided that ten percent of the billed amount would be retained by the Government of Bangladesh for a specified period of time after the work was completed. The Project Agreement stipulated that the Government would be reimbursed by USAID/Bangladesh for authorized payments made to the contractors.

Questionable payments were made to the Government of Bangladesh because the Government did not routinely assess the penalties when warranted. Data received from the technical assistance contractor on scheduled and actual completion dates disclosed that work under 132 contracts was not completed on time. The average length of delay for these contracts was about six months -- ranging from 7 days to about two years. Data received from the Government of Bangladesh showed that only 13 of the contractors had penalties assessed due to the delays.

A review of the the contractors' requests for extensions and data reported by the technical assistance contractor indicated that at least 54 of the contractors should have had the full penalty assessed for not completing the work on time. Assessment of these penalties would have reduced AID payments under the project by about \$108,000.

These figures on the number of contractors which probably should have had penalties assessed and the amount of penalties are conservative estimates based on available data. They include primarily contracts where the technical assistance contractor reported that the delays were specifically attributed to poor planning and performance by the construction contractors. Many other contractors possibly should also have been assessed penalties.

The technical assistance contractor representatives and the responsible USAID/Bangladesh officials told us that one of the problems that attributed to some work being delayed past the scheduled completion dates was the unrealistic time limits placed in the contracts. However, the technical assistance contract required that the contractor approve all tenders for construction work including the time allowed to complete the work.

The technical assistance contractor reported to USAID/Bangladesh as a general observation that among the primary contributors for the slow execution of the construction work were the non-availability of qualified contractors and the "practice of political patronage at the district level on behalf of the 'border line' contractors". This practice could be one reason why penalties were not routinely assessed.

Another area of questionable payments to the Government of Bangladesh concerned the Government's practice to request reimbursement from USAID/Bangladesh for the cost of construction work. The amount paid the contractors was actually ten percent less than that certified by the Government of Bangladesh and the technical assistance contractor as being paid and submitted to USAID/Bangladesh for reimbursement. Government of Bangladesh and technical assistance contractor officials said the total amount was submitted for administrative convenience. The Government of Bangladesh officials said the money retained was eventually paid upon the request of the construction contractor if the work remained in good condition for the time specified in the contract.

At the request of the audit staff, USAID/Bangladesh requested an accounting from the Government of Bangladesh on the status of the money retained under each contract; i.e., how much was paid the contractor, amount disallowed to the contractor, and current amount retained. The Government reported that as of September 1986, the total amount of AID payments retained during the course of the project and still being retained was about \$310,000 and \$110,000, respectively. The average retention period was about 13 months. The Government also reported that at least \$42,000 of the money still retained had not been paid to the contractors because funds were not available. Some of this money had been retained for over three years. In addition to the lack of USAID/Bangladesh accountability over these improper advances to the Government of Bangladesh, we estimate that the advances resulted in unnecessary interest costs to the U.S. Government during the past three years of about \$32,000.

USAID/Bangladesh did not monitor the enforcement of the penalty clause when construction work was not completed on time. USAID/Bangladesh officials said they did not believe this was a significant area under this project. Concerning the money retained under construction contracts, USAID/Bangladesh officials said they did not know the status of the money that was retained by the Government of Bangladesh until the data was provided in September 1986. In fact, USAID/Bangladesh officials thought the amounts identified in the requests for reimbursement submitted by the Government were the actual amount paid to the construction contractors. These officials said they relied on the certifications by the technical assistance contractor that the payments were made.

In conclusion, the exact amount of questionable payments could not be readily identified, but it is substantial. The payments were made primarily because USAID/Bangladesh did not have procedures to ensure that the Government of Bangladesh enforced the penalty clause in construction contracts for unwarranted delays in completion of the work, and USAID/Bangladesh officials were not aware that the Government of Bangladesh was submitting faulty claims for reimbursement. These problems would have been mitigated had the technical assistance contractor adequately reviewed the claims made by the Government of Bangladesh.

Management Comments

USAID/Bangladesh concurred in the finding and recommendation. It agreed to take actions to ensure (1) the penalty provisions in construction contracts are enforced, (2) an appropriate amount of each penalty assessed is refunded to AID and (3) the claims for reimbursements will be made only for actual payments. USAID/Bangladesh took action to ensure a proper accounting for the advance payments to the Government of Bangladesh for construction contracts and to recoup outstanding advances.

Office of Inspector General Comments

Based on the above actions, parts (a) through (d) of the recommendation are considered resolved and will be closed upon completion of the corrective actions. Parts (e) and (f) of the recommendation are considered closed upon issuance of this report.

5. Equipment Procurements Were Delayed

The Project Agreement authorized equipment valued at \$674,000. Additional equipment valued at \$500,000 was to be procured under the project extension. Most of the equipment initially authorized was not delivered to the project sites and some items were not even procured until four years after the scheduled delivery date. The procurement problem resulted in serious delays and inferior work of various road maintenance and improvement activities. A major cause of the delays was the absence of effective action and monitoring by USAID/Bangladesh to ensure timely procurement actions. Delays could also occur for the project extension because the design for the extension did not include a detailed procurement plan or specific time schedule for the procurement.

Recommendation No. 5

We recommend that USAID/Bangladesh:

- a. prepare a detailed procurement plan which includes a specific time schedule for completing the award of all contracts for the equipment to be acquired, and
- b. notify the Government of Bangladesh of the policy not to approve AID financing of any contracts awarded after the final scheduled date specified under the procurement plan.

Discussion

The Project Agreement included the procurement of various equipment items valued at \$674,000. Additional equipment valued at \$500,000 was to be procured under the project extension. The initially authorized equipment was to be procured and delivered at the project site by October 7, 1983. However, equipment valued at over \$464,000 was not yet delivered and some of the items were not even procured as of September 1986. See Exhibit 4 for the listing and status of equipment not delivered to the project site.

Delays in the procurement caused serious problems in the implementation of various road maintenance and improvement activities. The technical assistance contractor often reported instances of work delays and substandard work quality resulting from the lack of required equipment.

The delays in the equipment procurement were due to the unfamiliarity of AID procurement regulations on the part of the Government of Bangladesh and technical assistance contractor personnel. The lack of sufficient management attention by USAID/Bangladesh was also attributable to the delays.

The project design for the extension did not include a detailed procurement plan for the equipment or specific time schedule for implementing the procurement, except to mention that there was a possibility that the equipment could be in country around May 1987. In order to prevent recurrence of problems similar to those experienced in project implementation, we believe that USAID/Bangladesh should develop a detailed procurement plan and establish a firm time schedule for completing the award of all contracts for equipment.

Management Comments

USAID/Bangladesh agreed to work with the Government of Bangladesh and the technical assistance contractor to prepare a detailed procurement plan for the purchase of equipment to be acquired. USAID/Bangladesh believed, however, that a certain degree of flexibility be maintained to permit adjustment to the schedule when modifications are justified.

Office of Inspector General Comments

Part (a) of the recommendation is considered resolved and will be closed upon completion of the procurement plan. Part (b) of the recommendation remains open. We agree that justified adjustments to the plan should be allowed. However, based on the exorbitant delays experienced in purchasing equipment for the project, we believe the Government of Bangladesh should be formally notified that any adjustments to the plan must be justified.

B. Compliance and Internal Controls

Compliance - The major compliance exceptions noted were as follows:

- The Government of Bangladesh did not comply with the project covenants in the Project Agreement (Finding 1 and the following section).
- The project evaluations were not undertaken by USAID/Bangladesh in conjunction with the Government of Bangladesh as required by the Project Agreement and mandated by the respective AID regional bureau (Finding 1).
- The Government of Bangladesh did not provide the level of contributions required by the Project Agreement and Section 110 of the Foreign Assistance Act (Finding 2).

Other than the condition cited, tested items were generally in compliance with applicable laws and regulations, and nothing came to our attention that caused us to believe that untested items were not in compliance.

Internal Controls - USAID/Bangladesh had reasonably good procedures for reviewing reimbursement claims for construction work. In the year ended July 30, 1986, USAID/Bangladesh disallowed some of the costs claimed under 10 of the 18 requests for reimbursement when full payment had been endorsed by the technical assistance contractor. The primary reason for the disallowances was because the claims under the construction contracts exceeded the amount authorized by USAID/Bangladesh. The total amount claimed and disallowed were about \$830,000 and \$225,000 respectively.

The audit did, however, reveal two major internal control exceptions:

- USAID/Bangladesh voucher approval process did not prevent questionable payments to the technical assistance contractor and the Government of Bangladesh (Findings 3 and 4).
- USAID/Bangladesh management controls did not ensure that the Government of Bangladesh complied with the terms and conditions of the Project Agreement and that other critical components of the project were performed (Findings 1, 2 and 5 and the following section).

Other than the weaknesses cited, internal controls were found to be generally adequate in all material respects.

C. Other Pertinent Matters

The audit noted that the Government of Bangladesh did not comply with five of the seven project covenants including the three covenants discussed in Finding 1. The other two covenants not complied with were (1) improvement of the financial condition of each of the three districts covered by the project and (2) assurance that at least 25 percent of the budget of each of the districts was used for road maintenance activities. No record was available to indicate whether or not the Government of Bangladesh complied with a sixth covenant which required the Government to continue its regular allocation of funds for road improvement activities in the three districts. USAID/Bangladesh did not have established policies and procedures to ensure that the Government of Bangladesh complied with the project covenants in all its projects. Appropriate policies and procedures would preclude similar non-compliance problems in other projects.

The contractor was also routinely requesting reimbursement from USAID/Bangladesh for subcontractor costs before actual payments were made. For example, on May 17, 1986, the contractor requested reimbursement for the subcontractor's March 1986 expenses. The contractor did not pay the subcontractor for these reported costs until August 21, 1986. This practice was contrary to the reimbursement procedures stipulated in the technical assistance contract and provided the contractor cash advances which resulted in unnecessary interest costs to the U.S. Government. The contractor should be instructed to request reimbursement only for actual payments made.

AUDIT OF
FEEDER ROADS MAINTENANCE AND
IMPROVEMENT PROJECT IN BANGLADESH
PROJECT NO. 338-0056

PART III - EXHIBITS AND APPENDICES

List of Project Benchmarks Not Met

End of Year One

1. The Government of Bangladesh will have authorized the establishment of a trial maintenance unit in each of the three project districts.
2. Each maintenance unit will have its principal positions fully described and staff will be in place.
3. The road networks in each district will have been classified by priority and type of maintenance required.
4. Trial relationships between villages and the district engineers for simple maintenance activities will have been established.
5. The principal issues related to the project district revenue will have been identified and preliminary recommendation to improve revenue collective efficiency will have been made.
6. A review of the budget process of the project districts will have been completed and preliminary recommendations made.

End of Year Two

7. The organizational structure of each maintenance unit is sufficiently well established so that future activity can concentrate on improvements in efficiency and techniques.
8. An appropriate relationship with local villagers for road maintenance has been agreed to and is operating.
9. Routine maintenance is being carried out on at least 25 percent of each district's road networks.

End of Year Three

10. The organization of each maintenance unit including the involvement of villagers will have been finalized and the Government of Bangladesh will have issued the related authorizing directives.

11. Routine maintenance will have been carried out on 50 percent of the road networks in each project district.
12. The final version of the maintenance manual will have been completed and distributed to all districts in the country.
13. The Government of Bangladesh will have implemented or will be moving to implement the principal recommendations made by the finance study relative to improving the fiscal efficiency of the project districts.

Photographs: Badly Deteriorated
Road Segment Between Roads
Improved Under the Project

EXHIBIT 2

Improved Road Segments
Data

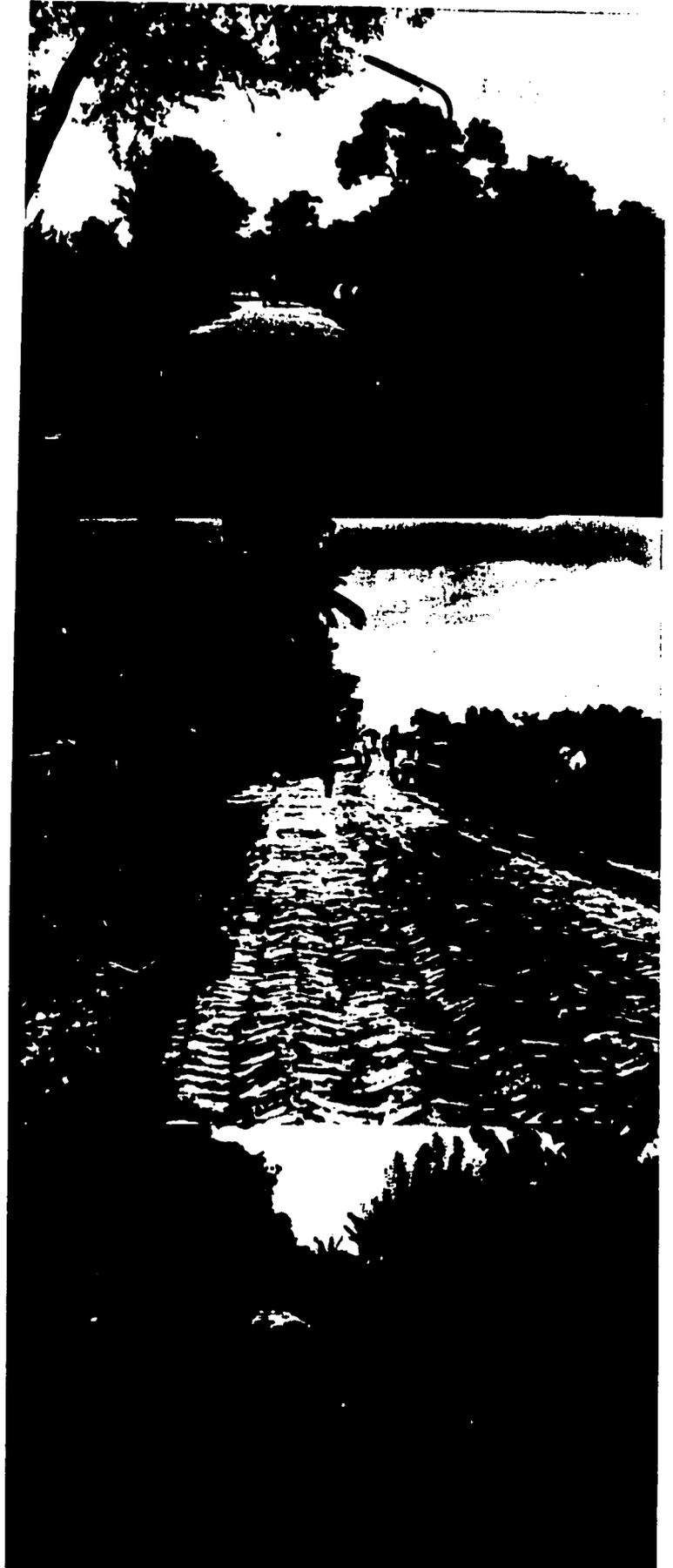
Date Work Stated: May 30,
1983

Date Work Completed: Nov 3,
1985

Miles Improved: 19 miles

Total Cost: \$1.2 million

AID Cost: \$1.1 million



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Shortfall in Government of Bangladesh Contributions in Local Currency

As of September 30, 1986

	<u>Contribution in Thousands of Taka</u>			<u>Net Shortfall</u>	<u>Shortfall in US Dollar Equivalent (3) (\$000)</u>
	<u>Amount Budgeted</u>	<u>Amount Required (1)</u>	<u>Amount Provided (2)</u>		
Technical Assistance	-	-	-	-	-
Equipment	-	-	-	-	-
Training	395	337	337	-	-
Road Maintenance	23,096	19,701	1,565	18,136	604
Road Development	35,629	30,392	25,792	4,600	153
Finance Analysis	-	-	-	-	-
Economic Study	-	-	-	-	-
Staff Salary	9,930	8,470	5,689	2,781	93
TOTAL	<u>69,050</u> =====	<u>58,900</u> =====	<u>33,383</u> =====	<u>25,517</u> =====	<u>850</u> =====

1) Represents the amount of budget as adjusted to the proportionate level of U.S. Dollar expenditures (85.3%) as of September 30, 1986.

2) Actual amounts were not available. Figures shown were estimated based on the best available information.

1) Exchange Rate of Tk 30 to US\$1.00 used.

Listing and Status of Equipment Items Not Delivered to the Project As Of November 30, 1985

<u>Type of Item</u>	<u>No.to be Procured</u>	<u>Status of Procurement As of November 30, 1985</u>	<u>Status of Procurement As of August 30, 1986</u>
Flat-bed Trucks	4	Contract decision approved by Government of Bangladesh and USAID/Bangladesh.	In process of shipment from the United States.
Road Rollers	6	Contract documents were approved by USAID/Bangladesh and sent to Government of Bangladesh for approval. (The contract was signed by the Government on January 20, 1986).	In process of shipment from the United States.
Concrete Vibrators	9	Consultant had requested the Government of Bangladesh to request USAID/Bangladesh for a "Source and Origin" waiver.	"Source and Origin" waiver which was granted by USAID/Bangladesh was no longer valid because a supplier was available from the United States. Procurement being delayed until USAID/Bangladesh decides whether or not funds were available.
Plate Compactors	6		
Shop Equipment	3	In process of shipment from the United States.	Being stored in contractor's warehouse until it is decided where they should be sent.
Tool Sets	3		
	--		
	31		
	==		

Listing and Status of Improvement Projects Active During the
Seven-Month Period Ended June 30, 1986

<u>Project Serial Number</u>	<u>Actual Contract Cost</u>	<u>Scheduled Completion Date</u>	<u>Percentage Complete as of 11/30/85</u>	<u>Actual Completion Date</u>
<u>SYLHET District</u>				
26	\$31,100	6/5/85	15%	4/20/86
32	\$36,200	5/21/85	50%	3/30/86
45	\$35,100	6/20/85	75%	4/15/86
<u>RANGPUR District</u>				
7	\$19,500	6/5/84	70%	6/-/86
<u>FARIDPUR District</u>				
27	\$32,100	7/31/85	60%	3/31/86

Note: This exhibit does not include five other uncompleted projects which had no or small amount of work performed during the seven-month period.

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UNITED STATES GOVERNMENT

memorandum

DATE: November 26, 1986

REPLY TO
ATTN OF: Dr. John Westley *JW* Director, USAID/Bangladesh

SUBJECT: Credit of the Feeder Roads Maintenance & Improvement
Project in Bangladesh (Project Number 388-0056)

TO: Mr. Richard E. Derrick, RIG/A/Singapore

Enclosed please find the Mission's comments on the subject draft audit report prepared by your staff.

While the report contains certain constructive recommendations which will assist the Mission in project implementation during the project extension phase, many of the findings draw conclusions from incomplete or inaccurate analysis.

AID acknowledges that nearly all projects with significant institutional development components experience sustained implementation difficulties. The Feeder Roads Maintenance and Improvement Project is no exception. Strengthening the institutional capability of the BDG to manage an effective program of routine annual maintenance and development of roads, requires a long term commitment of time and resources as well as flexibility in project design. Unsubstantiated statements such as "after five years and \$7.8 million in AID expenditures, little measureable accomplishments were made toward the project objective to institutionalize an effective program of routine annual maintenance and development of roads ...", will certainly attract headlines but will do little towards supporting the USAID in its efforts to achieve the overall project objective.

As stated in our cable Dhaka 8454, this Mission views audits as a valuable management tool. To be completely effective, however, there must be a mutual trust developed between the audit and mission staffs and the audit methodology should be fully discussed prior to initiating the audit. In the case of the subject draft audit, we requested the audit not be conducted prior to the Project Officer's (P.O.) return to post from leave. This was not the case, the audit was conducted in the P.O.'s absence. Had the audit been conducted while the P.O. was present many of the inaccuracies and misunderstandings contained in the report could have been avoided.

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For example, page 38 cites a statement which was included in the February 1986 consultant report. This statement was misinterpreted by the audit team and paraphrased in the audit report to support the auditors statement that the contractors were spending significant staff time on work beneficial to the contractor's interest and not within the scope of work required under the contract. This is not the case as we have indicated in our response.

I hope our response to the audit will allow prompt resolution to each of the recommendation and assure you the Mission staff will be working over the next few months to close all recommendations under terms mutually acceptable to our two offices.

I look forward to meeting with you in the near future to discuss our concerns in greater detail.

USAID/BANGLADESH RESPONSE TO AUDIT REPORT ON FEEDER ROADS
MAINTENANCE AND IMPROVEMENT PROJECT

The Feeder Roads Maintenance and Improvement project (FRMIP) represents one of USAID/Bangladesh's primary institution-building activities in support of rural infrastructure development--a critical component of the USAID strategy to stimulate rural employment and agricultural productivity. A long-term effect on sustained economic activity and productive employment opportunities requires that rural infrastructure be maintained and a reliable rural transportation system developed.

In the FRMIP, we have begun to institutionalize a routine road maintenance program in Bangladesh. We recognize that in this country, as elsewhere in the developing world, governments initially perceive little tangible benefit from, and thus provide little financial support to simple, routine infrastructure maintenance activities. The value of asset maintenance is critical to sustained economic growth, although it is admittedly difficult to inculcate. AID's Policy Paper on Institutional Development, as well as AID evaluation experience acknowledges that quote nearly all projects with significant institutional development components experience sustained implementation difficulties. unquote. The Paper similarly argues for the need for considerable experimentation in institution-building projects.

A commitment to building an institutional capability especially in rural asset maintenance, requires both a long-term commitment of time and resources, as well as flexibility in design. "Institutional development takes time-time to build capacity, time to develop effective working relationships with local populations, time to adapt a priori models of institutional development to on-the-ground circumstances. Thus, AID must be in a position to make longer term commitments to institutions (both public and private), and must be prepared to support a wide range of institutional development requirements."

The USAID thoroughly acknowledges implementation problems discussed in the audit. Nearly all had been discussed at numerous meetings of the Project Paper (PP) Supplement where issues were raised, discussed and consensus reached. Common implementation problems were discussed with other donors making investments in feeder roads and USAID took the lead in formulating recommendations to the BDG. The USAID had two options: (1) end the project at the Project Assistance Completion Date (PACD); or (2) extend the time and add the resources required to ensure continued progress toward the achievement of the original objectives. After considerable discussion, the USAID decided to approve the supplement. On August 31, 1986 a four-year extension to the project was signed to provide additional time and resources to further the project

objective--to institutionalize a program of annual routine maintenance and to increase the pace of feeder road development in Bangladesh. Although we recognize the difficulties inherent in this kind of activity, the critical importance of maintenance, and the catalytic effect that successful road maintenance may have on other rural infrastructure convinced us that the investment is worthwhile.

The importance of the lead role performed by USAID cannot be overemphasized. The donor community looks to USAID to provide the primary guidance because of our extensive involvement and experience with this category of infrastructure and the relative level of success we have been able to achieve. The Scandinavian donors have recently signed an agreement with the BDG that contains a feeder road development component. The implementation mechanisms to be employed in carrying out this activity simply makes a reference to the system agreed to under the USAID FRMIP. The Swiss Development Cooperation (SDC) has a proposed project with a feeder road element similar to that in the FRMIP. They have described project implementation precisely in the same terms as in the FRMIP.

Two important achievements of project implementation that have received limited to no discussion are the improved rate of feeder road construction realized in the later years of project implementation and the success of the overall training effort. The level of feeder road improvement performed in the last year of the project is a strong indication of the positive effects of the presence of the Consultant and from the technology transfer occurring from the on-the-job training effort and training in general. The latter point was highlighted in a draft evaluation report (submitted May 1986) of training activities funded by various donors working with the Local Government Engineering Bureau (LGEB), the technical unit in the MLG implementing rural infrastructure development projects.

Recommendation No. 1 a. The Government of Bangladesh establishes and fully staffs the organizations assigned responsibility for project implementation.

USAID concurs with the recommendation and believes that systems and procedures are in place to address the concerns identified in the recommendation.

The Project Grant Agreement Amendment No. 3 contains two Conditions Precedent (CPs) that address this recommendation. CP 4.1 (c) requires the BDG to establish the agreed Project Implementation Office (PIO) and appoint a Project Director. USAID will not consider the establishment of the PIO completed until all of the positions have been filled. CP 4.2 requires the BDG to appoint an additional Sub-Assistant Engineer (SAE) in eleven of the fourteen districts to supplement the existing district technical staff. This SAE will be assigned the

responsibility for feeder road maintenance. CP 4.2 must be satisfied prior to the release of the annual AID allocations for the Road Development Fund and Road Maintenance Fund.

Accordingly, USAID requests recommendation be closed.

Recommendation No. 1 b. The Government of Bangladesh agrees to provide quarterly reports with the names of individuals working in the organizations responsible for project implementation.

USAID does not concur with the recommendation.

Upon satisfaction of CP 4.1 (c) and 4.2, referenced above, USAID will issue a Project Implementation Letter (PIL) to advise the BDG of their compliance. This PIL will stress the importance of maintaining a fully staffed organization and will require the Consultant to include a section in their regular progress reports on the status of the staff in these positions. USAID does not see the additional value in having a quarterly report of the names of the individuals occupying the positions in the implementing organization.

Accordingly, USAID requests recommendation be modified. USAID will request recommendation be closed following issuance of PIL.

Recommendation No. 1:

c. Criteria are developed for the selection and scheduling of road improvement and maintenance activities; and

e. An economic feasibility study is initiated for potential road maintenance and improvement activities to be included under the project.

USAID concurs with these recommendations. In fact, criteria were established under the Rural Roads Study Phase I (dated August 1978) and by the Bangladesh Planning Commission for its strategy for rural development for Bangladesh.

The Rural Roads Study Phase I utilized the standard approach contained in the World Bank Staff Working Paper No. 241, The Economic Analysis of Rural Road Projects (August 1976). The five broad criteria used in ranking the roads were: (1) agriculture potential; (2) population density; (3) equity; (4) other economic activity; and (5) institutional and administrative capacity. Data was collected on a number of road links in the four selected districts of Faridpur, Rangpur, Patuakhali and Sylhet. The results of this effort was the identification of a core body of roads that formed the proposed road network to be reconstructed.

The BDG in 1982 adopted a strategy for rural development based on the fact that certain markets would act as poles for economic activity and classified these as Growth Centers (GCs). The initial criteria used in selecting markets as GCs was that: (1) there would be at least three and not more than four GCs in each Upazila; (2) the area of influence of each GC would be considered as the area within a radius of four miles of the market; and (3) the rank ordering would be determined as a result of an economic survey of all of the markets in the country. The survey was a three year effort that collected data on sixty-one variables that contributed to establishing a rating for the 6,000 markets in the country. There were 1,400 markets identified as GCs that form the basis for the long term (ten year period) rural development strategy of the BDG.

USAID recently matched the road segments improved under the project against the basic criteria established by the Rural Roads Study Phase I and those developed by the Planning Commission and found that, as we believed, the list does conform to the criteria of one of the two systems.

Future investments in feeder roads improvements under the FRMIP in the old districts of Faridpur and Rangpur will be limited to the completion of those segments on which work had already begun during the first phase of the project. It was agreed that an economic feasibility study would not be required for these roads.

In the old Sylhet district, new feeder road segments will be considered for improvement under the FRMIP. USAID did agree to undertake a review of the proposed list of roads to be included in the project and plans to perform appropriate economic analysis prior to any agreement on an AID investment on these roads.

It is noted that even in Phase II of the Rural Roads Study, not all of the roads identified in the road network were included in the full economic feasibility study. The Consultant for that study noted "To complete a thorough economic evaluation of thirty rural roads, totalling more than 235 miles, would require much more time and personnel than allotted in Phase II of this project." A representative sample of five road segments out of the twenty nine were selected with a total length of 69 miles out of the total of 235. During the Audit, USAID raised similar concerns that the cost and time required to conduct a full scale economic evaluation would be extensive and the results of the Phase II study indicate that the procedure employed in defining the road network proved effective as all five roads included in the complete economic evaluation were considered in terms of economic impact to be excellent candidates for an improvement investment.

The program for feeder road maintenance is based on the Maintenance Management report developed by the Consultant. In this report, maintenance activities were planned for all of the feeder roads that can be maintained as identified by the road inventory described below. The list of roads included in the inventory adheres to the criteria established by the the Rural Roads Study Phase I or the Planning Commission GC Strategy.

Accordingly, USAID requests these recommendations be closed.

Recommendation No. 1 d. A road inventory which classifies the condition of the roads covered by the project and type of work required is developed and used in the selection and scheduling of road maintenance and improvement activities.

USAID concurs with the recommendation.

The initial road inventory was, in fact, completed by the Consultant and submitted to USAID in October 1984. The inventory was used as the basic source of information for the proposed maintenance program that was field tested and adjusted as data on production rates were generated by the field. Maintenance tasks were prepared and performance standards developed that included such items as manpower requirements by skill category, equipment needs by type and material requirements. The rates for these performance standards were established by the Consultant based on experience in other developing countries and through discussions with local experts. The proposed maintenance program quantified the manhours, equipment hours and material needs from the information supplied by the inventory.

The development of an inventory is a dynamic process which must be updated periodically as conditions change. The initial inventory performed under the FRMIP provided a starting point from which a proposed maintenance plan was developed. It was never envisioned that the process would stop once the exercise was undertaken, but that constant review would be required. The first revision of the inventory was completed in the spring of 1986.

One aspect of the process that has not yet been completed was the description of the scale to be used to interpret the values assigned to the various road components. The Consultant, during the next five month period, will provide a detailed analysis with a description of the significance of the scores given in the inventory and how this relates to the development of a composite feeder road maintenance plan.

Accordingly, USAID requests this recommendation be closed.

Recommendation No. 1 f. An economic impact study is initiated for roads already improved under the project.

USAID concurs with the recommendation and has taken the initial steps to collect baseline socio-economic data.

The Socio-Economic Baseline study was performed September 1985 to May 1986 (the final report was submitted in September 1986) with the purpose of gathering data on roads improved under the project to determine the impact of a feeder road maintenance activity in rural Bangladesh. The focus of the FRMIP is to demonstrate the value of feeder road maintenance to the BDG and one mechanism to accomplish this is to collect data on the situation prior to the initiation of a routine maintenance program, to collect data at a later date and perform comparative analyses on the two sets of data to determine the impact.

USAID takes issue with the argument presented in the audit that two to three years is too long to wait to determine the impact of AID investment. Standard practice for road construction is to wait at least two years before comparative data is collected to judge the impact of the road on an area and it is widely accepted that the effects of maintenance take even longer. However, under the FRMIP extension, comparative data will be collected in early 1988 and then again in 1990. USAID continues to believe this approach is valid for assessing the impact of feeder road maintenance in the project areas and does not believe it would be useful to collect data before sufficient time has passed for the full effects of the effort to have taken place.

Accordingly, USAID requests this recommendation be closed.

Recommendation No. 1 g. Procedures are developed to ensure that USAID/Bangladesh approves road maintenance and improvement activities based on established criteria for the selection and scheduling of those activities.

USAID concurs with the recommendation. The review described for Recommendation Nos. 1. c and e above will lead to the development of a list of feeder roads to be included in the program.

As in the past, BDG requests for the release of AID funds for improvement and maintenance will contain a list of roads on which the funds are to be invested. USAID's release of funds will be based on not only the level of proposed funding, but also that the feeder roads are included in the approved list.

USAID also retains approval authority over specific activities on approved road segments. In the past, not all proposed improvement activities to be financed by AID were actually funded. For example, in Sylhet district for the 84/85 program a 265 ft. long bridge was proposed. The project paper stated that bridges with lengths of up to 75 ft. would be for

inclusion in the project for AID funding. The Sylhet administration tried to present a justification for the bridge based on its importance to the area and guaranteed the bridge would be completed by June 30, 1986. USAID eventually determined that the design was faulty and the bridge was not included in the project.

The review process does provide for final approval by USAID of individual activities prior to implementation. This process has proven to be effective. Accordingly, USAID requests this recommendation be closed.

Recommendation No. 1:

- h. Procedures are developed for semi-annual review and reporting on the status of meeting the project covenants; and
- i. A specific policy is established that the required project evaluations be made and reported to the Director of USAID/Bangladesh.

USAID concurs with the recommendations and has already taken steps to establish reporting on covenants and a policy is being drafted on evaluations.

A new Mission Evaluation Order on project reporting and evaluation requirements, recently drafted with assistance from AID/W and consultants, will provide decision makers with accurate and timely information on critical aspects of project activities so that implementation modifications can be initiated when required. A section of the reporting format will deal with reporting on the status of planned evaluations and the BDG adherence to project CPS and covenants.

Accordingly, following the issuance of the Mission Order, USAID will request this recommendation be closed.

Recommendation No. 2 a. Limit future payments to necessary technical assistance until the Government of Bangladesh provides the amount of the shortfall in its contributions to the project.

USAID does not concur with this recommendation.

The following table presents the BDG contribution to date by project element:

BDG CONTRIBUTION IN THOUSANDS OF TAKA

<u>Project Element</u>	<u>Amount Contributed</u>
Technical Assistance	-
Equipment	-
Training	337
Road Maintenance	18,502
Road Development MLG	25,792
Road Development District Councils	7,836
Finance Analysis	-
Economic Study	-
Staff Salary	5,568
Total	<u>Tk 58,035</u>

The BDG contribution to the FRMIP of Tk 58,035,000 has been calculated on actual taka provided for training, feeder road improvement and maintenance, and salaries of only those individuals permanently assigned to the project. It does not include any "in-kind" BDG contributions. The difference between the figures presented in the above table and the figures contained in Exhibit 3 of this Audit report (Tk 33,383,000) is Tk 24,653,000 which represents the updated figures for Rangpur and Sylhet District Council contributions for feeder road maintenance and the inclusion of the amounts all three District Councils invested in feeder road improvement. USAID agrees that this investment in feeder road improvement is justified.

In accordance with the terms of the project extension, the BDG is required to contribute a total of Tk 166,149,500 over the life of the project. A schedule of annual contributions to be made by the BDG over the remaining four years, incorporating the amounts shown in Tables A and B, Annex 1 of Amendment No. 3 to the Project Grant Agreement, will be developed. This schedule will be based on project needs for timely project implementation.

USAID did not agree during the Audit to limit future payments until the BDG provides the amount of any "shortfall" in its contribution. The position agreed to was that the BDG be required to contribute a total of Tk 166,149,500 over the life of the project. The Mission believes that as long as the annual BDG contribution over the life of the project meets the project implementation schedule and BDG contributions equal agreed upon total, the BDG will be in compliance with agreement.

Accordingly, USAID requests this recommendation be closed.

Recommendation No. 2 b. Establish procedures to ensure that the Government of Bangladesh provides its required contributions and deposits the amount of local currency contributions into a special accmount at the beginning of each program quarter.

USAID concurs with the recommendation in principle, but does not agree with the establishment of a special account. The CP Section 4.3 in Amendment No. 3 to the Project Grant Agreement provides the assurance the BDG will not only make annual allocations, but will disburse the funds.

Section 4.3. (a) states: "evidence that the Grantee has budgeted for and will disburse the amounts shown in the Table A, Annex 1, for the Road Maintenance Fund and the amounts shown in Table B for the Road Development Fund, both from the Grantee's budget for the applicable Bangladeshi fiscal year."

USAID will consider the BDG has satisfied this annual CP only after a review of: (1) the proposed allocations for the upcoming fiscal year; and (2) the status of the allocations and expenditures for the previous fiscal year. This will provide USAID with the opportunity to look both forward for future planned activities and backward at performance in meeting agreed upon commitments. These procedures will be the subject of a PIL.

Accordingly, USAID requests recommendation be modified. USAID will request recommendation be closed upon issuance of this PIL.

Recommendation No. 2 c. Require that the Government of Bangladesh provide quarterly reports on the status of the Government's contributions.

USAID concurs with the recommendation.

The PIO will be required to submit quarterly reports on the status of project activities including the level of the BDG contribution for the particular fiscal year of the reporting period and cummulative contributions to date. These reporting requirements will be the subject of a PIL.

Accordingly, upon issuance of this PIL, USAID will request this recommendation be closed.

Recommendation No. 3:

a. Perform a technical evaluation on the allowability of the labor hours and other technical aspects of costs billed by the technical asistance contractor; and

b. Take action to recoup questionble costs claimed by the technical assistance contractor.

USAID does not concur in full with the recommendations as presented. During the Audit, USAID agreed to review the systems in place to verify that only allowable costs had been paid the Consultant.

Standard Agency established procedures are in place within the Mission to review and certify Consultant payments. USAID reviewed vouchers submitted by the Consultant and determined the costs incurred to be allowable in accordance with the terms and conditions of the contract. Notwithstanding this review, the U.S. Government, through the Defense Contract Audit Agency, retains the authority to audit costs under this contract. A technical evaluation as proposed by the Audit report would be a purely subjective document which the Mission feels would be of little value.

Substantive work was performed by the Consultant during the seven month period identified. A management decision was made to reduce the T.A. staff during this period to a minimal level to enable continuation of ongoing activities and preparatory work for the extension period. As such, the expatriate staff was reduced from five full time advisers to three and the local staff was limited to those already on the payroll with a slight reduction in non-essential staff and the policy that no replacements would be named for existing or future vacant positions. This action did result in a reduction in contract costs and avoided additional expenses which would have been incurred had the contract been completely demobilized and subsequently remobilized.

USAID takes issue with the example cited in the report as an indication that unallowable work was paid for during that period. The Audit report references sections of T.A. contractor's February 1986 Progress report in which work performed by the T.A. contractor was not allowable. USAID reviewed this report and found the following: "During the reporting period, the staff of the project consultant were mainly engaged in documentation of the progress payments made to the Contractor and in minimizing the discrepancies between the records of the client and consultant."

The "Contractor" referred to in the report are the 166 construction contractors and the progress payments are their vouchers for the construction work performed. The Consultant was minimizing the discrepancies between the records of the client (BDG) and the Consultant for these construction contracts.

USAID does not believe it is in the best interest of the USG to perform a technical evaluation beyond what is already performed by USAID through the Project Officer's approval during the normal voucher review process.

USAID requests the reference to "technical evaluation" in Recommendation 3 a. be deleted and replaced by "review" and that both recommendations be closed accordingly.

Recommendation No. 4:

- a. Require the Government of Bangladesh to enforce the penalty clause in the completed construction contracts when there were unjustified delays in completing the work; and
- b. Recoup from the Government of Bangladesh the amount of penalties assessed.

USAID concurs with the recommendations and plans to take the actions described below to address the concerns identified in the recommendations.

USAID will prepare a letter under the signature of the Director, instructing the MLG to undertake a review of all construction contracts funded in whole or part by AID. The review will focus on the requests for time extensions submitted by the contractors to determine the validity of the requests and the amount of time the contract should be extended. In those instances where full time extensions are not justified, the BDG will be required to assess the appropriate amount of penalty and take steps to recoup this amount from the respective contractors. The BDG will then refund to AID the applicable amount of the AID contribution of the penalty for each contract.

USAID will review the BDG records to determine the level of penalty already assessed and the amount, if any, that has been reimbursed to the BDG will be deducted from the next set of reimbursement requests to be submitted by the BDG.

USAID will report further on level of penalties recouped prior to requesting closure of Recommendation 4 b. USAID will request Recommendation 4 a. be closed upon issuance of a letter to BDG.

Recommendation No. 4:

- c. Establish procedures to ensure the Government of Bangladesh routinely enforce the penalty clause in construction contracts; and
- d. Instruct the Government of Bangladesh and the technical assistance contractor that claims are only to be made for actual payments made by the Government and authorized by USAID/Bangladesh.

USAID concurs with the recommendations and plans to establish the procedures described below to address these recommendations.

USAID will include in the PIL earmarking funds for future Road Development Fund activities, instructions on enforcing the penalty clause contained in the construction contracts. In addition, USAID will require a review of the assessment of the penalty clause prior to disbursing funds for final payment to any construction contractor. USAID believes these steps will protect the U.S. Government interest in that an amount equal to 10% of the value of each contract is retained. This amount equals the maximum level of penalty permitted under the standard contract.

On the security retention issue, USAID will instruct the BDG in this same PIL that the security retained during the course of construction will be converted into the maintenance deposit at the completion of the actual construction. USAID will not consider reimbursing the BDG for this maintenance deposit until it has been returned to the construction contractor at the end of the specified maintenance period. Since this maintenance period varies from district to district and for various types of construction work, the BDG will indicate the length of the maintenance period at the completion of each contract. Also, the amount of the security retention will be clearly identified on individual progress payment vouchers to avoid the reimbursement of this item during construction.

Accordingly, upon issuance of this PIL, USAID will request these recommendations be closed.

Recommendation No. 4:

e. Review the Government of Bangladesh records to ensure a proper accounting of the advance payments to the Government for construction activities; and

f. Recoup outstanding advances retained by the Government of Bangladesh.

USAID concurs with the recommendations and has already initiated the review and recoupment of the outstanding advances.

USAID issued a letter to the BDG, AID Letter No. 1195 dated August 19, 1986, indicating that AID had been overbilled for the amount being retained as security by the BDG and this amount would be deducted from the next set of reimbursement requests. This amount will only be reimbursed to the BDG upon certification that the contractors have been paid these amounts.

The BDG indicated that it is common practice for the security retention to be converted to the maintenance deposit retained by the BDG for a specified period of time after the construction work has been completed. The BDG accounting system thus shows that the contractor has been paid the full amount, but has subsequently applied the security retention

toward the required maintenance deposit. USAID stated that this may be the practice, but as far as AID is concerned the security fund converted into the maintenance deposit will only be reimbursed at the end of the maintenance period. As stated above, this position will be reflected in the PILs earmarking funds for Road Development Fund.

84. Accordingly, based on the issuance of AID Letter No. 1195, USAID requests these recommendations be closed.

Recommendation No. 5:

- a. Prepare a detailed procurement plan which includes a specific time schedule for completing the award of all contracts for the equipment to be acquired; and
- b. Notify the Government of Bangladesh of the policy not to approve AID financing of any contracts awarded after the final scheduled date specified under the procurement plan.

USAID concurs with the recommendations and will work with the PIO to develop a comprehensive procurement plan.

USAID in conjunction with the BDG and the Consultant, will prepare a detailed procurement plan for the purchase of the equipment required for the FRMIP extension. The plan will contain specific dates by which certain activities will have to occur. USAID will not approve any PILs earmarking funds for this project element until this plan is developed and agreed to by both parties. USAID, however, believes that a certain degree of flexibility be maintained to permit adjustments to the schedule when USAID agrees that modifications are justified.

Accordingly, upon completion of the procurement plan, USAID will request these recommendations be closed.

LIST OF REPORT RECOMMENDATIONS

Recommendation No. 1

We recommend that USAID/Bangladesh limit funding to necessary technical assistance until:

- a. the Government of Bangladesh establishes and fully staffs the organizations assigned responsibility for project implementation;
- b. the Government of Bangladesh agrees to provide quarterly reports on the status of staff working in the organizations responsible for project implementation;
- c. criteria are developed for the selection and scheduling of road improvement and maintenance activities;
- d. a road inventory, which classifies the condition of the roads covered by the project and type of work required, is developed and used in the selection and scheduling of road maintenance and improvement activities;
- e. an economic feasibility study is initiated for potential road maintenance and improvement activities to be included under the project;
- f. an economic impact study is initiated for roads already improved under the project;
- g. procedures are developed to ensure that USAID/Bangladesh approves road maintenance and improvement activities based on established criteria for the selection and scheduling of those activities;
- h. procedures are developed for semi-annual review and reporting on the status of meeting the project covenants; and
- i. a specific policy is established that the required project evaluations be made and reported to the Director of USAID/Bangladesh.

Recommendation No. 2

We recommend that USAID/Bangladesh:

- a. take action to ensure that the Government of Bangladesh provides the amount of the shortfall in its contributions to the project;

- b. establish procedures to ensure that the Government of Bangladesh provides its required contributions; and
- c. require that the Government of Bangladesh provide quarterly reports on the status of the Government's contributions.

Recommendation No. 3

We recommend that USAID/Bangladesh:

- a. perform a technical evaluation on the allowability of the labor hours and other technical aspects of costs billed by the technical assistance contractor; and
- b. take action to recoup questionable costs claimed by the technical assistance contractor.

Recommendation No. 4

We recommend that USAID/Bangladesh:

- a. require the Government of Bangladesh to enforce the penalty clause in construction contracts when there were unjustified delays in completing the work;
- b. recoup from the Government of Bangladesh the amount of penalties assessed;
- c. establish procedures to ensure the Government of Bangladesh routinely enforce the penalty clause in construction contracts; and
- d. instruct the Government of Bangladesh and the technical assistance contractor that claims are only to be made for actual payments made by the Government and authorized by USAID/Bangladesh;
- e. review the Government of Bangladesh records to ensure a proper accounting of the advance payments to the Government for construction activities; and
- f. recoup outstanding advances retained by the Government of Bangladesh.

Recommendation No. 5

We recommend that USAID/Bangladesh:

- a. prepare a detailed procurement plan which include specific time schedule for completing the award of all contracts for the equipment to be acquired, and
- b. notify the Government of Bangladesh of the policy not to approve AID financing of any contracts awarded after the final scheduled date specified under the procurement plan.

Appendix 3

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