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AUDIT OF
USAID/EGYPT'S IMPLEMENTATION OF
AID'S PAYMENT VERIFICATION POLICY
Audit Report No. 6-263-87-10
June 30, 1987

UNITED STATES GOVERNMENT

memorandum

DATE: June 30, 1987

REPLY TO ATTN OF: Joseph R. Ferri, RIG/A/Cairo

SUBJECT: Audit Of USAID/Egypt's Implementation Of AID's Payment Verification Policy

TO: Mr. Arthur M. Handly, Director USAID/Egypt (A)

This report presents the results of audit of USAID/Egypt's Implementation Of AID's Payment Verification Policy. The objective of this compliance audit was to evaluate the adequacy of USAID/Egypt's overall compliance with the Payment Verification Policy in conjunction with a worldwide review being made by the Office of Inspector General.

The audit showed that USAID/Egypt complied in full with three and partially with nine Mission directed policies. Two important policy areas, dealing with capabilities of host country agencies and Mission voucher examination and payment processes were not complied with so as to promptly surface and correct weaknesses in these areas. The Mission took a number of actions recently that should bring it into more substantial compliance with agency policy.

Slowness in making assessments of Government of Egypt entities exposed the Mission to conditions that might have received more attention, if known earlier, to avoid or mitigate problems. For example: $275 million in planned projects were not effectively implemented in 1986, a $1.8 million advance was unneeded by a Government of Egypt agency, and some commodities were ineffectively controlled by the host country or contractors.

Incomplete assessments of USAID/Egypt's voucher examination and payment processes contributed to contractors being paid late or before due, cash advances needing liquidation, and invalid obligations.

Seven recommendations were made to improve compliance with the Policy. These recommendations include USAID/Egypt setting priorities and making Policy assessments, reimplementing voucher controls, establishing requirements and improving instructions to staff on Policy issues,

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establishing an adequate voucher due date system, and assisting the host government to resolve an issue of contractor overhead rates.

USAID/Egypt generally agreed with the recommendations and had started implementing them before the audit was completed. As a result, three recommendations were closed upon issuance of this report and Policy compliance significantly improved. Mission comments directed to the recommendations were excerpted and included at the end of the findings section along with Office of Inspector General comments. The full text of USAID/Egypt's comments on the draft report are included in this report as Appendix 1.

Please provide us within 30 days any additional information related to actions planned or taken to implement the remaining recommendations.

EXECUTIVE SUMMARY

AID's Payment Verification Policy, issued December 30, 1983, contains 16 individual policies developed by AID senior officials. The overall policy is directed to improving the Agency's system of internal controls over payments thereby reducing vulnerabilities to waste, fraud, and abuse in the payment process. To achieve this end responsibility was placed on Missions to analyze various aspects of the payment process. The individual policies include requirements for Missions to evaluate the methods for implementing and financing projects, the capabilities of host governments for awarding and administering contracts, and the adequacy of payment approval and voucher examination procedures.

The objective of this compliance audit was to evaluate USAID/Egypt's overall compliance with the policy direction.

The audit showed that as of September 30, 1986 USAID/Egypt had not complied fully with most of the policies applicable to its operations. During and subsequent to the audit the USAID/Egypt Controller began taking actions that would bring the Mission into more substantial compliance with these policies.

Of the 16 policy statements contained in the overall policy, 12 were directed specifically to Missions. Of these, USAID/Egypt complied in full with 3 and partially with 9 policies. Generally, USAID/Egypt did not comply with Policy Statement Numbers 1-5 and Policy Statement Numbers 8 and 9 dealing with assessments. These assessments included two singularly important areas: capabilities of individual host country and implementing agencies; and voucher examination procedures. The lack of compliance with these policies meant that inefficiencies and internal control weaknesses in USAID/Egypt projects and operations were not surfaced and corrected in a timely manner.

Problems related to Policy Statements 1-5 included, among others: (a) delays in implementing planned projects; (b) excessive cash advances; and (c) ineffective control over inventories. Problems related to Policy Statement Numbers 8 and 9 included, among others: (a) unnecessary interest costs; (b) invalid obligations; and (c) not adjusting provisional overhead rates to actual.

To reduce system vulnerabilities we recommended that USAID/Egypt give a high priority to implementing the policies by assigning responsibilities, amplifying guidance, training staff, and improving systems. USAID/Egypt supported the recommendations made and initiated actions to close several of them.

Office of the Inspector General

AUDIT OF
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AID'S PAYMENT VERIFICATION POLICY

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AUDIT OF USAID/EGYPT'S IMPLEMENTATION OF AID'S PAYMENT VERIFICATION POLICY

PART I - INTRODUCTION

A. Background

AID's Payment Verification Policy contained 16 policy statements and guidance developed by a task force of AID senior officials for implementation at the Mission level. The Policy, issued December 30, 1983, was directed to improving internal controls over payments, thereby reducing vulnerability to waste, loss, unauthorized use, or misappropriation of funds. The policy was in response to Congressional concerns and the results of audits made by AID's Office of Inspector General and the General Accounting Office that highlighted weaknesses in AID's payment processes. The work of the task force coincided with a 1983 self assessment of AID's internal control vulnerability.

The 16 statements set forth AID policies and guidance for: (a) assessing methods of project implementation and financing, and host government capabilities to contract, monitor, examine invoices, perform audits, and financially manage and control the use of funds; (b) evaluating audit needs and coverage; (c) strengthening administrative approval of vouchers; (d) assessing voucher examination procedures; (e) encouraging the use of public accounting firms as consultants; and (f) revising AID practices to achieve better accountability in its operations.

USAID/Egypt officials did not indicate any problems in interpreting the policy statements or make any specific recommendations during the audit for improving on them. The Controller expressed a positive attitude toward the statements, saying they were long overdue and needed to protect the Agency.

B. Audit Objectives And Scope

The objective of this compliance audit was to evaluate USAID/Egypt's compliance with the Payment Verification Policy. The audit was made in conjunction with a worldwide audit by the Office of Inspector General. The results of this audit were provided for inclusion in a consolidated audit report to AID management.

The audit examined USAID/Egypt's system, as of September 30, 1986, for complying with the Policy. Mission officials were interviewed. Controller files and records, recent Regional Inspector General for Audit, Cairo audits, non-federal audit reports, consultants' assessments, project papers and, vouchers were examined.

Judgementally selected tests were made of vouchers drawn from $7.4 million in randomly-selected project and operating expense vouchers. The tests consisted of 12 payment vouchers, totaling $4.9 million. These vouchers were reviewed for compliance with terms of the agreements involved and with other AID regulations.

The audit also included a review of 10 payment vouchers, totaling $5.3 million, for the purpose of determing how payment due dates were established. The $7.4 million consisted of 39 contract payments, totaling $5.8 million, and 72 other expenditures, totaling $1.6 million. These other expenditures included cash advances, advance liquidations, payments to other U.S. Government entities, travel vouchers and other operating expense type items.

During fiscal year 1986, USAID/Egypt expended $970 million; $380 million for projects and operating expense; $360 million for cash transfers; and $230 million for nonproject commodity imports. The audit did not include cash transfers, nonproject commodity imports, or small-value procurements financed by AID in local currency. Internal controls and prior audit findings were considered in areas examined. The review of internal controls and compliance was limited to the finding areas presented in this report.

In reference to prior Office of Inspector General audits mentioned in this report, recommendations in these reports were concurred in by USAID/Egypt management and corrective actions were reported. The actions taken were considered responsive, and the recommendations were closed.

This audit was made between September 1986 and February 1987, and was made in accordance with generally accepted government auditing standards.

AUDIT OF
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PART II - RESULTS OF AUDIT

Of the 16 policy statements contained in the overall policy, 12 were directed specifically to Missions. Of these, USAID/Egypt complied in full with 3 and partially with 9 policies. Generally, USAID/Egypt did not comply with Policy Statement Numbers 1-5 and Policy Statement Numbers 8 and 9 dealing with assessments. These assessments included two singularly important areas: capabilities of individual host country and implementing agencies; and voucher examination procedures. The lack of compliance with these policies meant that inefficiencies and internal control weaknesses in USAID/Egypt projects and operations were not surfaced and corrected in a timely manner.

Problems related to Policy Statements 1-5 included, among others: (a) delays in implementing planned projects; (b) excessive cash advances; and (c) ineffective control over inventories. Problems related to Policy Statement Numbers 8 and 9 included, among others: (a) unnecessary interest costs; (b) invalid obligations; and (c) not adjusting provisional overhead rates to actual.

USAID/Egypt's initial general assessment in June 1984 was forthright and the Mission took steps on the basis of it to reduce some vulnerabilities in its system. The Mission substantially reduced the use of bank letters of commitment (L/Comms) to finance cost-reimbursable contracts, and implemented a program for audits of host country contractors. Independent accountants were hired to make some assessments. Subsequent to the September 30, 1986 cutoff date of the audit, the Mission Controller took other actions that significantly improved compliance with Policy Statement Numbers 1-5, 6, 8 and 9.

Before September 30, 1986, however, few, mostly incomplete, detailed assessments were made of host country entities and of new projects. USAID/Egypt had not formally assessed voucher examination procedures during 1986, or included tests of all vouchers in prior years' assessments. Further, USAID/Egypt had not maintained adequate files of assessments and had allowed slippage in reporting assessments to AID/Washington.

The report makes seven audit recommendations to achieve better compliance with the policy statements. We recommended that USAID/Egypt: assign a high priority to assessing capabilities of individual host country entities; issue staff guidelines and training for making annual voucher assessments, specific project paper assessments, and for instituting voucher controls; establish a system for determining voucher due dates, and provide assistance to host country contract agencies in resolving an issue concerning audits of a contractor's overhead rates.

USAID/Egypt supported the desirability of the seven audit recommendations and initiated corrective actions. Several recommendations were closed on the basis of the indicated actions.

A. Findings And Recommendations

Better Compliance With Several Key Policy Statements Was Needed

USAID/Egypt complied with some, but not adequately with most, Payment Verification Policy statements and guidance, as of September 30, 1986. The primary cause of inadequate compliance was the lack of a sustained level of priority by USAID/Egypt management to implement the policies and to issue detailed instructions to Mission staff. Exhibit 1 summarizes the extent of compliance by policy statement.

USAID/Egypt's slowness in completing assessments of host country implementing agencies contributed, in part, to not identifying the root causes for conditions wherein: (a) USAID/Egypt could not effectively implement $275 million in planned projects during fiscal year 1986; (b) a cash advance of $1.8 million was excess to the grantee's immediate cash needs; (c) equipment and inventories were ineffectively controlled; (d) there were weaknesses in accounting and reporting systems for AID-financed local currency; and (e) poor relations existed between the host country and AID-financed contractors.

USAID/Egypt's incomplete assessments of voucher examination and payment processes contributed, in part, to: (a) late payments of contractors' invoices and unnecessary interest costs of $340 thousand in 1986 for paying vouchers before due; (b) cash advances of $16.2 million needing liquidation; (c) invalid obligations totaling $2.3 million that did not meet AID criteria; and (d) a contractor using a provisional billing rate for more than 5 years without contest.

Recommendation No. 1

We recommend that USAID/Egypt assign a high priority to assessing the capabilities and systems used by individual host country contracting and local currency implementation entities, in accordance with AID Payment Verification Policy statements and guidance. USAID/Egypt should ensure initial coverage of all entities within a reasonable period. Assessments should include recommendations for improving conditions, controls, accounting, reporting, eliminating bottlenecks, or changing methods of implementation and financing.

Recommendation No. 2

We recommend that the USAID/Egypt Controller's staff in carrying out annual assessments of USAID/Egypt's voucher approval and voucher examination processes, include representative samples of vouchers as set forth in the Policy.

Recommendation No. 3

We recommend that USAID/Egypt require that voucher examiners prepare and use contract abstracts and letters to contractors for revised invoice detail requirements as set forth by the USAID/Egypt Controller.

Recommendation No. 4

We recommend that USAID/Egypt require Mission officials, in preparing project papers and Program Assistance Approval Documents, to use designated formats and charts for reporting on methods of implementation and financing, host country capabilities, audit coverage needs and other Policy issues.

Recommendation No. 5

We recommend that USAID/Egypt issue instructions to clarify the role of project officers in the proper procedures for processing vouchers for payment and in requesting disallowances under host country contracts.

Recommendation No. 6

We recommend that USAID/Egypt continue working to establish a system for paying vouchers as closely as administratively possible to due dates determined in accordance with contract terms, AID Handbook 19, Appendix 1C and Prompt Payment Act standards.

Recommendation No. 7

We recommend that USAID/Egypt assist host country contracting agencies to finalize the actual overhead rates for periods audited for Contract No. 263-0045-03.

Discussion

The December 1983 Payment Verification policy statements and implementation guidance were issued to improve systems of internal control over AID payments. The following pages set

forth the extent to which USAID/Egypt complied with the individual policy statements and guidance which are paraphrased below, and shown in complete context in Exhibit 2.

1. Policy Statement Nos. 1-5: General and Detailed Assessments

Complied in part

Policy Statements Nos. 1-5 required USAID/Egypt to conduct general assessments of its methods of implementation and financing, covering all existing and planned projects and programs, to further support these by detailed assessments in its project papers, and to justify certain methods of financing when used. Host country contracting agencies were to be assessed as to their abilities to contract, monitor implementation, examine invoices and audit contractors. Assessments were also required of host country arrival and accounting systems under Commodity Import Programs (CIPs) and of financial management procedures for AID-financed local currency provided to intermediate credit institutions or indigenous private voluntary organizations.

The policy guidance required USAID/Egypt to report its assessments to AID/Washington, and to obtain Controller's concurrence in methods of implementation and financing. Decentralized host country entities were to be assessed on a sample basis in the initial general assessments, with reviews of all entities completed over time. Annual updates were to indicate changes in the initial assessment as a result of a continuing review process. Results of assessments by the Mission Controller under Policy Statement Numbers 8 and 9 were to assist the Mission in preparing its general assessments.

General Assessments

The initial general assessment, due March 31, 1984, was submitted in June 1984. No update was prepared for December 31, 1984; and the update due December 31, 1985, was submitted on February 2, 1986. Except for the initial reporting delay, slippage was attributed to a lack of significant additional information to report primarily due to the paucity of individual assessments.

The initial assessment was candid in describing general methods of project implementation and financing, and in rating these methods. Weaknesses reported were generally

accurate and supportive of reviews made by outside accountants and USAID/Egypt internal control vulnerability assessments. The assessment, however, did not specifically address or indicate the extent to which reviews were made of individual projects or entities. Moreover, USAID/Egypt had not adequately assessed the host country contracting procedures and accounting systems of many implementing agencies.

Host Country Assessments

A few of the approximate 45 host country contracting agencies were partially assessed, but after 33 months of the policy requirement USAID/Egypt had not completed plans for making all assessments. Discussions with Office of Financial Management officials indicated that Financial Analysts had visited some implementing agency offices during fiscal years 1984 through 1986, but not for the purposes of making full assessments. For example, in 1986, visits were generally to answer project office requests for information and to view project sites. Only in one case did a project officer's request to find out why an implementing agency had not promptly paid its host country contractors lead to a change in the method of financing.

USAID/Egypt also assessed a few host country entities accounting for AID-financed local currency, using the services of an outside consultant. The consultant's report, dated November 13, 1984, indicated the need for greater knowledge of host country practices. The consultant identified 38 projects and 44 Government of Egypt entities accounting for $392 million in local currency commitments. The consultant visited four agencies comprising $86.9 million of the total. Of the four, the consultant categorized the Basic Education Project No. 263-0139, with $45.9 million committed, as "high risk" and the Small Farmer Production Project No. 263-0079, with $23.4 million, as also having substantial accounting and reporting deficiencies. Of these two cases requiring USAID/Egypt follow-up, a Financial Analyst assigned to the Basic Education Project reported that the consultant's recommendations led to an improved system of accounting and reporting and control over cash advances. Financial Analysts had not visited the Small Farmer Production project for follow-up of accounting procedures.

Regarding new project papers, specific assessments of host government agencies also had not been made regularly. Although USAID/Egypt had properly used standard or justified methods of financing, a review of project papers issued during fiscal years 1985 and 1986, showed a lack of complete assessments and conclusions for 4 of 5 methods of implementation and financing tested. The prescribed chart for financial analysis, showing the dollar values by each method, was not used.

RIG/A/Cairo Audit Report No. 6-263-86-9, USAID/Egypt's Assessment of Host Country Contracting Capabilities disclosed that the lack of appropriate written assessments of host country contracting during this period was due mainly to unfamiliarity with requirements on the part of USAID/Egypt officials. The report noted that the Controller had approved all project face sheets, except one due to an oversight; however, the project papers and program assistance approval documents, generally did not follow the prescribed format. For example, the project papers did not spell out all methods of implementation to be used in each proposed project and the various financing under each method. The program assistance approval documents (1984-1986) did not include evaluations of the host country commodity arrival accounting systems, as a basis for selecting USAID/Egypt systems to monitor the Commodity Import Program.

The major reason that USAID/Egypt had not established a more active program of making regular assessments and was slow in working toward a complete overall assessment of all projects, programs and implementing agencies, was the low priority assigned to such efforts.

Recent Mission Actions

During the audit, USAID/Egypt took steps to improve compliance with the policies. After September 30, 1986, the USAID/Egypt Controller greatly increased efforts to comply with Policy Statement Nos. 1 through 5. The Controller's office identified 45 host country implementing agencies needing assessments and prioritized 22 for assessment. By May 20, 1987, USAID/Egypt had completed 6 of these assessments, compared with 11 partial assessments made in prior periods. The 6 assessments disclosed a lack of supporting documentation for payments in one case, accounting deficiencies in other cases, and corrective actions initiated. Also, new project papers, and those in

process, were amended to show methods of implementation and financing by project activity and justifications for departure from preferred methods using appropriate chart formats as required.

Project And Program Problems

A more aggressive effort earlier by USAID/Egypt to make the required assessments and take preventive actions, however, could have reduced Mission vulnerabilities in the payment process. USAID/Egypt files, prior audit reports, consultants' reports, and discussions with USAID/Egypt officials clearly established the existence of structural weaknesses in USAID/Egypt projects and programs in need of correction. As discussed below, these weaknesses, among other things, contributed to: delays in implementing projects; unneeded cash advances; ineffective control of inventories; and failure to pay contractors or other problems.

(1) USAID/Egypt's project expenditures for fiscal year 1986 of $374 million, amounted to 57.6 percent of the planned expenditures of $649 million. According to USAID/Egypt's analysis, one of the principal reasons for expenditure shortfalls of $275 million was GOE project management indecision and delays in planning and approving procurement documents and awarding contracts. According to the analysis, GOE indecision greatly slowed many projects with construction or procurement components. Of the 20 projects with the largest shortfalls, 16 projects with large construction or procurement components accounted for $182 million, or 66 percent of the total shortfall (Source: Cable, Cairo to AID/W, No. 27127, November 24, 1986).

(2) Intermediate Credit Institutions (ICIs) and other entities responsible for controlling and reporting on uses of AID-financed local currency made available to them did not properly follow AID procedures or held cash advances in excess of needs. For example:

- An AID advance of $1.8 million remained unused from December 4, 1984, through May 26, 1986. The amount needed to be recovered from GOE agency because construction of banks and warehouses was not taking place in three governorates. The advance cost the U.S. Government about $244,000 in unnecessary interest. (Source: RIG/A/C Audit Report 6-263-86-8 dated August 20, 1986, Small Farmer Production Project No. 263-0079).

- An AID-financed consultant reported, in November 1984, on one of four local currency systems tested, that: (a) the amount advanced project-wide to Governorates, exceeded current needs by an estimated $800 thousand; (b) the accounting/reporting system was inaccurate, faulty and did not reflect actual expenditures of the Governorates; (c) accounting records were prepared from telephone-reported estimates of costs that had not been recorded; (d) other costs were not properly chargeable to the project; and (e) the entity had not made audits of project-related records, as required (Source: Consultant's report on the Basic Education Project No. 263-0139).

(3) Host country agencies or contractors lacked effective systems of control over inventory or use of equipment. For example:

- The GOE's inventory system did not assure that all $75 million of equipment and materials financed by AID were received in good condition, accounted for, and used as intended. Receiving reports were either incomplete or not prepared at all, claims were unresolved, and transfers from port to warehouses and construction contractors were not documented (Source: RIG/A/C Audit Report No. 6-263-85-5, dated July 25, 1985, Canal Cities Water and Sewerage Project No. 263-0048,).

- A GOE implementing agency lacked effective procedures for monitoring and reporting equipment utilization. As a result, USAID/Egypt was unaware that $1.8 million of equipment was unused or used for proscribed purposes. In addition, accountability was lacking over $3.4 million disbursed for spare parts. Auditors found that: (a) claims for damaged and missing parts were not being pursued; (b) shipments were delivered without packing lists; (c) there were no stock cards or other control records; (d) receiving documents were missing; and (e) physical security was inadequate to protect parts from elements and theft (Source: RIG/A/C Audit Report No. 6-263-85-1, dated October 31, 1984, The Decentralization Support Fund Activity No. 263-K-605.4).

(4) Contractors complained of unreasonable delays by the GOE in settling claims, approving vouchers for payment, or other factors contributing to poor relations with the GOE implementing agencies. For example:

- A contractor requested USAID/Egypt to establish a direct letter of commitment and pay the contractor in accordance with the contract provisions over the objection of the GOE implementing agency (Source: USAID/Egypt files, Canal Cities Water and Wastewater Project No. 263-0048).

- The GOE Ministry of Supply did not provide the contractor with a written explanation, in accordance with the disputes resolution provisions in the contract, for grounds under which the Ministry claimed ownership for equipment imported by the contractor for work under the contract (Source: USAID/Egypt files, Safaga Grain Silos Project No. 263-0165).

- A contractor requested AID's assistance in resolving contractual disputes that allegedly denied the contractor $1,000,000 in payments. The contractor cited one case in which it had furnished materials, but had not been reimbursed for $170 thousand in materials that were to be supplied by the GOE (Source: USAID/Egypt files, Helwan Housing and Community Upgrade Project No. 263-0066).

2. Policy Statement No. 6: Need for Audits

Complied in part

Under this policy statement, Project Papers were to include an evaluation of the need for audit coverage and project funds were to be budgeted for independent audits unless adequate audit coverage by the host country was reasonably assured, or audits by third parties were not warranted.

The audit showed that USAID/Egypt contracted with a public accounting firm (Arthur Young and Company) to perform audits and, thereby, reduced the Mission's vulnerability to improper payments on selected host country contracts. In 1982, USAID/Egypt with Office of Inspector General concurrence, contracted with a non-Federal auditing firm to audit direct costs of cost reimbursable host country contracts. A study completed by the auditing firm in April 1984 identified 37 "high-vulnerability" contracts from a field of about 200 contracts. In September 1984, USAID/Egypt under a one-time arrangement with GOE approval, increased the funding to $1.5 million for such audits.

The non-Federal auditors completed some of the scheduled audits and issued reports of findings, but efforts were still continuing at the time this audit was completed. USAID/Egypt was working to establish an effective method for

dealing with the findings in these reports, i.e. for collecting or negotiating and settling questioned costs under host country contracts, which involved host country, not AID, contracting officers.

Although audit coverage was provided on these contracts, USAID/Egypt did not properly budget audit funds in all new project papers to allow for future audits. Since July 1985, for example, the Mission provided funds for audit coverage in 3 of 5 of recently-funded projects tested. Two of the three, had not indicated the audit purposes for which the funds were to be used. In one case, the funds were lumped together under the caption "audits and evaluations" without adequate explanation of audit needs.

Partial compliance with Policy Statement No. 6 was attributed to a lack of definitive USAID/Egypt guidelines. The Mission had not established procedures that ensured audit funds and an evaluation of the need for audit coverage would be included in project papers.

USAID/Egypt's Controller subsequently took steps to improve compliance with Policy Statement No. 6. New project papers and those in process were amended to show the needs and purposes of funds budgeted for audit coverage.

3. Policy Statement No. 7: Administrative Approval of Vouchers

Complied

Project officers were to provide the Controller a statement advising the basis upon which administrative approval of payment vouchers was given.

A sample of 19 recent vouchers indicated that USAID/Egypt had properly instituted this requirement for approving vouchers prior to payment. A checklist described in the policy guidance was added by the Mission on August 29, 1984 (Financial Management Bulletin No. 3/84), to the former negative statement of approval.

Although project officers interviewed generally considered the checklist and statement to be adequate, other USAID/Egypt personnel had varying opinions of what was required of the project officer in signing the statement. For example, one opinion was that the language served no purpose because it had never resulted in any court action

against the signer and that the project officer needed only sign the face of the voucher. Another opinion was that the statement required the project officer to carry out more of a review than was required by AID Handbook 19. A third observation was that some project officers, in connection with their approval, sometimes duplicated the work of voucher examiners, and at times, had requested the USAID/Egypt certifying officer to make disallowances without approval of the host government.

Based on the limited review and discussions with USAID/Egypt personnel, there was no reason to doubt the validity or adequacy of the use of checklists in connection with the negative statement of approval by project officers. Although USAID/Egypt technically complied with the policy statement, and some project officers received project implementation course training on the administrative approval process, the policy statement needed to be more clearly explained to Mission project officers in terms of processes and responsibilities of project officers, voucher examiners, and certifying officers.

4. Policy Statements No. 8 and 9: Assessments of Mission Voucher Examinations and Host Country Monitoring and Invoice Examination Procedures

Complied in part

Mission Controllers were responsible for providing annual assessments of Mission voucher approval and voucher examination procedures. The review was to involve a randomly selected sample of vouchers large enough to provide reasonable assurance that the voucher approval and examination procedures, in place, were adequately represented by the assessment. Mission Controllers were also to provide annual assessments of the adequacy of the monitoring and invoice examination procedures followed by host country contracting agencies. In doing so, bottlenecks in the vouchering and paying processes within the host country agencies were to be highlighted. The first annual assessment could include reviews of only a few host country agencies. The annual updates were to include additional agencies until all were reviewed.

Mission Controller Guidebook, Chapter V, Section III further stated that "...Mission Controllers in the field are responsible for the establishment and maintenance of voucher examination units..." (and) "...The voucher examiner is responsible for the proper review of bills submitted to AID

for payment. This review includes: (a) ascertaining that the voucher is adequately supported by appropriate authorizations, documentation, and certifications; (b) observing established internal controls designed to prevent any improper or duplicate payment; (c) determining that disbursements pursuant to the voucher are in accordance with laws and regulations; and (d) determining payment due dates and computing late payment interest, if required...Although final responsibility for certifying a voucher for payment rests with the Certifying Officer, the voucher examiner's review must be of a quality and depth sufficient to afford ample protection to the Certifying Officer in discharging his responsibility..."

USAID/Egypt did not provide adequate annual assessments of its voucher approval and voucher examination procedures as required. During 1986, USAID/Egypt did not formally assess the procedures by a random sampling of vouchers. Prior years' samplings were deficient because cash advances, operating expenses, AID direct contracts or bank L/Comm payments were not included.

USAID/Egypt did not sample the 1986 vouchers because there had been little personnel turnover of voucher examiners. Also, a certified public accounting firm (Arthur Young and Company) had trained and assisted the staff, in 1985, in preparing and using abstracts of host country contracts to improve controls over the examination process. During 1985 and prior, USAID/Egypt did not sample all types of vouchers because the Mission concentrated on host country contract vouchers, as the most significant area. Thus, weaknesses in other payment areas did not come under review. USAID/Egypt was unable to determine the exact number of host country contracting agencies that were assessed because the files had not been organized for that purpose.

Nevertheless, USAID/Egypt acted upon some areas of high vulnerability discussed in the general assessment. It:

- reduced the use of Bank L/Comms to finance cost-reimbursable contracts from 17 to 3 (see next paragraph).

- implemented a program to audit "high vulnerability" host country contractors.

- formed a Mission office to provide support services to project officers.

participated in the American Contractors in Egypt organization as a medium to air contractors' problems and to work toward solutions with the host government.

The majority of USAID/Egypt's host country contracts were funded through either a Bank Letter of Commitment (Bank L/Comm) or a Direct L/Comm. A Bank L/Comm authorizes the contractor's designated bank to make payment to the contractor upon submission of an invoice. After payment, the Bank requests reimbursement from AID/Washington. Although this type of implementation document is used frequently for fixed-price commodity procurements, it has also been used for cost-reimbursable contracts. AID generally has no indication of the extent or quality of the review performed by the host country agency or the bank, and USAID/Egypt receives no copies of the actual invoice, except in rare cases when courtesy copies are sent. So, the project officer does not have the opportunity to review the invoice. Instead, the contractor submits his voucher to the GOE for review; the GOE certifies performance and sends the package directly to the bank for payment. This process differs from the AID Direct L/Comm procedure in which AID, generally, receives and reviews cost reimbursable invoices after the GOE completes its review and certifications.

In 1984 and 1985, under directions of the USAID/Controller, Arthur Young and Company studied and evaluated the Mission's system of internal control with respect to the payment processing system in the area of host country contracts. The review, dated April 15, 1984, included "limited sampling of transactions to determine if controls were functioning as intended." In June 1985, a subsequent Arthur Young and Company review was reported for the period October 22, 1984 to June 17, 1985, of 42 host country contracts/work orders and related invoices. Bank L/Comm-financed contracts were not included in the 42 contracts tested by Arthur Young and Company. Since then, USAID/Egypt has not formally sampled vouchers as required by the Policy Statement. The audit was unable to examine the details of the public accounting firm's voucher examinations. Neither USAID/Egypt nor the firm could locate the workpapers. Therefore, the audit could not determine if USAID/Egypt corrected all the exceptions noted by the firm. The firm sampled 42 contract agreements and reported 95 apparent payment discrepancies. Recommendations were made for voucher examiners to keep contract abstracts up to date, monitor compliance with minimum invoice detail requirements, and for the Controller's office to perform the same type of review

(including the preparation of contract abstracts) for AID direct contracts as performed by the public accounting firm for the host country contracts.

Voucher And Payment Process Problems

The audit established that as of September 30, 1986, some controls instituted by Arthur Young were not continued. Moreover, there were other weaknesses in areas not previously reviewed by the firm. The audit's review was based on recent Regional Inspector General for Audit audits, tests of vouchers, and discussions with USAID/Egypt personnel. USAID/Egypt's lack of assessments of the voucher and payment processes contributed, in part, to payments issued late or before due; excessive advances; overstated obligations; voucher examination controls not being instituted; and other payment discrepancies.

(1) Payment due dates were not properly determined by voucher examiners in scheduling vouchers for payment. Most vouchers tested were either paid late or before due. Late payments disadvantage AID-financed contractors while premature payments result in unnecessary interest costs to the U.S. Government.

Regulations specify that payment shall be due under the terms of the contract or, if not established in the contract, the due date shall be determined by the provisions of the Prompt Payment Act. AID Handbook 19, Appendix 1c, further states that "...AID will make payment under all types of contracts as close as possible to, but not later than, the due date..." In foreign locations, the due date if not established in the contract, is "...45 calendar days after receipt of a proper invoice...or 45 calendar days after a designated AID official or authorized representative accepted the property or services, whichever is later..."

At the time of the audit, voucher examiners were not giving attention to due dates. USAID/Egypt did not have an adequate system in place to establish voucher due dates from vouchers and contract terms, and to know the length of time vouchers were held by the host country contracting agencies.

A test of 10 vouchers drawn from the 39 contract vouchers in our random sample of 111 vouchers showed that 2 vouchers, due when received by USAID/Egypt, were paid timely (within 3-5 days). Five other vouchers were paid late (within 8-22 days) and 3 vouchers, without specified due dates

established in the contract, were paid early, at cost to the U.S. Treasury. The interest cost of these early payments, calculated at a 9 percent borrowing rate, totaled $4.695. The sample represented about 5 percent of the total number of payments in the period tested. Projecting these results, the total interest cost to the U.S. Treasury was estimated at about $340,000 for 1986.

During the audit, USAID/Egypt started taking steps to pay vouchers when due. A financial officer assigned by the Controller was working on a system for assigning proper due dates to incoming vouchers, setting priorities for voucher examination and payment in accordance with contract terms and Prompt Payment regulations.

(2) Under agreements providing advances, host government institutions submitted vouchers to substantiate the use of advance monies and to justify additional or replenishing advances. The examiner, in addition to the standard voucher audit, should examine further to determine whether there is a continuing need for a subsequent advance based on the submitted documentation. A Regional Inspector General for Audit, Cairo audit found that cash advances often exceeded immediate cash needs of recipients. The audit identified 165 balances, totaling $16.2 million of cash advances, that needed to be liquidated or refunded as of June 30, 1986, with an estimated interest cost to the U.S. Government of $854 thousand. The audit also found that voucher examiners did not always make or use appropriate calculations to adjust advance levels to realistic needs of recipients (RIG/A/C Draft Audit Report dated June 1987 of Cash Advances).

(3) An audit of unliquidated obligations for operating expense activities showed an estimated $2.3 million of invalid obligations. These idle funds which could have been used productively were attributed, in part, to voucher examiners not having closed out residual balances after goods and services were paid for and delivered (Source: RIG/A/C Audit Report No. 6-263-86-7, Unliquidated Obligations for Operating Expenses, dated July 31, 1986.)

(4) Voucher examiners did not fully institute contract abstracts for voucher payment controls as recommended by Arthur Young and Company, and USAID/Egypt had not made an annual review to see if the controls were established, kept up to date and used. Instead, voucher examiners used a system partially based on highlight pens and yellow tabs to

flag important contract terms. As a result, voucher examiners did not use contract abstracts as checklists to ensure that important contract provisions and amendments were enforced.

Out of 9 contracts reviewed, 6 abstracts were incomplete or inaccurate and 3 were not on file. In prior reviews, Arthur Young and Company had found that no one at the Mission was comparing vouchers with the terms and conditions of contracts before payment. The firm had recommended the Office of Financial Management perform a more detailed voucher examination using a payment checklist (contract abstract) for each contract. It concluded that the awareness by voucher examiners of the meaning and implication of several key payment related contract clauses, coupled with contract abstracts and the increased level of detail required for invoices, strengthened the host country contract payment process. This audit found that contract payment terms had not been fully observed resulting in early or late payments to contractors.

(5) Voucher examiners did not require contractors to comply with minimum invoice detail requirements recommended by Arthur Young and Company and specified in a USAID/Egypt Controller's memo dated November 15, 1984. In prior reviews, the firm found that information missing from payment files was critical to determining the accuracy of invoices submitted for payment. This audit found that substantial documentation was present in most cases tested. Voucher examiners, however, did not routinely continue to send letters to contractors specifying missing invoice detail, current approved overhead rates and other necessary information, or follow-up such letters previously sent to contractors.

- In one case a contractor's invoices were paid based on the provisional overhead and general and administrative rates stated in the contract. The contract required the contractor to submit proposed final rates to the host country contracting agency within 6 months after the close of each fiscal year. These rates were to be audited and approved by the contracting agency and by AID. Instead, the provisional rates were continually applied during the life of the contract, from October 1981 through November 1986.

USAID/Egypt officials pointed out that even when contractors do comply with the overhead-proposal requirements, it takes several years in some cases for audits to be completed and

final rates negotiated. In this case, USAID/Egypt correspondence received in December 1986, indicated that proposed rates had been audited by the Defense Contract Audit Agency (DCAA) for fiscal years ended June 30, 1982 and 1983 and the DCAA had reported these audits in December 1984. The DCAA also had been requested by the cognizant agency, Department of State, to audit fiscal years 1984 and 1985, and DCAA had planned to start the audit by June 30, 1987. Even though the audited rates appeared to be higher, USAID/Egypt needed to determine the final negotiated rates for fiscal years through 1983 and the current provisional rate from the cognizant agency, and take steps to correct the contractor's billing (Source: USAID/Egypt files Development Industrial Bank II, L/Comm No. 263-0045-03: Price Waterhouse/Khattab).

5. Policy Statement No. 10: Utilizing Accounting and Financial Services

Complied

Mission Controllers were encouraged to use the services of competent public accounting firms in providing accounting and financial management consulting services within the project design, as a part of program funding and in auditing host country contracts. Controllers were also encouraged to use contract personnel for voucher examinations.

USAID/Egypt beneficially used the services of independent public accountants to make tests of voucher payment processes, establish systems and train voucher examiners, prioritize and audit direct costs of host country contractors, design a CIP counterpart accounting system, and make assessments of accounting and reporting systems of AID-financed local currency recipients. The use of such services noticeably increased after 1983. Generally, such services were funded from operating expenses and from project funds in cooperation with the GOE. Various types of contracts were used, including Indefinite Quantity Contracts. Other areas, in which outside accountants could have been used (but were not), were preaward audit surveys and assessments of host country or indigenous Private Voluntary Organization capabilities.

USAID/Egypt Financial Management officials supported the concept of Policy Statement No. 10 and found the services of outside accountants useful and need-filling, although these officials had expected greater cost recoveries from audits

of host country contracts. All of the accountants and auditors had issued, or were in the process of issuing, reports of services performed, findings and recommendations. The contracted for auditing services complied with the requirement for pre-approval by the Office of Inspector General.

With respect to using contract personnel for voucher examinations, the Mission's voucher examination staff was composed chiefly of contract-hires throughout the period reviewed. Office of Financial Management officials did not see an immediate need to hire more voucher examiners. We agreed with the Mission's evaluation.

6. Policy Statement No. 11: Commodity Price Analyses

Mission Compliance Not Required

This policy stated that AID's commodity price analysis function should be strengthened to permit more adequate prepayment or postpayment audits of commodity costs. The implementation guidelines designated AID/W (M/SER/COM) as the action office. Thus, Mission compliance was not required.

The USAID/Egypt officials that we questioned had not been exposed to M/SER/COM functions, at least for several years and, therefore, declined to comment on the need for more effective audits of commodity costs.

7. Policy Statement No. 12: Emphasizing Incentive Contracting

Mission Compliance Not Required

This policy stated that AID should place greater reliance on incentive contracting approaches where contractors shared in savings or received extra benefits for timely completion of contracts. The implementing guidelines designated AID/W (M/SER/CM) as the action office. Thus, Mission compliance was not required.

USAID/Egypt officials had mixed reactions regarding the use of performance incentives in USAID-financed contracts. Generally, officials agreed that incentives were worthwhile in construction contracts. For engineering services, however, the concept had not been well-tested. A USAID/Egypt construction management contract was executed in June 1986 with award fees for engineering performance based on grading

the contractor, subjectively and quantitatively, on five aspects with consideration given to control and reduction of costs. The five aspects were: change-order management, ingenuity, completeness, technical competence, and implementing cost accounting systems. Since this was a fairly new contract, the benefits had not been proven.

An earlier (May 1982) contract, for technical advisory services involved award fees for: (1) submitting timely work plans annually; and (2) maintaining staff in remote field locations for extended periods of time. According to Mission officials, the incentive to submit work plans in a timely manner was a weak aspect since it paid the contractor for what it was required to do. The second incentive helped keep the contractor's staff in outlying communities for longer periods, but also had the possible negative effect of perpetuating contract personnel, whether effective or not. The USAID/Egypt experience with incentive type contracts was not sufficient to draw meaningful conclusions about effectiveness.

8. Policy Statement No. 13: Host Country Contract Invoice Requirements

Complied

The policy set forth that host country contracts include definitive requirements for submission of invoices and supporting documents.

USAID/Egypt had taken steps to ensure that invoice requirements were well-defined. The Mission had, according to officials:

- used standard provisions in host country contracts,
- required contracts to be reviewed by USAID/Egypt Legal, Contract and Controller office personnel prior to approval,
- held discussions between new contractors and Controller's staff at start of the job,
- issued the Controller's letter, dated November 15, 1984, to establish Revised Invoice Detail Requirements and distributed these requirements to appropriate host country cost-reimbursable contractors.

These steps improved the detail level of invoice and supporting documents; however, better monitoring was needed to ensure that these controls were in place. For example, the Controller's letters to contractors needed periodic follow-up to ensure that requested supporting documents were received. (See Policy Statement Nos. 8 and 9 for discussion of the Mission's practices regarding minimum invoice detail requirements.)

9. Policy Statement No. 14: Utilization of Fixed Amount Reimbursement (FAR) Procedures for Non-Construction Projects

Mission Compliance Not Required

The policy stated that models for use of the FAR concept for nonconstruction projects should be developed. In order to assist AID/W, Missions were requested to transmit examples of expanded uses of FAR and any suggestions that may be helpful. Mission compliance with the policy statement was not required.

We contacted several USAID/Egypt officials from the Contracts, Legal, Controller, and Projects offices. The consensus was that few, if any, projects had made use of the FAR concept in nonconstruction contracts and, therefore few, if any, examples had been submitted to AID/W.

USAID/Egypt was planning to use performance disbursement, a variant of FAR, in a proposed agriculture production credit project. Capital funds would be distributed incrementally, based on policy reforms instituted by the GOE. Some reforms, such as crop selection and pricing, would require cooperation between ministries. The project officer was optimistic about the program and believed that it would work.

USAID/Egypt officials interviewed, had not seen the AID Evaluation Occasional Paper No. 1, Implementing Policy and Institutional Change via Performance Disbursement: Examples from the Philippines, Bangladesh and Niger, dated July 1985. The paper was not available in USAID/Egypt's development information center. Following our inquiry, the document was requested from AID/W.

10. Policy Statement No. 15: CIP Arrival Accounting Systems

Complied in part

All Missions with existing or planned CIP programs were to evaluate host country arrival accounting systems as part of the overall evaluation and include the assessment in each program assistance approval document (PAAD) requesting future CIP authorizations. Missions that could not positively attest to the adequacy of the host country systems were to provide a satisfactory alternative.

The audit found that no assessments of the host country arrival accounting system were included in PAADs during the last three years. Present USAID/Egypt officials were not aware of any documented assessment to satisfy this policy statement. According to the Mission Controller's review of files from the start of the CIP program through fiscal year 1980, the host government had considered to an arrival accounting system but had not put such a system in place. As a result, USAID/Egypt established and relied on its own CIP commodity arrival and information systems.

11. Policy Statement No. 16: Two-Step Loan Agreements

Mission Compliance not Required

This policy stated that AID would explore resuming use of formal two-step loan agreements, given the increased emphasis on private sector participation. AID/W was designated as the action office for providing guidance on this issue. Accordingly, USAID/Egypt compliance with this policy statement was not required.

Except for a few loan agreements dating back to 1978 or prior USAID/Egypt's projects were grant-funded and, two-step loan arrangements were not applicable.

Management Comments

USAID/Egypt generally agreed with the audit report recommendations. It commented on actions taken since the audit for closing the recommendations.

Recommendation No. 1. USAID/Egypt said that priority had now been assigned within Mission work requirements by designating Mission financial analysts with primary, specific objectives for assessing 22 host government

agencies by June 1988. As of May 20, 1987, 6 assessments had been completed and 3 were partially completed. Analysts were devoting more than half of their time to these tasks.

Recommendation No. 2. USAID/Egypt scheduled an assessment of its voucher approval and examination process for June 1987.

Recommendation No. 3. USAID/Egypt cited its existing practices as reasons for not adopting this recommendation. It said (1) highlighted photocopies of contract payment terms were being used in lieu of preparing separate contract abstracts, and (2) contractors were being advised of appropriate reporting procedures in specific contracts, as necessary, in lieu of maintaining the general financial-reporting requirements set forth, previously, by the Mission Controller.

Recommendation No. 4. USAID/Egypt developed a standard format, in project papers, to report on the methods of implementation and financing, host country contracting capabilities, audit coverage needs and other issues, which meets the requirements of the Policy. It said all new project papers now include appropriate financial analyses, formats and charts prepared by Mission financial analysts.

Recommendation No. 5. USAID/Egypt said its project officer training courses, for the last three years, were reasonable steps taken to implement AID instructions on the role of project officers in processing vouchers.

Recommendation No. 6. USAID/Egypt evaluated its payments process, reorganized its voucher examination section and instituted a computerized voucher control and prompt payment system to control the processing of invoices on proper due dates and to ensure timely examination and tracking of vouchers.

Recommendation No. 7. USAID/Egypt did not indicate any action taken, but commented that provisional overhead rates usually increase based on overhead audits and that the U.S. Government is not damaged by delayed adjustments. USAID/Egypt also commented that it advises the parties to host country contracts to finalize rates as expeditiously as possible and works with GOE agencies to do so.

Office Of Inspector General Comments

In view of actions taken by USAID/Egypt Recommendation Nos. 1, 4 and 6 were closed upon issuance of this report. Recommendation No. 2 will be closed when USAID/Egypt completes and reports the results of its 1987 annual assessment of voucher approval and voucher examination procedures in accordance with Policies 8 and 9.

Concerning Recommendation No. 3, we agree that highlighting important contract payment terms is important, but contract abstracts should continue to be used as checklists. Also, specific criteria for contractors to follow in submitting details with invoices can reduce AID exposure, pending post audit, by ensuring that contractors provide adequate supporting documents. These two controls also provide criteria for evaluating voucher examiner performance. The recommendation can be closed upon USAID/Egypt's written instructions reimplementing the use of contract abstracts and instructions to contractors for invoice detail requirements.

Regarding Recommendation No. 5, the USAID/Egypt project officers' training course provides instructions to Mission personnel. All project officers, however, do not attend the courses. The recommendation will remain open pending issuance of USAID/Egypt instructions to clarify the role of project officers in conducting administrative reviews, processing vouchers, and questioning costs under host country contracts.

Recommendation No. 7 will be closed upon evidence that USAID/Egypt has obtained for Contract 263-0045-03, the final negotiated overhead and general and administrative expense rates for audited years, determined billing adjustments, and notified the host country agency concerned.

B. Compliance And Internal Control

Compliance

USAID/Egypt had not taken appropriate steps to ensure that AID Payment Verification Policy and related USAID Controller Guidebook guidelines were followed. Also, AID Prompt Payment Implementation Policy and Procedures, issued relative to OMB Circular A-125 dated August 19, 1982, and the Prompt Payment Act of 1982 was not followed. These matters were discussed in appropriate sections of this audit report. Nothing else came to our attention that indicated noncompliance in areas untested. The audit work in compliance was limited to the finding areas presented in this report.

Internal Control

There was a lack of oversight to ensure that evaluations were made of host country implementing agencies or entities; that proper assessments were made of implementation, financing and auditing of new projects; and that voucher examiners were performing properly and were making proper use of contract abstracts and revised invoice detail controls established by the Controller's office. The audit work in internal controls was limited to the weaknesses in findings reported.

AUDIT OF
USAID/EGYPT'S IMPLEMENTATION OF
AID'S PAYMENT VERIFICATION POLICIES

PART III - EXHIBITS AND APPENDICES

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EXHIBIT 1

Extent Of USAID/Egypt Compliance With Payment Verification Policies

Policy Statement Number	Description	Compliance
1-5	General and Detailed Assessments	In Part
6	Evaluation of Need for Audits	In Part
7	Administrative Approval of Vouchers	In Full
8-9	Assessments of Mission Voucher Examination Function and Host Country Monitoring	In Part
10	Utilizing Accounting and Financial Services	In Full
11	Commodity Price Analyses	Not Applicable
12	Emphasizing Incentive Contracting	Not Applicable
13	Host Country Contract Invoice Requirements	In Full
14	Utilization of FAR Procedures for Non-Construction Projects	Not Applicable
15	CIP Arrival Accounting Systems	In Part
16	Few-step Loan Agreements	Not Applicable

(In Full 3, In Part 9, Not Applicable 4.)

UNITED STATES INTERNATIONAL DEVELOPMENT COOPERATION AGENCY
AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON D C 20523

DEC 30 1983

MEMORANDUM

TO: All Mission Directors

FROM: AA/M, R. T. Rollis, Jr.

SUBJECT: Payment Verification Policy Implementation Guidance

Based on the Administrator's approval of sixteen (16) Payment Verification Policy Statements last April, the attached implementation guidance has been developed in coordination with the various AID/W bureaus.

These policy changes complement the effort currently underway for improving our systems of internal control (OMB Circular A-123) and should be implemented effective January 1, 1984. We do understand that this process, like A-123, will take several years to fully implement. In addition, during the next year applicable handbooks and policy guidances will be revised accordingly.

Attachment: a/s

cc: AID/C, F. Kimball
AA/AFR, F. Donatelli
AA/ASIA, C. Greenleaf
Actg. AA/LAC, M. Brown
AA/NE, A. Ford
AA/PPC, R. Derham
AA/S&T, N. Brady
AA/FVA, J. Bloch
AA/PRE, E. duPont
GC, H. Fry
IG, H. Beckington
AFR/PMR, F. Brown
ASIA/DP, A. Evans
LAC/CONT, J. Davison
NE/DP, R. Bornaffon
All Mission Controllers

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PAYMENT VERIFICATION POLICY

IMPLEMENTATION GUIDANCE

As a result of the Administrator's emphasis on implementation of AID programs and for consistency with the Federal Managers Financial Integrity Act and OMB Circular A-123 on Internal Control, the Administrator has approved 16 policy statements on financial and administrative management. This document reviews the policy statements and provides general guidelines for their implementation. Until these policies and guidelines have been incorporated into the handbooks, this document and any future amendments will serve as the Agency directive for these policies.

As the first five policy statements are so interrelated, the guidance addresses them as a unit. The final eleven policy statements are treated individually.

I. Policies establishing the most appropriate methods of implementation and financing as an essential part of the initial development assistance planning process.

A. Policy Statements:

1. A comprehensive general assessment of methods of implementation and financing, reviewed from the standpoint of accountability, is to be presented on a regular basis and more specific assessments are to be included in the Project Papers.

2. AID/W Controller concurrence on the implementation and financing aspects are to be included in the the general assessment and the more specific PP assessments requiring AID/W review.

Discussion:

The CDSS does not include a full assessment of accountability, implementation and financing methods. At the PID and PP/PAAD stages, such considerations generally have not received sufficient

attention. The CDSS is not an appropriate document for assessing program implementation and financing (e.g. use of Fixed Amount Reimbursement procedures) host country contracting, and the acceptability of the host country commodity procurement process. However, a general assessment should be performed and submitted to AID/W early in the project/program approval process. At the PP/PAAD stage, more specific assessments and findings should cover methods of implementation and financing. The PP/PAAD should refer to the effectiveness of various methods of implementation and financing in the country program overall and relate the overall assessment to the projects and to the level of efficiency of the implementing organizations.

3. As a part of the assessments under 1. above, a justification is to be submitted whenever the mission proposes to depart from any of the following general policies:

(a) The use of Fixed Amount Reimbursement (or modified Fixed Amount Reimbursement) as the preferred method in financing multiple unit construction.

(b) Use of the Federal Reserve Letter of Credit (FRLC) procedure. (Note that FRLCs may be used only in the case of non-profit organizations. They cannot be used in any case for host country contracts or loan-financed contracts.)

(c) The use of the direct reimbursement procedure (reimbursing the host country, contractors and others) instead of other methods of payment which entail AID financial credit instruments to direct payments for contractors and suppliers.

Discussion:

The direct payment procedure is considered synonymous with direct reimbursement in the context of these policies.

4. As part of the assessments under 1. above, a justification is to be provided whenever the mission proposes use of the bank letter of commitment rather than the direct letter of commitment except for CIP and project commodity financing for which the mission anticipates a proliferation of invoices.

Discussion:

Agency experience indicates that greater accountability is achieved where certain methods of financing are selected, while other methods tend to increase the agency's vulnerability. This is one reason Policy Statement 3 dictates a preference for three specific modes of payment. Another reason is Agency and USG cash management policies which aim to minimize advances and defer payments as long as possible, i.e. until all work is completed or goods and services delivered. As programmatic considerations sometimes dictate methods of financing that are less preferable from a vulnerability or cash management standpoint, flat prohibitions are not feasible. However, to ensure the maximum compliance, it is essential that a decision to utilize other methods be fully justified.

5. Where host country contracting is proposed as a means of implementation, the assessments required under 1. above must set forth a realistic appraisal of the prospective contracting agency's ability to (a) advertise, award and negotiate contracts, (b) monitor contract implementation, (c) examine invoices and (d) audit contractor records and reports. If local currency is to be made available to an ICI or to any other organization responsible for controlling and reporting on the use of such funds, the mission

should first assess the organization's financial management procedures and related internal controls. Such an assessment should also be performed as a prerequisite for providing grants to indigenous PVOs. Subsequent audit or evaluation reporting on the project should measure performance in reference to the assessments made under 1. above, as well as other appropriate factors.

Discussion:

It is desirable for the agency to utilize the host country contract means of implementation, whenever appropriate, in light of its developmental institution building effect and establishment of permanent U.S.-host country commercial channels. Considerations of accountability and overall management effectiveness are vital in determining the appropriateness of the use of host country contracting in a particular case. The capacity of the host country and its implementing agencies must be realistically assessed as a part of the planning process. Similar considerations apply where local currency is to be made available to an ICI or any other organization (e.g., grants to indigenous PVOs) responsible for controlling and reporting on the use of such funds.

Implementing Guidelines

1. General Assessments:

In conjunction with the annual review of mission internal controls, the USAID should prepare a general assessment of methods of implementation and financing procedures used by the USAID. The first such assessment should cover all existing and planned projects and programs. The mission should review and update this first assessment annually. The annual update will involve minimal effort except when missions undertake substantial changes in the way they do business.

In order to assist in developing the general assessment we have attached a matrix entitled "AID Payment Process". This matrix relates various types of assistance with methods of implementation and methods of payment.

The title of the general assessment will be "Mission Financing Policy and Procedures"; the assessment will be in narrative form. The initial report as of December 31, 1983 will be due in AID/W (copies to M/FM and cognizant Regional Bureau) on March 31, 1984.

Thereafter, annual updates will be due by December 31st. The body of the general assessment should be limited to ten pages; charts, schedules and backup material may be attached as annexes. The narrative should be in the following format:

(a) Summary statement of methods of implementation and financing used by the USAID in its current and planned program. The summary should include a chart of all methods of implementation used in the USAID program and the various methods of financing used for each method of implementation (see "AID Payment Process" matrix for guidance). While some may wish to quantify these methods in numbers and dollar amounts, it is not required in the assessment. A narrative, general description of these methods in the USAID/host country context should also be included in this section and should contain an explanation of how USAID practices differ from those indicated on the "AID Payment Process" matrix.

(b) Justification for methods of financing used if other than Fixed Amount Reimbursement, Federal Reserve Letters of Credit and direct payment/ reimbursement. Include separate justification for the proposed use of Bank Letters of Commitment as outlined in Policy Statement No. 4.

If the exercise outlined in Section (a) above results in methods of payment other than the three methods indicated in Policy Statement No. 3, a specific justification must be provided for each. This justification should include a description of procedures which the USAID intends to use to minimize the vulnerability of the selected methods of financing.

(c) Overall assessments of the procedures used by the host country government for contracting, commodity procurement and payment verification (voucher review). This section should also address the adequacy of the accounting systems of the implementing agencies of the host government and their arrival accounting systems if CIP programs are part of the USAID assistance package.

While some host country governments have centralized these functions, others leave such functions with each implementing agency. As a result there will be a range of difficulty in complying with this policy directive. For those USAIDs where the functions are decentralized it is expected that this review will be completed over time and that the first assessment will indicate the results of a sample test of agencies. Later assessment updates will then indicate differences from the original assessment as a result of the continuing review process. It has been assumed that the Mission Controllers assessments under Policy Statements No. 8 and 9 (see pages 17 and 18) will assist the USAIDs in general assessment of this area.

2. Project Papers and Program Assistance Approval Documents:

Each and every PP/PAAD, whether for AID/W or field authorization, will include as part of the financial analysis section a detailed assessment of the methods of implementation and financing of the proposed activity. The assessment should refer to the general assessment discussed in 1. above and provide detailed justification for departures from the general assessment concurrence by AID/W as a result of the annual submission of the "Mission Financing Policy and Procedures."

The approval of this section of the PP/PAAD will provide the basic approval for later issuance of financing documents such as Bank Letters of Commitment and Federal Reserve Letters of Credit requested by the USAIDs during project implementation. As indicated in Policy Statement No. 2 the AID/W Controller will review and provide his concurrence of this section of the PPs/PAADs submitted to AID/W. Additionally he will provide a delegation of authority to the Mission Controllers to require their review and concurrence for those PPs/PAADs approved in the field as well as those submitted to AID/W. In order to facilitate the AID/W review process the USAID Controller concurrence should appear on the Project Data Sheet attached to the PP and on the face sheet of the PAAD.

The methods of implementation and financing section of the PP/PAAD should be presented in the following general format:

(a) As in the general assessment a chart should be prepared indicating all methods of implementation to be used in the proposed project/program and the various methods of financing under each. This chart should include approximate dollar amounts by method of implementation and by method of financing. The following is an illustrative example:

Methods of Implementation and Financing
(Illustrative example)

Method of Implementation	Method of Financing	Approximate Amount (U.S. $000)
TA - HC Institut. Contract	Direct L/Com	5,000
	HC Reimb.	500
	Bank L/Com	1,500
		7,000
TA - HC-PSCs	Direct Pay	300
Construct. - Schools	Fixed Amount Reimbursement	13,000
Commod. - AID Proc. Proc. Agt. Contracts	Bank L/Com	6,000
	Direct L/Com	2,000
		8,000
Commod. - HC Proc. Purch. Orders	HC Reimb.	500
	Direct pay	500
		1,000
Total Project		29,300

(b) This section should provide a narrative justification for departures from the three financing alternatives outlined in 3. above. The financing methods which would need justification in the example in (a) above are direct L/Com, and bank L/Com. If these methods had been previously approved in the general assessment the justifications should merely indicate how the financing methods in this project/program meet the criteria provided in the general assessment or, if they differ, discuss the new set of circumstances under which they should be approved.

Again the justification should include if applicable procedures which the USAID intends to use to improve on the vulnerability of the methods of payment chosen and/or on weaknesses mentioned in the general assessment. For instance, if the method chosen is direct L/Com issued by the Mission Controller under a host country contract for technical services, the justification might be simply that the host country does not have the financial resources to make payment and seek daily reimbursement from AID. References should be made to section c. of the general assessments and the Mission Controller analysis (section II.C. below) of the USAID voucher review process.

(c) A detailed explanation and assessment of the host country government's specific procedures for contracting, commodity procurement and payment verification, if applicable, should be provided in this section. Again, if a CIP is proposed, the procedures by which commodities will be tracked (through an arrival accounting system) should be discussed. The requirements of this section would likely involve a review of the procedures followed in the implementing agency(s) of the project/program.

The USAID should keep track of the methods of implementation and financing included in PPs/PAADs not previously discussed in the general assessments (Mission Financing Policy and Procedures) for assistance in preparing the annual updates to the general assessments.

It is recognized that occasions may arise subsequent to the PP/PAAD submission and approval stage, where it becomes necessary for the mission to consider altering the financial implementation plan. If this occurs, the USAID should, by immediate cable submit PP/PAAD amendment to Washington outlining the nature of and justification for such change. If no response is received from Washington within ten days of the cable submission, the USAID can assume Washington approval.

II. Policies to Strengthen Verification, Auditing and Other Monitoring Procedures.

As various degrees of verification are associated with particular methods of financing, the initial choice of method under the procedures described in "I.A." will often contribute to overall accountability. (For example, the direct letter of commitment procedure will ensure AID voucher review, while a bank letter of commitment will not.) While such choices will in and of themselves increase or decrease vulnerability since they influence the level of AID involvement, it will be in the day-to-day exercise of oversight that accountability can be improved. Where responsibility for administration is shared, as in the case of host country contracts, AID's accountability for the use of taxpayers' funds nevertheless remains. Given the scarcity of resources, it is essential that the Agency increase provision for monitoring as an integral part of its operations. To that end, a number of new procedures are advisable in the interest of strengthening accountability and reducing vulnerability, without imposing unrealistic burdens on AID personnel.

A. Provision for audit as part of the project planning process. Assessments regarding the choice of method of financing or method of implementation, as in the case of host country contracting, will often dictate the degree and means of appropriate audit coverage.

1. Policy Statement No. 6:

PPs are to include an evaluation of the need for audit coverage in light of potential risks and are to describe planned contract and project audit coverage by the host government, AID, and/or independent public accountants. Project funds should be budgeted for independent audits unless adequate audit coverage by the host country is reasonably assured or audits by third parties are not warranted as, for example, in the case of direct AID contracts or direct placement of participants by AID.

2. Implementing Guidelines:

(To be provided later in coordination with the IG.)

B. Basis for AID project officers administrative approval of vouchers and other certifying instruments: In the administrative approval of vouchers, a project officer is currently required to state that he/she knows of no reason why the voucher should not be approved. This statement falls short of the positive statement that would be desirable, were supporting resources fully available throughout AID's operations. On the other hand, since it does not reveal the basis for the approval, the current "negative" sign-off suggests that much less is being done in the way of monitoring than is or should be the case. For informed management of its resources, it is essential that the agency know the basis upon which funds are being approved.

1. Policy Statement No. 7:

In lieu of the current negative statement, the project officer is to provide to the Controller a statement advising of the basis upon which administrative approval is given.

2. Implementing Guidelines:

The purpose of the administrative approval of any voucher is to provide the authorized certifying officer with notice that the officer responsible for charges billed to the government for services, commodities or other costs considers that these charges represent actual performance, delivery or other benefits received. A project officer will rarely have full knowledge of all services performed in a billing period by a contractor. The project officer performs an important function in administratively approving a contractor's invoice if she/he (1) has reasonable knowledge of contractor activities or other project activites which result in costs billed to AID and (2) reviews the voucher for the level of contractor effort charged during the period, types and general quantities of locally procured commodities delivered during the period and other costs which are reasonably familiar to the project officer because of his or her role as a monitor of project implementation. Internal control of the payments made by AID diminishes if project officers are unable to relate observed project implementation to costs billed in related vouchers.

In order to provide a more complete documentary tracking of project payments, the project officer will now, in addition to providing the project officer administrative approval of vouchers, complete and attach the following checklist to the voucher. This will provide the authorized certifying officer with a more thorough knowledge of the relative vulnerability of each payment. The checklist is not intended to be used as a substitute for the current project officer approval statement(s), but merely as a clarifying addendum. The checklist is as follows:

ficer Checklist for Administrative Approval of Vouchers

(Please check as many as are applicable)

1. I have made ____ field visits to the project site(s) in the last three months and have personally observed project implementation _____

2. I have visited the main office of the implementing agency(ies) ____ times in the last three months and discussed project implementation _____

3. I met with my counterpart(s) ____ time in the last three months and discussed contractor level of performance and/or commodities delivered _____

4. I have visited the project site(s) as part of my Project Officer responsibilities and have sufficient information to enable me to provide an administrative approval _____

5. None of the above. My administrative approval is based on the following: (Please be concise, i.e., two or three sentences.)

_____
Project Officer Name

_____
Project Number

C. Assessments of mission voucher and voucher approval examination procedures: To ensure accountability and other implementation planning objectives, it is important that AID/Washington be aware of the extent of monitoring procedures carried out by missions, as well as by host countries.

1. Policy Statement No. 8:

Mission controllers are responsible for providing annual assessments of the mission voucher approval and voucher examination procedures. Such assessments should indicate the adequacy of supporting documents submitted with contractor invoices and the ability of project officers and authorized certifying officers to relate contractor performance with contractor invoices.

2. Implementing Guidelines:

The annual review called for under this policy directive is designed to formalize a process which should already be in place. The review should involve a randomly selected sample of vouchers large enough to provide reasonable assurance that the voucher approval and

examination procedures in place are adequately represented by the assessment. A flow chart of the vouchering and paying process should accompany the assessment so that points brought out in the assessment can be related to the actual flow of documents and procedures. Areas of special concern to the controller as well as procedures which indicate relatively high vulnerability should be highlighted in the assessment. Projected solutions or changes in procedures which will result in decreasing vulnerability should be indicated. The review should be submitted with the annual Mission Financing Policy and Procedures Assessment.

D. Annual assessments of the monitoring and invoice examination procedures followed by host country contracting agencies: In addition to the general and project specific assessments of host country and contracting agency capacity as a part of the planning process, it is important that AID be assured of the continuance of this capability and performance over time to support its reliance upon host country performance certificates and voucher reviews.

1. Policy Statement No. 9

Mission controllers are to provide annual assessments of the adequacy of the monitoring and invoice examination procedures followed by host country contracting agencies. Such assessments should serve as the basis for reliance on host country performance certificates and voucher reviews.

2. Implementing Guidelines:

As a part of the assessment provided under Policy Statement No. 8 the controller should include an assessment of the host country government's project monitoring and voucher review process using the same general guidelines. For USAIDs where these processes are scattered throughout many host country agencies the first annual assessment may include reviews of only a few, especially where procedures differ substantially. The annual updates will then include additional agencies until all have eventually been reviewed. An additional area which should be highlighted is the problem of bottlenecks in the vouchering and paying process within the host country agencies.

E. Methods of Monitoring and Auditing: Given AID's limited financial management and auditing resources generally, USAID controllers should utilize more frequently the services of competent public accounting firms in providing accounting and financial management technical services and in auditing host country contracts as well as designated direct contracts and grants. Also, to strengthen voucher examination, controllers should be encouraged to use contract personnel to supplement direct-hire foreign nationals.

1. Policy Statement No. 10:

(a) USAID controllers are encouraged to utilize the services of competent public accounting firms to a greater degree in providing accounting and financial management consulting services within the project design as a part of program funding and in auditing host country contracts. Auditing services will be conducted on the basis of pre-approval by the Inspector General staff.

(b) In their areas of responsibility, USAID controllers are encouraged to use contract personnel to supplement direct-hire foreign nationals for voucher examinations.

2. Implementing Guidelines:

Both sections of this Policy Statement are self-explanatory. However, when using contract personnel to provide voucher examination, procedures will need to be adopted which will limit internal control vulnerability.

Bureaus, REDSOs and even larger missions are encouraged to set up IQCs using PD&S funds to provide accounting and financial consulting services early in the life of a project.

III. Policies related to specific other practices which will contribute to accountability:

A Commodity Price Analysis

1. Policy Statement No. 11:

The agency's commodity price analysis function should be strengthened to permit more adequate pre- or post-payment audit of commodity costs.

2. Implementating Guidelines:

AID/W action. (M/SER/COM)

B. Incentive Contracts

1. Policy Statement No. 12:

Where suitable and subject to Federal and AID control guidelines, the agency should place greater reliance upon incentive contract approaches, where contractors share in savings or receive extra benefits for timely completion.

2. Implementating Guidelines:

AID/W action (M/SER/CM). Comments and examples from the field would be helpful and are hereby requested.

C. Host Country Contracts - submission of invoices

1. Policy Statement No. 13:

Host country contracts should include definitive requirements for submission of invoices and supporting documents.

2. Implementing Guidelines:

Further AID/W (M/FM) action is needed to provide world-wide implementing guidelines. However, USAID's will be able to begin implementation based on their reviews of host country voucher examination procedures peculiar to each country.

D. Expanded application of the Fixed Amount Reimbursement concept.

1. Policy Statement No. 14:

Models for use of the Fixed Amount Reimbursement concept for non-construction projects should be developed for consideration.

2. Implementing Guidelines:

While formulation of specific guidance on this policy is for AID/W (PPC and M/FM) action many USAID's have already designed and implemented Fixed Amount Reimbursement procedures for non-construction projects. In order to assist AID/W it is requested that USAID's transmit to AID/W examples of expanded uses of Fixed Amount Reimbursement and any suggestions which may be helpful.

E. CIP arrival accounting:

1. Policy Statement No. 15:

Definitive requirements for arrival accounting should be developed and published for CIP programs. Assessments of arrival accounting systems should be included in all CIP approval documents (PAADs).

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2. Implementing Guidelines:

While AID has increased its level of CIP financing the attention paid to arrival accounting has not been consistent. All USAID's with existing or planned CIP programs should evaluate host country arrival accounting as part of the overall evaluation and for inclusion in the PAAD's requesting future CIP authorizations. If missions cannot positively attest to the adequacy of host country systems, they must provide a satisfactory alternative. For additional guidance, USAID's should review Handbook 15, Chapter 10. (Excellent examples of tracking systems can be found in Manual Order 754.6 until the handbooks are revised.)

AID/W (M/FM) will be providing more specific guidance in the near future.

F. Two-step loan agreements:

1. Policy Statement No. 16:

The agency will explore resuming use of formal two-step loan agreements given the increased emphasis on private sector participation.

2. Implementing Guidelines:

AID/W action (PPC). Guidance will be provided as developed.

UNITED STATES AGENCY for INTERNATIONAL DEVELOPMENT

USAID EGYPT

May 20, 1987

MEMORANDUM

TO: Joseph R. Ferri, RIG/A/Cairo

FROM: William A. Miller, AD/FM

SUBJECT: Draft Audit Report: USAID/Egypt's Implementation of AID's Payment Verification Policy

As a preface to our comments on the revised draft audit we are pleased that you have taken into consideration several of our suggestions regarding rewording and have incorporated into the report actions taken by the mission subsequent to the audit cut-off date. The draft report in our view is now much more balanced.

We do however want to make some general observations on the overall report as well as specific comments on the recommendations.

In general we feel that the report could convey a false impression of overall fiscal operations by overstating deficiencies and the omission of accomplishments during and since the audit. Examples of our exceptions to the report are:

- It is not reasonable to contend that agency assessments are the panacea to resolve the endemic problems of project implementation in Egypt. (See Item 1, Office of Inspector General Footnotes)
- Numerous audit findings from prior audits by RIG/A/Cairo are woven through this report despite the report noting that all such recomendations have been satisfactorily closed. (See Item 2, Office of Inspector General Footnotes)
- The methodology used to impute interest costs is not statistically valid because it is built on a judgmental selection of 10 vouchers out of a universe of 9,000 vouchers. (See Item 3, Office of Inspector General Footnotes)

- Failure to reduce properly obligated funds and to maintain appropriate accounting classifications does not constitute invalid obligations. (See Item 4, Office of Inspector General Footnotes)

Findings and Recommendations

USAID/Egypt supports the desirability of the seven audit recommendations but we wish to comment on each recommendation:

Recommendation # 1 (See Office of Inspector General Comments, Page 26)

USAID/Egypt believes that agency assessments have now been assigned proper priority within Mission work requirements. Assessments were designated as the primary, specific objective for Financial Analysts for the June' 86 to May' 87 rating period. Analysts are devoting over 50 % of their time to performing assessments.

USAID/Egypt believes that its schedule to perform 22 assessments over a two year period beginning June 86 is reasonable. The Mission is meeting this schedule (6 assessments fully completed; 3 partially completed).

This recommendation should be closed upon issuance.

Recommendations # 2 (See Office of Inspector General Comments, Page 26)

An assessment of USAID/Egypt's voucher approval and voucher examination process has been scheduled for June 1987.

Recommendations # 3 (See Office of Inspector General Comments, Page 26)

Voucher Examiners do use contract abstracts to review payment vouchers. The abstracts consist of photocopies of contract payment terms with important provisions further highlighted. Our experience has shown that this procedure is more efficient and effective than preparing separate contract abstract documents.

In order to clarify general financial reporting requirements, the Mission issued a letter on this subject to all existing contractors approximately two years ago. Although no contractors took exception to this letter, the Mission feels that the better course of action is to ensure that contract provisions are proper and comprehensive. Contractors are advised as necessary concerning appropriate reporting procedures in accordance with the terms and conditions of the specific contracts.

USAID/Egypt has been fully complying with the requirement to examine vouchers according to contract terms by use of contract abstracts. This recommendation should be closed upon issuance.

Recommendation # 4 (See Office of Inspector General Comments, Page 26)

Financial Analysts, as members of Project Committees, prepare the recommended formats and charts for inclusion in project papers and other documents to report on methods of implementation and financing, host country contracting capabilities, audit coverage needs and other policy issues. A standard format has been developed which meets the requirements of the Policy Statement. All seven FY-87 project papers prepared to date have contained appropriate financial analysis documentation.

This recommendation should be closed upon issuance.

Recommendation # 5 (See Office of Inspector General Comments, Page 26)

The Mission has been conducting Project Officers training courses for the last three years that include instructions on procedures for processing vouchers. These procedures are well defined in Handbook 3, the Project Officers Guidebook, and Handbook 19. AID Washington has recently issued a clarification to the "Criteria for Project Officers Administrative Approval.

USAID/Egypt believes that sufficient documentation has been issued to define the role of project officers in processing vouchers and that the Mission has taken all reasonable steps to implement such instructions.

This recommendation should be closed upon issuance.

Recommendation # 6 (See Office of Inspector General Comments, Page 26)

At the end of FY-86 the Mission conducted a comprehensive evaluation of the voucher payment process. Since the begining of FY-87 the Voucher Examination Section has been reorganized, new procedures have been instituted and a new computerized Voucher Control and Prompt Payment (VOUCAPP) system has been developed and implemented.

USAID/Egypt is now better able to control the processing of vouchers in relation to properly determined due dates. VOUCAPP includes procedures and management reports which ensure that all 9,000 vouchers received in a fiscal year are examined on a timely basis and tracked from receipt through final disposition.

This recommendation should be closed upon issuance.

Recommendation # 7 (See Office of Inspector General Comments, Page 26)

Provisional overhead rates are normally adjusted on the basis of audits performed by the cognizant audit agency, in many cases the Defense Contract.

Audit Agency (DCAA). DCAA overhead audits usually result in the provisional overhead rates being increased. Since the U.S. Government is not damaged by a delay in the adjustment of these rates, USAID/Egypt advises the parties to host country contracts to finalize the rates as expeditiously as possible according to contract terms and works with GOE agencies to do so.

This recommendation should be closed upon issuance.

Flawed Methodology - Audit Sample (See Item 5, Office of Inspector General Footnotes)

We believe the audit sample of vouchers paid does not support the contention that "most vouchers tested were either paid late or before due":

- The statement is based upon a judgmental review of 10 vouchers.
  - .. 3 of the 10 were cited as paid early according to prompt payment guidelines.
  - .. 5 were cited as paid late according to RIG/A/Cairo assumptions.
  - .. 2 were cited as paid appropriately.
- The random audit sample consisted of 111 vouchers - not 10 nor 39.
- Less than 3 % of the 111 vouchers sampled were identified as paid inappropriately according to US government regulations.

The audit sample does not support the projection of $340,000 of imputed interest:

- Only $4,695 of imputed interest was specifically identified based upon 3 vouchers.
- The $340,000 estimate resulted from a rework of calculations which originally estimated a range of $1.6 million to $3.3 million from the same sample.
- It is questionable whether the 10 judgmentally selected vouchers are truly representative of the universe of 9,000 vouchers processed during FY 86.

Office Of Inspector General Footnotes To Mission Response To Draft Report

1. Assessments are required by agency policy and should be done. Agency assessments, however, are not panaceas for resolving all the problems in Egypt. The report doesn't say that, nor do we believe this to be the case. Assessments can identify shortcomings in Mission operations and in the areas effecting projects. Once the problems are identified, work can start on how to correct them or to avoid them. Assessments of host country agencies provide information on which to base informed decisions on the contracting and financing modes.

2. The use of past audit findings in the report was meant to indicate the type and nature of management problems in the payment verification area. Although corrective action was responsive on issued reports, proper assessments could have disclosed the problems at a much earlier point in time and the problems could have been resolved by the Mission prior to the audits.

3. The methodology used to select the sample and to project a rough estimate of interest costs for fiscal year 1986, was valid. A sample was drawn, statistically, from payment records in USAID/Egypt's accounting section. In the 4 months of fiscal year 1986 activity selected for examination, there were 2,451 payment vouchers. Of these 2,451 payments, 111 payment vouchers totaling $7.4 million were judgementally selected for further examination. The 111 represented every 22nd item during the 4-month period. Of the 111 vouchers, 39 vouchers represented actual payments to vendors. Of the 39 vouchers, 10 vouchers were judgementally selected for detailed examination. The 10 vouchers totaled $5.3 million; or 91 percent of the value of the 39 vouchers subject to prompt payment act standards. In our opinion, the methodology used provided a reasonable basis for projecting a rough calculation of the unnecessary interest costs due to the early payment of vouchers.

4. Recorded obligations are required to be certified annually by the Mission Controller. The assumption is that obligations so certified represent valid, binding commitments of the U.S. Government. When the Mission rolls

the remaining funds of past liquidation actions into suspense accounts, as it did, or certifies obligations that no longer represent valid and binding commitments, the remaining balances cannot be passed off as a function of poor accounting practice. These balances are invalid obligations as stated in the report.

5. The audit sample supports a finding that most vouchers tested were either paid late or before due. The projection of $340 thousand in unnecessary interest costs, based on three vouchers, is considered a reasonable calculation of the cost of paying vouchers before the due dates. Of the 10 payments in the sample, eight vouchers were paid either early or late. The cost of interest, at 9 percent, for early payment of the 3 vouchers in the sample, was $4,695. The estimated cost of early payments for fiscal year 1986 of $340,000 was projected by dividing the $4,695 by the 91 percent dollar value tested, times the sample interval of 22, times 3 periods in the year, or $340.5 thousand. Due to the small number of early payments the projected interest cost should be viewed as an approximation. The actual amount could be much greater or less. The point remains, however, that the Mission lacked an adequate system for knowing when to pay vouchers on time. It has now taken corrective action on this matter.

LIST OF RECOMMENDATIONS

Page

Recommendation No. 1 5

We recommend that USAID/Egypt assign a high priority to assessing the capabilities and systems used by individual host country contracting and local currency implementation entities, in accordance with AID Payment Verification Policy statements and guidance. USAID/Egypt should ensure initial coverage of all entities within a reasonable period. Assessments should include recommendations for improving conditions, controls, accounting, reporting, eliminating bottlenecks, or changing methods of implementation and financing.

Recommendation No. 2 6

We recommend that the USAID/Egypt Controller's staff in carrying out annual assessments of USAID/Egypt's voucher approval and voucher examination processes, include representative samples of vouchers as set forth in the Policy.

Recommendation No. 3 6

We recommend that USAID/Egypt require that voucher examiners prepare and use contract abstracts and letters to contractors for revised invoice detail requirements as set forth by the USAID/Egypt Controller.

Recommendation No. 4 6

We recommend that USAID/Egypt require Mission officials, in preparing project papers and Program Assistance Approval Documents, to use designated formats and charts for reporting on methods of implementation and financing, host country capabilities, audit coverage needs and other Policy issues.

Recommendation No. 5 6

We recommend that USAID/Egypt issue instructions to clarify the role of project officers in the proper procedures for processing vouchers for payment and in requesting disallowances under host country contracts.

Recommendation No. 6 6

We recommend that USAID/Egypt continue working to establish a system for paying vouchers as closely as administratively possible to due dates determined in accordance with contract terms, AID Handbook 19, Appendix 1C and Prompt Payment Act standards.

Recommendation No. 7 6

We recommend that USAID/Egypt assist host country contracting agencies to finalize the actual overhead rates for periods audited for Contract No. 263-0045-03.

APPENDIX 4

REPORT DISTRIBUTION

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