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AUDIT OF
THE WATER SUPPLY AND SANITATION
SECTOR PROJECT IN SRI LANKA
PROJECT NO. 383-0088

AUDIT REPORT NO. 5-383-89-2
February 20, 1989

AGENCY FOR INTERNATIONAL DEVELOPMENT
OFFICE OF THE REGIONAL INSPECTOR GENERAL FOR AUDIT
- Singapore -

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February 20, 1989

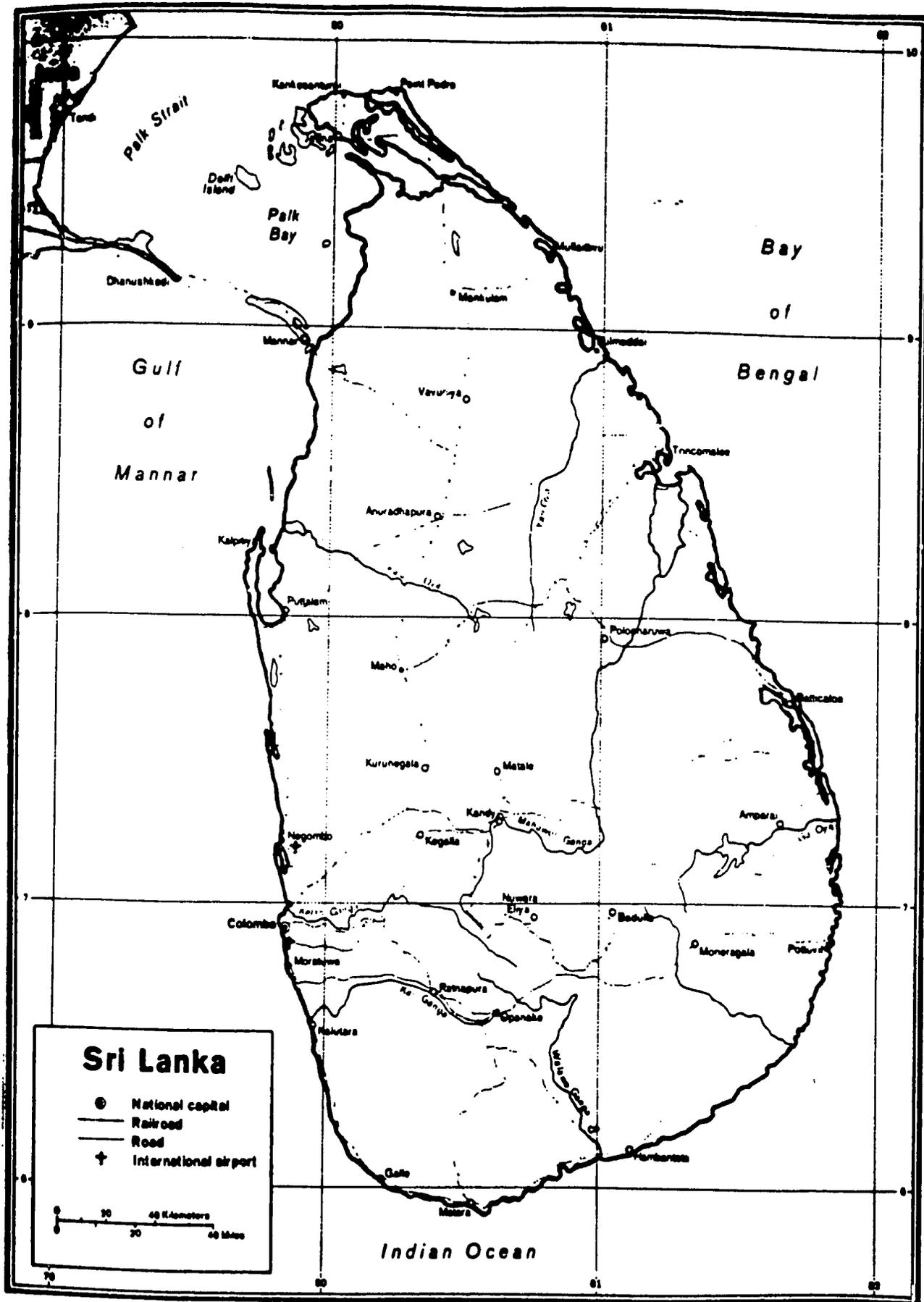
MEMORANDUM FOR Peter Bloom
Director, USAID/Sri Lanka
FROM *B. Howard*
Reginald Howard, RIG/A/Singapore
SUBJECT Audit of the Water Supply and Sanitation
Sector Project in Sri Lanka, Project No.
383-0088 (Audit Report No. 5-383-89-2)

The Office of the Regional Inspector General for Audit/Singapore has completed its audit of the USAID/Sri Lanka Water Supply and Sanitation Sector Project No. 383-0088. Five copies of the audit are enclosed for your action.

Your comments to the draft report are summarized after each finding and included in their entirety as an appendix to this report. Based on your comments, all of Recommendation Nos. 1 and 2 and parts (a) and (c) of Recommendation No. 3, are resolved and will be closed when the agreed to action is completed. Part (b) of Recommendation No. 3 is closed and no further documentation need be provided. Please advise me within 30 days of the additional actions taken to implement the resolved recommendations.

I appreciate the cooperation and courtesy extended to my staff during the audit.

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EXECUTIVE SUMMARY

The Water Supply and Sanitation Sector Project in Sri Lanka was approved in August 1984. A.I.D. was to provide \$12.3 million for this project and the Government of Sri Lanka \$7.3 million. The objectives were to strengthen the institutional capabilities of the National Water Supply and Drainage Board and to improve health education.

Political problems in Sri Lanka and local resistance to the restructuring of the Water Board placed constraints on project achievements. Consequently, although the project was to be nearing completion, only \$5.2 of the \$12.3 million had been expended.

Our office made a performance audit to determine whether project objectives were being met, funds were efficiently and effectively spent, host country contributions were adequate, mid-term project evaluation recommendations were resolved, and management control systems were adequate. While no reportable findings were noted in these last two areas, the audit did disclose that:

- The Mission could not assess project accomplishments because:
 - . quantitative indicators were not clearly established.
 - . target dates for completing tasks were not fixed.

- Over \$1 million of funds used to purchase commodities were not used effectively and efficiently because:
 - . planned construction was behind schedule.
 - . insurance claims were not filed for missing and damaged items.
 - . inspection and inventory of commodities was not adequate.
 - . commodities needed repairs and were improperly stored.

- Host country contributions were not adequately monitored since:
 - . only about \$1.1 million of the \$7.3 million required had been provided to date.
 - . about \$198,000 of the \$1.1 million reported was unallowable.

To correct these problems, recommendations were made to improve the monitoring and reporting of specific quantitative indicators, increase controls of project commodities, and strengthen oversight over host country contributions. Management officials generally concurred. Their comments are summarized after each finding and presented in their entirety as Appendix A to this report.

Office of the Inspector General

AUDIT OF
THE WATER SUPPLY AND SANITATION
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PROJECT NO. 383-0088

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THE WATER SUPPLY AND SANITATION
SECTOR PROJECT IN SRI LANKA
PROJECT NO. 383-0088

PART I - INTRODUCTION

A. Background

The objectives of the Water Supply and Sanitation Sector Project were to strengthen the National Water Supply and Drainage Board's institutional capabilities, improve health education, and increase community participation. Project outputs were to include a revised organizational structure for the Water Board; construction and renovation of workshops, offices, and other facilities; and construction or rehabilitation of six water schemes.

The project was approved on August 24, 1984 and was to be completed by August 31, 1989. The total estimated cost of the project was \$19.6 million, with A.I.D. and the Government of Sri Lanka providing \$12.3 million and \$7.3 million, respectively. A.I.D. had disbursed about \$5.2 million as of September 30, 1988. As shown below, most of A.I.D. funds were to pay for technical assistance, construction/rehabilitation of water schemes, commodities, and facility construction.

A.I.D. Obligations and Expenditures
As of September 30, 1988 (in \$000)

<u>Budget Category</u>	<u>Obligations</u>	<u>Disbursements</u>
Technical Assistance	\$ 4,810	\$ 3,810
Construction/Rehabilitation	2,910	29
Commodities	2,235	1,074
Facilities	1,700	82
Training	570	145
Research Studies	<u>75</u>	<u>10</u>
 Total	 \$ 12,300 =====	 \$ 5,150 =====

The National Water Supply and Drainage Board was responsible for day-to-day project management. An A.I.D. funded technical assistance contractor was to assist in achieving the project objectives. USAID/Sri Lanka was to monitor project implementation to ensure the effective and efficient use of A.I.D. funds, and compliance with the terms and conditions of the project agreement.

B. Audit Objectives and Scope

The Office of the Regional Inspector General for Audit/Singapore made a performance audit of the project. Audit objectives to determine whether (1) the project objectives were being accomplished; (2) A.I.D. funds were efficiently and effectively spent for technical assistance, commodities, and facility construction; (3) the Government of Sri Lanka provided its required financial contributions; (4) recommendations in the mid-term project evaluation were appropriately resolved and implemented; and (5) management controls systems were adequate.

Audit work included reviews of project records and interviews with responsible officials of USAID/Sri Lanka, the National Water Supply and Drainage Board, and the project technical assistance contractor. Project commodities were inspected at only two locations due to security problems in Sri Lanka. Review of internal controls, compliance, and host country contributions were limited to the issues raised in this report.

The audit was performed during the period August through October 1988. It covered the period from inception (August 24, 1984) to October 28, 1988 and reviewed A.I.D. expenditures of \$5.2 million. The audit was made in accordance with generally accepted government audit standards.

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PART II - RESULTS OF AUDIT

The Water Supply and Sanitation Sector Project primary objectives were institutional restructuring of the National Water Supply and Drainage Board and construction/renovation of facilities. Due to political problems within the Government of Sri Lanka, there were certain understandable constraints on the achievement of these objectives. Also, delays were initially encountered because of local resistance to the proposed restructuring of the Water Board. Consequently, the project was significantly behind schedule. In fact, construction and renovation of water schemes and facilities had been delayed and little A.I.D. funds had yet been spent on these activities. As of September 30, 1988, only \$6.2 of the \$19.6 million (includes A.I.D. and Government of Sri Lanka funds) planned for this project had been used.

While the management control systems were generally adequate and the funds which were spent were generally proper, USAID/Sri Lanka project management could make certain improvements. For example, progress in achieving the project objectives could not be accurately measured in some areas because consistent quantitative indicators were not used. Also, controls over project commodities could be improved and host country contributions were behind schedule. While not reported as a finding, it was noted that mid-term evaluation recommendations were not adequately resolved/implemented, and an overhead audit of the technical assistance contractor was needed.

The report recommended actions to improve the monitoring and reporting on specific quantitative indicators, increase the controls over project commodities, and strengthen oversight of host country contributions.

A. Findings And Recommendations

1. Monitoring and Reporting on Project Achievements Needed Improvements

USAID/Sri Lanka was not obtaining adequate information to measure certain of the project achievements. This occurred because the Mission needed to better determine the indicators used to measure achievements and establish meaningful target dates for completing tasks. Such information was required by the Foreign Assistance Act, the Office of Management and Budget, as well as the A.I.D. Handbook. Lacking this information, the Mission's ability to effectively monitor the project was reduced.

Recommendation No. 1

We recommend that USAID/Sri Lanka:

- a. in coordination with the Government of Sri Lanka and the technical assistance contractor establish quantitative indicators with realistic target dates to measure project achievements; and
- b. require the technical assistance contractor to accurately report the progress in achieving each indicator, identify progress problems and offer solutions, and justify changes in target dates and indicators.

Discussion

Various quantitative indicators were mentioned in the project paper, the USAID quarterly implementation reports, and other documents. However, there was no consistency between these documents regarding the indicators used to monitor project accomplishments. Also, indicators were frequently changed with little or no explanation.

The Foreign Assistance Act, Office of Management and Budget Circular A-117, and A.I.D. Handbook 3 all require a management system that includes quantitative indicators to measure the progress of a project. The Handbook also specifically states that there must be a reporting system

which keeps all parties advised of the current status of project activities and deviations from the plans.

For some of the project elements, these requirements were not adequately met. This occurred because the Mission did not determine which indicators were to be systematically used to monitor project activity and measure accomplishments. Consequently, as shown below, there was no consistency as to the number of indicators which were used.

<u>Source</u>	<u>Number of Indicators</u>
Project Paper	14
Quarterly Project Implementation Reports	10
Contractor's Progress Reports	11
Contractor's Proposal for Contract Extension	11
Annual Project Reviews	9
Mid-Term Evaluation	10

While some of these indicators were similar in nature, there was only limited consistency as to the specific type used. Instead, the various participants determined which indicators they believed should be measured and reported. For example, the consultants for the annual project reviews used an indicator for water quality and process control. This indicator, however, was not used in the Mission Quarterly Project Implementation Reports or the technical assistance contractor's progress reports.

In order to provide more meaningful information on the status of the project, it is important to use uniform indicators. Since neither the number nor the type of indicators were consistently used, the Mission's ability to effectively monitor the project was reduced.

Realistic dates for accomplishing the various tasks were also not established. For example, one of the indicators used by the technical assistance contractor was to finalize an in-country program for A.I.D. training funds. The technical assistance contractor's progress report frequently changed the target dates for accomplishing this item shown as follows:

<u>Quarterly Report</u>	<u>Planned Date For Completion</u>
December 1986	February 28, 1987
March 1987	April 30, 1987
June 1987	July 31, 1987
September 1987	September 30, 1987
December 1987	January 31, 1988
March 1988	May 31, 1988
May 1988	July 31, 1988

Up to and including the May 31, 1988 progress report, the technical assistance contractor stated that all required activities except construction would be completed by December 1988. However, just a few months later (August) his progress report extended the completion dates to September 1990. He also submitted a proposal in August stating a two year extension to his contract was necessary, and noted that even this extension may not be adequate to ensure attainment of all the required tasks. (The estimated cost for the two-year extension was \$1.3 million.) Such significant changes in a short period of time detracts from the usefulness of the reports.

The above is typical of the changes made to the indicators without any explanations. Therefore, planned completion dates which should be important and carefully monitored became meaningless.

The usefulness of the contractor's progress reports to USAID was also reduced because quantitative indicators were frequently added or deleted with little or no comment. To illustrate, the report as of May 31, 1988 included 11 training tasks which were deleted from the August report. All of these tasks were deleted without completion. On the other hand, the August report included 28 training tasks which were not included in the May report. No explanation was given for these changes. Because of the importance of measuring the progress of a project, the Mission should be more actively involved in these modifications.

The lack of specific indicators with realistic target dates also mitigated the usefulness of USAID/Sri Lanka's Quarterly Project Implementation Report. These reports identified 10 major project outputs and the percentage of completion. The reports prepared over the past year showed that the percentage for most outputs was routinely increased between 5 and 15 percentage points for each three-month period. USAID/Sri Lanka officials said that there was no real support for this progress.

Without specific quantitative indicators and accurate measurement of their achievements, the Mission lacked information to assess the effectiveness of certain project elements, could not readily identify project constraints on these elements, and was not complying with regulations.

Management Comments

USAID/Sri Lanka officials concurred with this finding and the recommendations. They stated that while the Water Board has made great progress, such subjective judgements should be quantitatively verified for the record.

Office of Inspector General Comments

Based on the above response, Recommendation No. 1 is considered resolved and will be closed when USAID/Sri Lanka provides the information agreed to which would document that certain action has been completed.

2. Controls Over Project Commodities Needed Improvements

A.I.D.-funded commodities costing about \$1 million were not adequately controlled. This occurred because USAID/Sri Lanka did not implement certain monitoring systems required by A.I.D. regulations. As a result, there was not adequate assurance that commodities were promptly inspected upon arrival, correctly stored and accounted for, and effectively used for project purposes.

Recommendation No. 2

We recommend that USAID/Sri Lanka:

- a. evaluate the Government of Sri Lanka's commodity arrival and disposition system as required by A.I.D. Handbook 15 and establish procedures to be used to monitor this system;
- b. require the Water Board to take action to secure missing equipment associated with the commodity shipments and to repair damaged items;
- c. require the Water Board to provide adequate storage for all equipment, and ensure the equipment is properly identified and marked with the A.I.D. emblem; and
- d. require the Board to prepare reports mainly for its own use on the operational status of equipment over a certain value, and periodically review these reports.

Discussion

Inspecting Project Commodities - The Water Board with the assistance of the technical assistance contractor was responsible for (1) monitoring commodity arrivals, (2) clearing goods through customs, (3) inspecting the goods, and (4) reporting shortages and damages to the procurement service agent so that he could file insurance claims. These actions should be completed within 30 days of the commodity's arrival in order for the insurance claim to be honored. These responsibilities were not effectively carried out.

Most of the commodities arrived from the United States in two shipments. The first, costing about \$460,000, arrived

in October 1987 and the second, costing about \$532,000 arrived in September 1988. The inspections for the 1987 shipment were not completed until five months after the commodities had arrived. The second shipment arrived on September 24, 1988, but had not cleared customs or been inspected at the completion of the audit field work on October 26, 1988.

The failure to inspect the two shipments within 30 days of arrival negated A.I.D.'s right to file insurance claims for missing and damaged commodities. The Water Board estimated that missing and damaged commodities amounted to about \$5,000 from the 1987 shipment. The inspections for the 1988 shipment had not been performed so there was no information concerning the amount of missing and damaged equipment. Since these inspections were not made timely, the insurance costs of over \$10,000 was in effect providing coverage only against catastrophic losses rather than the full coverage actually purchased.

There was also some question as to the adequacy of the inspections made by the Water Board. For example, one inspection report only contained a brief description of the commodities received and made no mention of any inspection of the commodities. Another inspection report indicated electrical items would be checked at a later time. Also, the Mission's project officer stated that during a visit to a warehouse in 1987, he received the impression that site personnel were not aware of what they were supposed to do in the way of inspecting and inventoring the project commodities.

A.I.D. Handbook 15 requires missions to maintain a current description of a recipient country's commodity arrival and disposition system, an evaluation of such a system, and the procedures used to monitor the system. However, USAID/Sri Lanka did not fully implement these requirements.

Storing And Accounting for Project Commodities - Due to security problems in Sri Lanka at the time of the audit, visits were made to only two project locations--the central workshop and central laboratory in the Colombo area. Project equipment at these locations cost about \$142,000 and \$25,000, respectively. The storage and control of the commodities were adequate at the workshop but not at the laboratory. For example, the equipment at the laboratory was not marked with the A.I.D. emblem or with an identification tag. It was also stored in a poorly secured area which was partially open to the outside elements

thereby subjecting the equipment to possible environmental damage. The following picture shows how the equipment was stored:



This situation will shortly be aggravated since about \$66,000 in equipment from the September 1988 commodity shipment was scheduled to be sent to this laboratory.

According to the project paper, the Water Board was responsible for ensuring adequate storage of project commodities. The technical assistance contractor was to assist the Water Board in developing and implementing an inventory control system. However, neither Water Board nor Mission officials could explain the storage conditions or the absence of AID emblems and identification tags.

Utilizing Project Commodities - Visits to the two project locations mentioned above disclosed that most items were not being utilized. This occurred primarily because the facilities where the items were to be utilized had not been constructed or renovated as planned. However, in some cases it was because parts were missing or repairs were needed. For example, the laboratory had two meters costing \$500 each which could not be used because they were missing a part. The laboratory also had a \$560 refrigerator/freezer which had not worked since it was received in November 1987.

The project paper stated the Water Board was responsible for equipment utilization and was to submit semi-annual utilization reports to the Mission. In fact, Handbook 15, Chapter 10C, specifically requires the Mission to review project progress reports on commodity utilization. However, no utilization reports had been prepared and there was virtually no other information available on equipment utilization.

Accordingly, the Water Board should prepare periodic reports on the operational status of equipment over a certain value such as \$500. The Mission could review these reports and thereby have greater assurance that commodities were being effectively utilized as required by the Handbook.

Management Comments

While USAID/Sri Lanka officials did not believe the magnitude of the problem noted to be significant, they concurred with the recommendation.

Office of Inspector General Comments

Based on the above response, Recommendation No. 2 is considered resolved and will be closed when USAID/Sri Lanka provides the documentation that the agreed to action has been completed.

3. Host Country Contributions Were Behind Schedule

Host country contributions for the Water Supply and Sanitation Sector Project were below the scheduled levels. While this occurred in part because of delays in the project's schedule, a contributing factor was that Mission oversight required by A.I.D. and Mission polices was not sufficiently thorough. As a result, a clear message was not being provided to the Government of Sri Lanka on the need to provide the contributions. Also, according to the mid-term evaluation, a lack of contributions delayed accomplishing important project segments.

Recommendation No. 3

We recommend that USAID/Sri Lanka:

- a. revise the financial implementation plan for host country contributions to ensure the Government provides the required \$7.3 million;
- b. increase overall monitoring of host country contributions and ensure inadequate levels of contributions and related problems are reported and discussed in the Mission's Quarterly Project Implementation Reports; and
- c. notify the Government to discontinue claiming unallowable items as host country contributions, review the amounts being claimed to ensure unallowable items are not included, and adjust the amount reported by the \$198,000 discussed in this report.

Discussion

The Government of Sri Lanka was not making all its contributions to the project as scheduled by the terms of an agreement signed on August 24, 1984. Accordingly, it may have difficulty reaching the \$7.3 million required in host country contributions.

To illustrate, a financial plan prepared in August 1986 prescribed that over \$4 million should be contributed by December 31, 1987. However, as of this December date, only \$1.1 million was reported as being contributed.

The latest revision to the financial plan (April 1987) noted that to accommodate for earlier shortages as well as to avoid serious project implementation problems, the Government needed to contribute about \$3.6 million during calendar year 1988. However, the Government only authorized \$1.8 million for this period and as of September 30, 1988 spent only about \$266,000.

Mission officials stated that the reason for the "slowness" in providing required contributions was due primarily to delays in construction caused by a decision to fund the construction in a slower but more logical and efficient manner. The mid-term evaluation, however, stated that the planned training center renovation, which was to be funded by host country contributions, had not yet been undertaken. The evaluation further stated that the unrenovated center resulted in less than optimum training conditions and the underutilization of project equipment.

Whatever the reason for the deficiency in host country contributions, the Mission needs to be more involved in monitoring the level of these contributions. For example, we noted the following specific problems with the Mission's monitoring:

- The project officer did not estimate the host country contributions required for calendar year 1989. Also, no analysis was made of required local currency amounts compared to the Government's proposed budget for calendar year 1989. Additionally, a document required by A.I.D. Handbook 3 outlining proposed changes in project implementation caused by insufficient host country contributions was not prepared. Mission management, on July 11, 1988, did request that certain information on host country contributions be included in future reports. As of the date of this audit, this information had not been received.
- While discussed at meetings, Mission Quarterly Project Implementation Reports prepared during the past year did not report on the level of host country contributions and related problems. The Mission Order which implements Handbook 3, Chapter 11, stipulates such monitoring is required.

- The Government of Sri Lanka reported that more than \$1.1 million was contributed as of December 31, 1987. The Mission accepted the Government's claim without review. Our review of these reported contributions disclosed that at least \$198,000 were for unallowable items such as customs duties and other Government of Sri Lanka taxes. Therefore, the actual allowable contributions were less than reported.

Similar problems were discussed in a recent audit report addressed to USAID/Sri Lanka (Audit Report No. 5-383-87-6 dated September 3, 1987). This prior audit report recommended the establishment of policies and procedures to improve monitoring of host country contributions. Based on this recommendation, a Mission Order, Monitoring Project Budgets, was issued in November 1987. In monitoring host country contributions, the Mission should more closely follow the procedures established in the Mission Order.

Improved monitoring would not guarantee full compliance with host country contribution requirements. However, more rigorous monitoring would provide a clearer message to the Government about the necessity of providing the agreed funding, establish accountability over the amounts needed to be provided, and comply with the various A.I.D. requirements.

Management Comments

USAID/Sri Lanka officials concurred with this finding and the recommendations. However, they stated that the monitoring system currently in place was far more detailed than other missions and that this audit finding was encouragement to be even more vigilant.

Office of Inspector General Comments

Based on the above response and the documentation which was provided, part (b) of Recommendation 3 is considered closed and parts (a) and (c) are considered resolved. These last two parts will be closed when the agreed to action is completed.

B. Compliance and Internal Controls

Compliance

The three findings in this report identified that USAID/Sri Lanka did not fully comply with A.I.D. requirements for monitoring and reporting on project achievements; monitoring the receipt, disposition, and utilization of project commodities; and monitoring the level of host country contributions. The review of compliance was limited to the findings presented in this report.

Internal Controls

The findings in this report contained internal controls problems. Findings 1 identified the need for improved controls over reporting of project achievements. Findings 2 and 3 discussed the need for improved controls over project commodities and host country contributions. The review of internal controls was limited to these areas.

C. Other Pertinent Matters

More timely action was needed in resolving recommendations contained in a mid-term evaluation report. To illustrate, the March 1988 mid-term evaluation report for this project contained 11 recommendations. The project Officer prepared the required Project Evaluation Summary Sheet in which he proposed that the recommendations be implemented by July 1988. The project officer said the recommended actions and proposed target dates were agreed to by Water Board officials. However, at the end of October 1988, the Mission had not yet determined whether or not the recommendations should be implemented and did not know the status of implementation. Such information is required by the A.I.D. Evaluation Handbook. In response to the draft report, Mission officials stated that the Project Evaluation Summary has now been finalized and a time schedule to implement the recommendations established.

An audit of indirect costs claimed by the technical assistance contractor is needed. This contractor was paid \$1.3 million (as of September 30, 1988) for indirect costs -- the maximum allowed under the contract. However, there have been no audits of the overhead rates charged. Most of the overhead was for field staff. However, based on a cursory review of information available in Sri Lanka, it appears as if home office type overhead items were included in the field staff overhead rate. Downward adjustments in the rates could result in a substantial savings. In response to the draft report, Mission officials agreed to perform an in depth review of the contractor's records to determine if an audit would likely result in a significant savings.

**AUDIT OF THE
WATER SUPPLY AND SANITATION
SECTOR PROJECT IN SRI LANKA**

PROJECT NO. 383-0088

PART III - APPENDICES

UNITED STATES GOVERNMENT

memorandum

DATE: January 19, 1989

REPLY TO
ATTN OF: Director, USAID/SL, Peter J. Bloom

SUBJECT: Water Supply and Sanitation Project Audit (383-0088)
- Mission Comments on Draft Audit

TO: RIG/A, Reggie Howard

Ref. Howard to Bloom memo of December 23, 1988

The Mission Comments on the subject audit are keyed to the format which indicates space for Mission Comments to be included in the text of the audit report.

Finding and Recommendation 1 - Quantitative Indicators -
USAID/ Sri Lanka concurs with finding and recommendation number 1. Despite the quantitative deficiencies, all evaluative work done by USAID, the WASH project, the IBRD water sector analysis, ADB water sector experts, DANIDA and FINIDA water sector review have indicated that the Water Board has made great progress in the institutional restructuring which was the purpose in the Water Supply and Sanitation Project. USAID is aware that these largely subjective judgements should be quantitatively verified for the record. We believe a gap in quantification occurred due to the failure to draw linkages between the shorter term contractor activity objectives and the longer term project paper purpose indicators. By their very nature, contractor tasks and objectives are more dynamic in nature, changing more often and being constantly adjusted to meet the current situation. However, the overall project objectives must be constantly kept in sight as these tasks are adjusted. The mission will review the project objectives in the project revision which is being prepared and will task the contractor to draw the linkages from its specific tasks to the project objectives. Progress against the project objectives will be incorporated into the contractor's quarterly reporting format. USAID requests that this recommendation be considered resolved. USAID will submit documentation when completed to close the recommendation.

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Finding and Recommendation Number 2 - Commodities - USAID feels that the magnitude of problems identified by the audit (damages and losses amounting to approximately 1% of the total value of procurement) are insignificant and that the finding and recommendation should have been treated as other pertinent matters. This said, USAID concurs that controls over commodities can always be improved and we concur with the recommendations. The USAID controller will review the Government of Sri Lanka system for arrival and disposal of commodities and either certify the system or establish a suitable control system for our project commodities. USAID is in the process of preparing a Mission Order on Project Commodities which will define the procedures for monitoring the system. The Water Board and the TA contractor has completed a re-surveying of commodities which were damaged or missing in shipment and has determined that the most cost effective and efficient approach is to buy the necessary small parts and effect repairs using local materials. Since in many cases the lack of a small part such as an electrical plug has rendered an expensive piece of equipment unservicable, this local rectification of the problems is the preferred route to take. The problem of inadequate storage of the commodities occurred because the commodities arrived prior to the completion of the facilities. It has proven impossible in projects around the world to precisely calibrate commodity arrival with facility completion. USAID is writing to Water Board instructing them to assure that all commodities awaiting final distribution be properly stored in secured and weather tight storerooms or warehouses. As the audit report indicates, USAID has a system in place to track utilization of large value equipment. We are preparing a letter to the Water Board requesting that they work with their TA contractor to design a system of periodic internal reports on the operational status of lesser value project funded equipment to continue for at least the life of the AID project. Based on this response we request that this recommendation be considered resolved. USAID will forward documentation discussed above when it is developed to close the recommendation.

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Finding and Recommendation Number 3 - Host Country Contribution

While USAID concurs with the finding and recommendation we consider our system for monitoring host country contributions to be far more detailed than any other mission with which we are familiar. We consider the audit finding as encouragement to be even more vigilant in refining the system. We would also like to point out that our tracking system for host country contributions was developed and implemented prior to the audit of Host Country Contributions conducted in 1987 and that audit, as this one, offered some suggested refinements to that system. As documented to RIG/A in late December, our PIR process explicitly reviewed host country contributions in nearly all the projects in the portfolio. Unfortunately, we did not have the data for the Water Supply and Sanitation project at that time. USAID does not consider that failure to meet the PP schedule for contributions has had an adverse effect on the progress of the project as a whole. The failure to rehabilitate the training center was due to a combination of bureaucratic inertia and problems in the contracting process rather than lack of financial resources. In fact the Water Board has underspent its budget for the project up to the present time. With the construction component coming on line, the contributions will clearly accelerate. The audit process has stimulated extra effort at the Water Board and they are currently reviewing all the contribution accounts to purge the unallowable items and accurately reflect the staffing costs. A revised financial plan will be included in the project revision which is now underway and the Water Boards revised accounting of contributions to date will be included. Host Country Contributions have been included as a standard issue item in the quarterly report format. USAID has attached the revised format for internal PIRs including the host country contribution and therefore requests that recommendation 3b be closed. We request that recommendations 3a and 3c be considered resolved. USAID will forward documentation discussed above to close the recommendation as soon as it is completed.

Other Pertinent Matters

Evaluation - The Project Evaluation Summary was completed by USAID in early November and is attached for your reference. The time schedule for actions to resolve the issues in the evaluation is shown on page one. This time schedule was revised to reflect the situation at the time and we will be monitoring adherence to the schedule.

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Audit of ESI - The USAID controller's office will be taking an in depth look at the financial records kept in the contractor's office here in Colombo to determine if an audit would be likely to result in significant cost savings to the USG. If the audit appears warranted, we will contact you under the non-federal audit process.

Clearance:

CTR: W. Butler (Draft)
PRJ: D. Zvinakis (Draft)
ENG: J. Thanarajah (Draft)

AID:D/D:GLNelson
WSSPAUDT

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RIG/A/Nairobi	1
RIG/A/Tegucigalpa	1
RIG/A/Washington	1