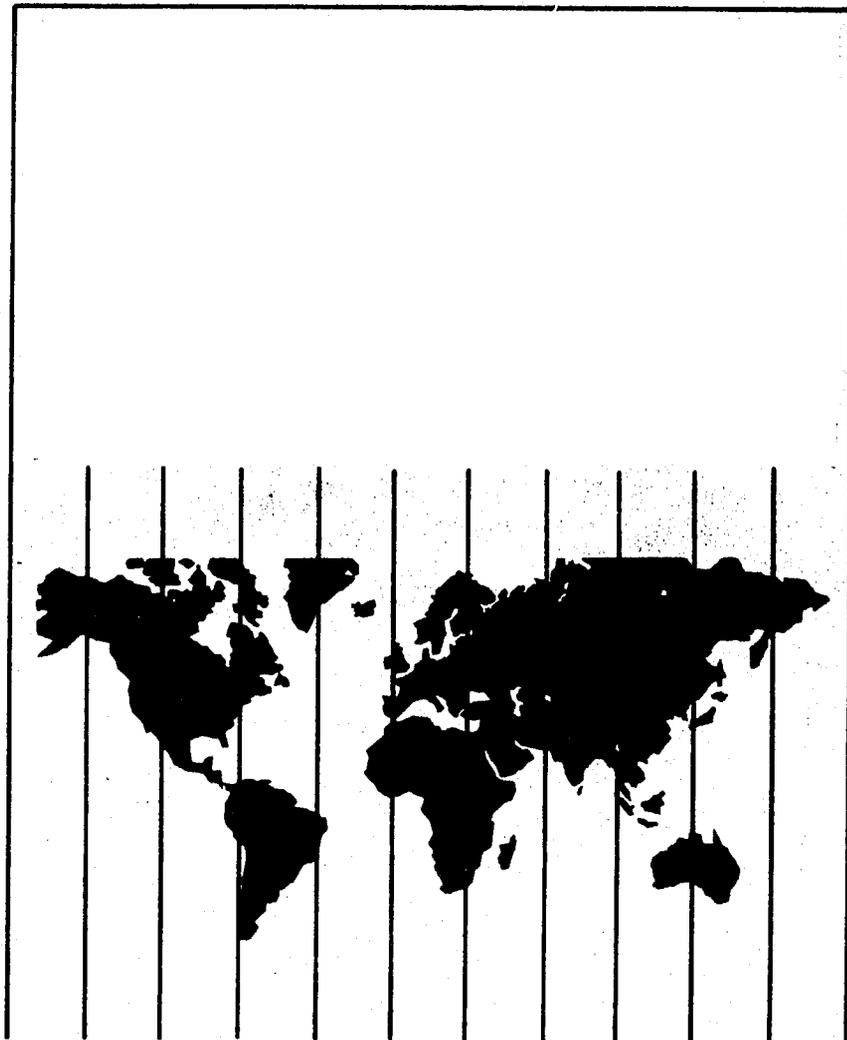


UNITED STATES  
AGENCY FOR INTERNATIONAL DEVELOPMENT

THE  
INSPECTOR  
GENERAL



Regional Inspector General for Audit

SINGAPORE

PD-ABD-354

**Audit of  
USAID/Philippines' Rural Infrastructure  
Fund Project No. 492-0420**

**Audit Report No. 2-492-92-01  
October 10, 1991**

---

**USAID/Philippines complied with A.I.D. policies and procedures on monitoring, reporting, contracting and accounting for A.I.D. funds. However, it needs to improve its controls to ensure the provision of host-country contributions, effective utilization and marking of commodities and verification procedures to preclude the reimbursement of taxes.**

---

**UNITED STATES OF AMERICA**  
**AGENCY FOR INTERNATIONAL DEVELOPMENT**  
**RESIDENT AUDIT OFFICE**  
**MANILA**

UNITED STATES POSTAL ADDRESS  
USAID/RAO/Manila  
APO AP 96440

INTERNATIONAL POSTAL ADDRESS  
c/o AMERICAN EMBASSY  
MANILA, PHILIPPINES

DATE: October 10, 1991

**MEMORANDUM**

TO: Mr. Malcolm Butler  
Director, USAID/Philippines

FROM:   
Dennis L. Smith  
Resident Auditor

SUBJECT: Audit of USAID/Philippines' Rural  
Infrastructure Fund Project No. 492-0420  
Audit Report No. 2-492-92-01

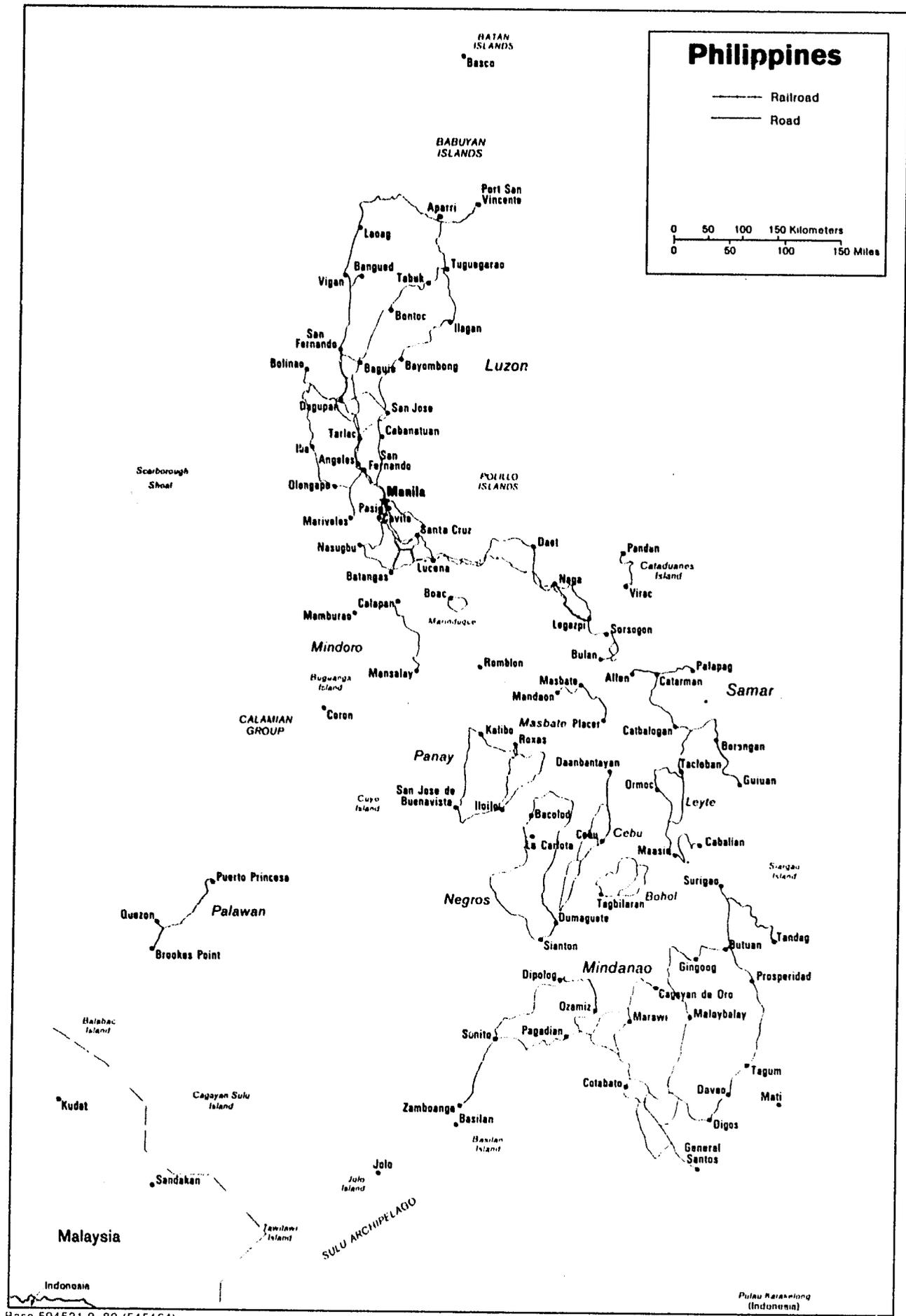
The Resident Audit Office/Manila has completed its audit of USAID/Philippines' Rural Infrastructure Fund Project. Five copies of the report are provided for your action. The draft report was submitted to you for comment and your comments are attached to the report. The report contains five recommendations. Recommendation No. 2.4 is closed. Recommendations No. 1, 2.1, 2.2, 3, 4 and 5 are resolved and can be closed when the actions in process are complete. Recommendation No. 2.3 is unresolved pending a determination on the amounts to be recovered. In addition, we reached general agreement on potential savings of about \$3.2 million from funds committed to pay for unallowable host-country taxes.

Please advise me within 30 days on the status of actions planned or in process to close the recommendations. I appreciate the courtesy and cooperation extended to my staff during the audit.

# Philippines

— Railroad  
— Road

0 50 100 150 Kilometers  
0 50 100 150 Miles



## **EXECUTIVE SUMMARY**

Started in September 1987, the \$170 million Rural Infrastructure Fund Project was initiated to expand the construction and improve the maintenance of rural transport facilities, including roads, bridges, ports and airports. By its planned completion in December 1994, the project should have contributed to the goal of developing facilities that will attract investment and sustain the economic growth of rural areas. The project provides funds for construction, engineering services, technical assistance, commodities, training and monitoring. The Philippine government contributions are to total \$14.5 million (pages 1-2).

The audit was conducted from February 25 through May 6, 1991, in accordance with generally accepted government auditing standards. The specific objectives for this audit are listed on pages 2 and 3 of the report and the audit scope and methodology are described in Appendix I.

The audit revealed that USAID/Philippines complied with A.I.D. policies and procedures on monitoring, reporting, contracting and accounting for A.I.D. funds. However, USAID/Philippines needs to:

- develop a system for monitoring host-country contributions to ensure that the Philippine government fulfills its financial commitment to the project (pages 5-7),
- adopt verification procedures to preclude the payment of identifiable taxes in host-country contracts and to ensure the recoupment of mobilization payments (pages 10-13) and
- require the Philippine government to provide routine utilization reports that would track the distribution and use of vehicles and the marking of AID-financed commodities (pages 15-18).

This report contains five recommendations to correct the weaknesses described above. Our assessments of internal controls related to the audit objectives and compliance with applicable laws, the grant agreement and contractual provisions are discussed in the "Report on Internal Controls" and "Report on Compliance" sections of the report, respectively.

USAID/Philippines officials reviewed the draft report and agreed with our findings and conclusions. USAID/Philippines has initiated actions to implement the report recommendations. Management comments on our draft report, included as Appendix II, were considered in preparing the final report.



Office of the Inspector General

October 10, 1991

---

# TABLE OF CONTENTS

---

	<u>Page</u>
<b>EXECUTIVE SUMMARY</b>	i
<b>INTRODUCTION</b>	1
Background	1
Audit Objectives	2
<b>REPORT OF AUDIT FINDINGS</b>	
Did USAID/Philippines follow A.I.D.'s procedures in monitoring, reporting and evaluating project activities?	4
Host-country Contributions Are Not Known	5
Did USAID/Philippines ensure that A.I.D.'s procedures were followed in obtaining (a) qualified and eligible construction contractors at a fair price; (b) timely, effective and efficient contractor performance; (c) an accounting for the services provided and (d) an accounting for the obligation and expenditure of A.I.D. funds?	7
Verification Procedures Need to be Improved	10
Did USAID/Philippines ensure that A.I.D.'s procedures were followed in (a) obtaining necessary and eligible commodities at a fair price; (b) safeguarding the commodities against waste, loss and misuse; (c) using the commodities effectively, efficiently and in a	

**Page**

timely manner; (d) providing accounting for the receipt, storage and use of commodities and (e) accounting for the obligation and expenditure of A.I.D. funds? 13

A Reporting System Is Needed 15

Did USAID/Philippines ensure that A.I.D.'s procedures were followed in obtaining (a) qualified and eligible technical assistance contractors at a fair price; (b) timely, effective and efficient contractor performance and (c) an accounting for the services rendered? 19

REPORT ON INTERNAL CONTROLS 21

REPORT ON COMPLIANCE 25

**Appendix**

SCOPE AND METHODOLOGY I

MANAGEMENT COMMENTS II

REPORT DISTRIBUTION III



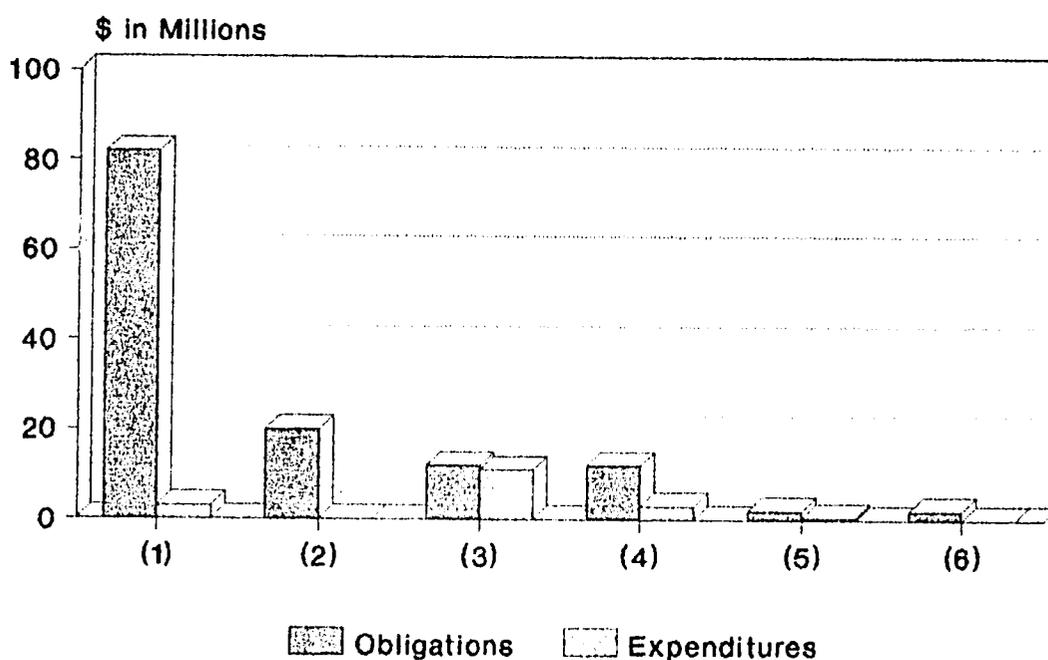
# INTRODUCTION

## Background

Started in September 1987, the Rural Infrastructure Fund Project was initiated to expand the construction and improve the maintenance of rural transport facilities, including roads, bridges, ports and airports. By its planned completion in December 1994, the project should have contributed to the goal of developing facilities that will attract investment and sustain the economic growth of rural areas. Project outputs include:

- design and construction or upgrading of about 480 miles of rural roads and bridges;
- rehabilitation, improvement or construction of feeder ports in about 35 municipalities and
- procurement, installation or rehabilitation of air navigational aids equipment at the Manila International Airport and airports of selected provinces.

Obligations and Expenditures  
As of March 31, 1991



(1)Construction (2)Gen. Santos City  
(3)Eng. (4)Commodities (5)Tech. Services  
(6)Training, Monitoring & Audit

Project inputs are to reach \$184.5 million. A.I.D. authorized life-of-project funding is \$170 million and the Government of the Philippines (GOP) agreed to provide \$14.5 million. As of March 31, 1991, A.I.D. expenditures had reached \$18 million, or 14 percent of the total obligations. The GOP had budgeted about \$4 million and expended about \$1 million, as of March 31, 1991, for road construction and maintenance, land and right-of-way acquisitions, and operating costs.

The GOP's Department of Public Works and Highways is implementing the construction or improvement of roads, bridges and ports and the Bureau of Air Transportation, in coordination with an AID-contracted U.S. firm, is implementing the procurement, installation and maintenance of the air navigational aids equipment.

---

### **Audit Objectives**

The Resident Audit Office/Manila reviewed USAID/Philippines' Rural Infrastructure Fund Project to answer the following audit objectives:

1. Did USAID/Philippines follow A.I.D.'s procedures in monitoring, reporting and evaluating project activities?
2. Did USAID/Philippines ensure that A.I.D.'s procedures were followed in obtaining (a) qualified and eligible construction contractors at a fair price; (b) timely, effective and efficient contractor performance; (c) an accounting for the services provided and (d) an accounting for the obligation and expenditure of A.I.D. funds?
3. Did USAID/Philippines ensure that A.I.D.'s procedures were followed in (a) obtaining necessary and eligible commodities at a fair price; (b) safeguarding the commodities against waste, loss and misuse; (c) using the commodities effectively, efficiently and in a timely manner; (d) providing accounting for the receipt, storage and use of commodities and (e) accounting for the obligation and expenditure of A.I.D. funds?

4. Did USAID/Philippines ensure that A.I.D.'s procedures were followed in obtaining (a) qualified and eligible technical assistance contractors at a fair price; (b) timely, effective and efficient contractor performance and (c) an adequate accounting for the services rendered?

To answer the audit objectives, we tested whether USAID/Philippines (1) followed applicable internal control procedures and (2) complied with certain provisions of laws, regulations, a grant, and contracts. Our tests were sufficient to provide reasonable--but not absolute--assurance of detecting abuse or illegal acts that could significantly affect the audit objectives. However, because of limited time and resources, we did not continue our examination when we found that, for the items tested, USAID/Philippines, the GOP and contractors followed A.I.D. procedures and complied with legal, grant and contractual requirements. Therefore, we limited our conclusions concerning these positive findings to the items actually tested. But when we found problem areas, we performed additional work

- to conclusively determine that USAID/Philippines, the GOP or contractors were not following a procedure or not complying with a legal, grant or contractual requirement;
- to identify the cause and effect of the problems and
- to make recommendations to correct the condition and cause of the problems.

Appendix I contains a complete discussion of the scope and methodology for this audit.

---

# **REPORT OF AUDIT FINDINGS**

---

## **Did USAID/Philippines follow A.I.D.'s procedures in monitoring, reporting and evaluating project activities?**

USAID/Philippines provided project monitoring and reporting in accordance with A.I.D.'s procedures except that a system to monitor host-country contributions had not been developed. Because of the two-year extension of the project completion date, USAID/Philippines decided to postpone the mid-term evaluation, planned for November 1990, to August 1991.

USAID/Philippines established a system for monitoring and reporting project activities. USAID/Philippines' system of project monitoring includes attending coordination meetings and conducting site visits. Coordination meetings are held weekly among contractor, consultant engineer, USAID/Philippines and Government of the Philippines (GOP) officials. Matters discussed during the meetings were documented in the project files. USAID/Philippines project officials performed site visits as part of the Mission's monitoring process and prepared site visit reports identifying the status of subproject construction, including implementation problems. A consultant engineer supervised the day-to-day construction activities of the subprojects. The GOP submits monthly reports to USAID/Philippines, prepared by the consultant engineer, which summarize the progress of project activities, including subproject identification, design, construction and commodity procurement. The reports also identify implementation problems, planned solutions to the problems and other matters discussed during the coordination meetings.

USAID/Philippines' system of reporting follows the AID-prescribed system of project reporting. Project implementation reports are prepared quarterly and outline the implementation progress of the project and the planned

accomplishments for the next quarter. In addition, the reports describe whether the project fits A.I.D. objectives, whether the project is financially and institutionally sustainable, and whether project progress is meeting project objectives.

While project monitoring and reporting are generally adequate, USAID/Philippines needs to monitor host-country contributions as discussed below.

### **Host-Country Contributions Are Not Known**

A.I.D. procedures require that a system for monitoring project inputs be developed. Because USAID/Philippines did not recognize until recently that a system for monitoring host-country contributions was needed, the extent that host-country contributions were being provided was not being monitored. Consequently, USAID/Philippines did not know whether the GOP was fulfilling its financial commitment to the project.

**Recommendation No. 1: We recommend that USAID/Philippines develop a system for monitoring GOP contributions to the project, including verification of the validity of reported contributions.**

A.I.D. Handbook 3, Chapter 11 requires that a project monitoring system be established to gather timely information about project inputs, outputs and actions that are critical to project success. The project agreement, as amended, requires the GOP to provide \$14.5 million for road construction and maintenance, land and right-of-way acquisitions and operating costs.

Because a system for monitoring host-country contributions had not been established, USAID/Philippines did not know the extent that host-country contributions were being provided. To determine whether GOP contributions were being provided, we reviewed reports of USAID/Philippines and the GOP and held discussions with USAID/Philippines and GOP project officials. We found that USAID/Philippines quarterly implementation reports do not include information about GOP contributions. While the GOP tracks its contributions, USAID/Philippines has not been provided this information. The GOP report

showed that \$3.5 million had been budgeted but only about \$1 million had been expended as follows:

<u>Year</u>	<u>Budget</u> (in Million \$)	<u>Expenditures</u>
1989	\$ .255	\$ .133
1990	<u>3.302</u>	<u>.819</u>
Totals	<u>\$3.557</u>	<u>\$ .952</u>

However, we found that these expenditures were overstated. For example, the GOP report showed that about \$600,000 had been expended for right-of-way acquisitions. We reviewed \$400,000 of the \$600,000 reported and found that only \$224,000 were actual expenditures. GOP project officials explained that fund releases to field offices are recorded as expenditures.

USAID/Philippines has taken corrective actions regarding the monitoring of host-country contributions. In September 1990, USAID/Philippines contracted with a local accounting firm to report on and develop a monitoring system for host-country contributions in bilateral projects. A progress report of April 1991 submitted by the contractor showed GOP contributions of about \$1 million as of October 1990. The contractor's work is expected to be completed by November 1991, with a monitoring system for host-country contributions in place by that time.

Because a system for monitoring host-country contributions is not yet in place, USAID/Philippines does not know the extent that the GOP is fulfilling its financial commitment to the project.

### **Management Comments and Our Evaluation**

In September 1990, USAID/Philippines funded a study to (a) determine the current status of host-government counterpart contributions in Mission-funded projects and programs and (b) recommend an appropriate reporting system. USAID/Philippines anticipates completion of the study by December 1991.

USAID/Philippines is taking a responsive course of action on Recommendation No. 1. Accordingly, the recommendation is resolved on issuance of this report and can be closed once the reporting system, implemented as a result of the study, is in place.

---

**Did USAID/Philippines ensure that A.I.D.'s procedures were followed in obtaining (a) qualified and eligible construction contractors at a fair price; (b) timely, effective and efficient contractor performance; (c) an accounting for the services provided and (d) an accounting for the obligation and expenditure of A.I.D. funds?**

For the items tested, USAID/Philippines ensured that A.I.D.'s procedures were followed in contracting for project construction, in the performance of the construction contractors, and in accounting for the services provided. However, USAID/Philippines needs to improve its review procedures to ensure an accounting for the obligation and expenditure of A.I.D. funds in accordance with A.I.D.'s policies and procedures.

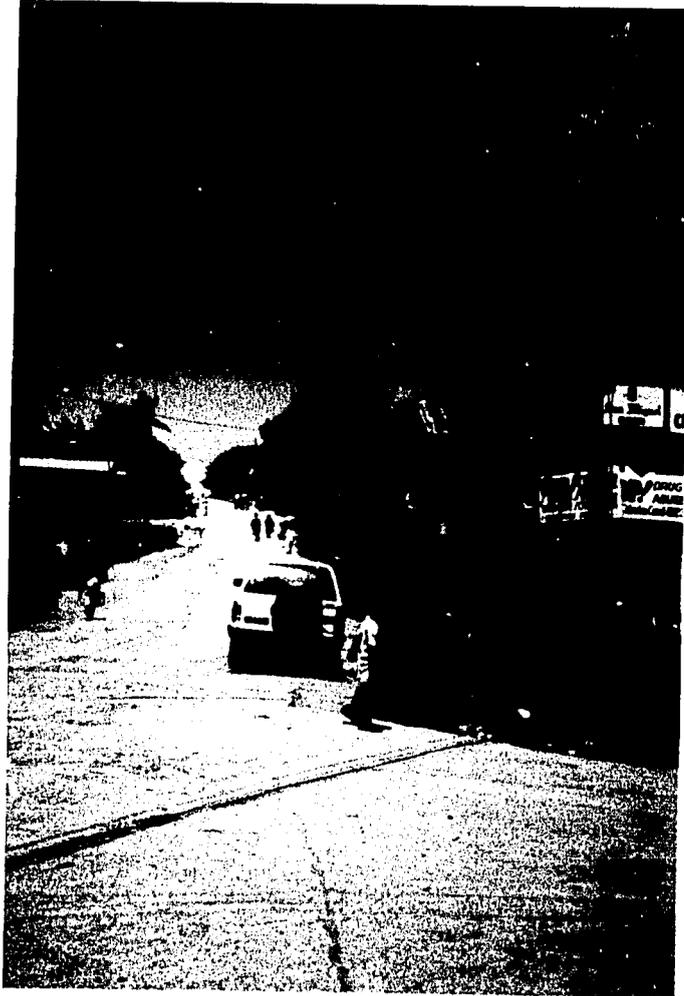
The host country contracted for the construction services, but USAID/Philippines approved all contracts in excess of \$100,000. At the time of audit, A.I.D. was financing nine subprojects for roads, bridges and ports, totaling about \$41 million. We reviewed about \$38 million of the construction contracts and tested about \$1 million of the \$1.6 million of expenditures. We found that USAID/Philippines ensured that the GOP awarded construction contracts on a competitive basis in accordance with A.I.D. procedures. Construction contractors were prequalified before being allowed to bid on subprojects. Host-country criteria for prequalification of construction contractors included financial capacity, technical capacity and experience. After competitive bidding, construction contracts were awarded to prequalified contractors who submitted the lowest responsive bids.

Construction services were defined to ensure timely, effective and efficient contractor performance. However, contractor performance has been affected by problems that were not foreseeable during the prequalification and selection processes. For instance, a joint venture, contracted to construct 66 miles of roads costing about \$30 million, has been incurring delays because of inadequate

construction equipment, insurgency problems at the construction site, and disputes about land and right-of-way acquisitions. Contractor officials said that a member of the joint venture did not provide the equipment it agreed to provide to the joint venture. Also, construction activities at one site were suspended for about eight months because of insurgent threats to contractor personnel, and property owners have refused to vacate land designated for road construction.



**A \$20 million road construction project suspended for about eight months due to threats by communist insurgents**



**A portion of a \$10 million road construction project with  
right-of-way problems**

**USAID/Philippines developed procedures to adequately account for construction contractor services. USAID/Philippines' procedures require the consultant engineer to verify and review the accomplishments of construction contractors. In addition, the GOP and consultant engineer must approve accomplishment reports and the progress billings of construction contractors. However, USAID/Philippines needs to adopt effective review procedures for host-country contracts to ensure an accounting of A.I.D. funds as discussed below.**

## **Verification Procedures Need to be Improved**

A.I.D. procedures prohibit the use of A.I.D. funds for payment of host-country taxes. In addition, A.I.D. procedures allow payment and recoupment of mobilization advances in construction contracts. Because USAID/Philippines had not perceived a need to establish review and verification procedures, A.I.D. funds have been committed to pay host-country taxes and mobilization payments were not recouped as planned because the applicable contractual provision was misinterpreted. As a result, as much as \$3.2 million in A.I.D. funds may have been committed for host-country taxes and about \$100,000 may already have been paid to a construction contractor. Also, about \$110,000 in mobilization payments have not been recouped.

### **Recommendation No. 2: We recommend that USAID/Philippines:**

- 2.1 adopt verification procedures to preclude the payment of identifiable taxes in host-country contracts and to ensure the recoupment of mobilization payments,**
- 2.2 determine the amount of host-country taxes that were included in host-country contracts and exclude commitments of A.I.D. funds for these amounts,**
- 2.3 recover from the Government of the Philippines payments made for host-country taxes and**
- 2.4 recover from construction contractors under-recouped mobilization payments of about \$110,000.**

**Recommendation No. 3: We recommend that USAID/Philippines report to A.I.D. officials, responsible for internal control matters, that verification procedures did not preclude host-country taxes from being included in host-country construction contracts.**

A.I.D. Handbook 11, Chapter 2 prohibits the use of A.I.D. funds for payment of host-country taxes. Annex II, Section B.4 of the project agreement requires (a)

that the grant be free from any taxes or fees and (b) to the extent that any contractor is not exempt from identifiable taxes, the grantee shall pay or reimburse the same with funds other than those provided under the grant.

A.I.D. funds have been committed and appear to have been used to pay value-added taxes of the host country. USAID/Philippines approves host-country construction contracts. Once approved, A.I.D. binds itself to pay for the services by issuing letters of commitment to construction contractors. We reviewed bid documents for three of the nine construction contracts, which amounted to \$38 million of about \$41 million of host-country construction contracts. We found that about \$500,000 in value-added taxes had been included in the A.I.D. commitment for a construction contract of about \$8 million. No payments had been made under this contract at the time of our review. The contractor bid documents and cost analyses in the two other contracts (both awarded to the same contractor), totaling about \$30 million, identified taxes of about \$2.7 million as included in the contracted amount. A USAID/Philippines project official explained that the contractors were advised that their bids should be free of host-country taxes and, therefore, the bids and the contracts should not have included host-country taxes. While the contractor bid documents for the two contracts did not identify the taxes as host-country taxes, the project accountant for the contractor stated that these were value-added taxes that were being remitted to the host country. As of March 1991 about \$100,000 appears to have been paid for value-added taxes through progress payments of about \$1 million on the two contracts.

This happened because USAID/Philippines does not review the detailed cost analyses of subprojects because it considers the bill of quantities sufficient to identify project costs. While the bill of quantities provides information on project costs, the detailed cost analysis identifies how the amounts in the bill of quantities are arrived at. USAID/Philippines project officials explained that detailed cost analyses are proprietary documents and, therefore, USAID/Philippines project officials are not required to review them. Both the contractors' bid documents and the cost analyses identified value-added taxes as included in the contracted amount.

A.I.D. policy and procedures allow the payment and recoupment of mobilization payments in construction contracts. Host-country contracts for construction

services allow construction contractors to claim 15 percent of the contract cost for mobilization expenses. The contracts provide for recoupment of the mobilization payments at 20 percent of the progress payment billings. The initial recoupment is to be made after 20 percent of the work has been completed or six months (for American firms; three months for local firms) after the notice to proceed has been given, whichever comes first. After the initial recoupment, succeeding recoupments are to be made at monthly intervals. Mobilization payments have not been recouped in accordance with the requirements of the construction contracts. USAID/Philippines has been recouping the mobilization payments from the contractors' progress billings every other month. This happened because USAID/Philippines interpreted incorrectly the contractual provision. The USAID/Philippines voucher examiner explained that he interpreted monthly intervals as every other month. Consequently, about \$110,000 of mobilization payments have not been recouped from \$1 million of progress billings in the two construction contracts we reviewed.

### **Management Comments and Our Evaluation**

Responding to Recommendation No. 2, USAID/Philippines agreed that there is a need to improve existing review procedures. As a new requirement in the voucher certification process, USAID/Philippines will require a certification from contractors on each invoice and from the GOP on each voucher approval that no identifiable host-country taxes are included in the request for payment. Also, USAID/Philippines has started reviewing the detailed cost analyses of existing contracts under the project and will adopt this review procedure for new contracts proposed for financing. USAID/Philippines expects the review of existing contracts to be completed by November 1991 and will adjust commitments for these contracts at that time. Once the review of existing contracts is completed, USAID/Philippines will analyze payments made under these contracts to determine the amount of host-country taxes paid and request reimbursement from the GOP. Regarding recoupment of the mobilization payments, USAID/Philippines determined that recoupment began at approximately the same time that the mobilization payments were made. However, it concluded that it was not intended for the recoupment to begin until six months after the mobilization payments were made. Therefore, USAID/Philippines refunded the

recoupments made and the GOP amended the contracts to provide for recoupment only after 20 percent of the contracted amounts have been billed.

USAID/Philippines is taking responsive courses of action on Recommendation No. 2. Accordingly, Recommendation No. 2.1 is resolved upon report issuance and can be closed when USAID/Philippines determines that the new certification process is precluding the reimbursement of identifiable taxes and that the new procedure has been adopted for review of detailed cost analyses. Recommendation No. 2.2 is also resolved upon report issuance and can be closed once the amount of host-country taxes included in the contracts is determined and decommitted from A.I.D. funds. Recommendation No. 2.3 remains open pending a determination on the amount of taxes to be recovered from the GOP; it can be closed once action to recover this amount has been taken. Recommendation No. 2.4 is closed upon issuance of this report.

Responding to Recommendation No. 3, USAID/Philippines stated that it is reasonable to assume that host-country taxes were included in A.I.D. commitments for construction contracts and agreed to analyze A.I.D. documents on this matter. While it does not agree that such a report is warranted, USAID/Philippines agreed to refer the substance of Recommendation No. 3 to the Mission Internal Control Oversight Committee and AID/Washington's Management Control Review Committee. This planned action is responsive to Recommendation No. 3 which is resolved on report issuance and can be closed when the agreed to reporting has been completed.

---

**Did USAID/Philippines ensure that A.I.D.'s procedures were followed in (a) obtaining necessary and eligible commodities at a fair price; (b) safeguarding the commodities against waste, loss and misuse; (c) using the commodities effectively, efficiently and in a timely manner; (d) providing accounting for the receipt, storage and use of commodities and (e) accounting for the obligation and expenditure of A.I.D. funds?**

For the items tested, USAID/Philippines followed A.I.D.'s procedures in obtaining, safeguarding and accounting for commodities and in accounting for the obligation and expense of A.I.D.'s funds. Also, most commodities were

utilized in accordance with A.I.D. procedures except that USAID/Philippines needs to develop a reporting system on the use of vehicles and the marking of commodities.

USAID/Philippines obligated \$12 million for the procurement of project commodities, including air navigational aids equipment, vehicles, computers and furniture. As of March 1991, \$3 million had been spent for project commodities. About \$2.9 million of the \$3 million of expenditures for commodities were for air navigational aids equipment. USAID/Philippines contracted directly with a U.S. firm to procure the air navigational aids equipment for the GOP. The contractor was to install and provide training for the maintenance of the equipment. In addition, about \$2 million was programmed for the purchase of commodities through the construction and technical assistance contracts. At the time of our audit, the construction and technical assistance contractors had purchased about \$1 million of vehicles, computer equipment and office furniture.

We found that USAID/Philippines had adequately reviewed, assessed and identified commodity needs and specifications and that none of the commodities were ineligible or restricted from A.I.D. financing. In addition, we found that commodities were obtained at a fair price. Vehicles, computer equipment and furniture were procured on a competitive basis with contracts awarded to the lowest responsive bidder. Because air navigational aids equipment is unique and available only from one source, procurement was conducted without full and open competition.

We found that inventory systems had been developed within the GOP and the technical assistance and construction contractors to safeguard project commodities against waste, loss and misuse. The GOP developed an inventory list of air navigational aids equipment provided to the different airports. A copy of the inventory list was provided to USAID/Philippines. The air navigational aids equipment were kept in locked and secured areas to prevent them from being lost or misused. Because air navigational aids are specialized equipment, the risk of their being misused is minimal. The technical assistance and construction contractors also developed an inventory system for project commodities in their possession. The inventory lists of project commodities were provided to USAID/Philippines. We found that the computer equipment and furniture were kept generally in secured areas. As discussed below, we found that some

vehicles were not being effectively utilized and some project commodities were not marked to ensure that the goodwill of the American people would be realized.

### **A Reporting System Is Needed**

A.I.D. procedures require the submission of utilization reports and the marking of project commodities. Some vehicles were not used for project purposes and some project commodities were not marked as provided by A.I.D. This happened because the contractor was not required by the GOP to establish a reporting system and this oversight had not been caught by USAID/Philippines. Consequently, maintenance costs were incurred for project commodities which did not benefit the project, and the goodwill of the American people was not being realized for about \$800,000 of project commodities.

**Recommendation No. 4: We recommend that USAID/Philippines require the GOP to provide routine utilization reports that would track**

- **the distribution and use of vehicles and**
- **the marking of AID-financed commodities with the A.I.D. handclasp emblem.**

**Recommendation No. 5: We recommend that USAID/Philippines report to A.I.D. officials, responsible for internal control matters, that utilization reports have not tracked the marking of AID-financed commodities with the A.I.D. handclasp emblem.**

A.I.D. Handbook 15, Chapter 10 requires that a monitoring system be established for commodities to ensure that they are used effectively for project purposes. The system should include the submission of periodic reports that identify the use of A.I.D. inputs. In addition, Chapter 9 of the Handbook requires that compliance with marking requirements be monitored.

Some vehicles were not used for project purposes. The technical assistance and construction contractors procured 36 vehicles for the project. In addition, A.I.D.

is charged a fixed monthly maintenance fee of \$500 for every vehicle. The consultant engineer was to use the vehicles for construction design and supervision. At the time of audit, 13 vehicles had been distributed to the consultant engineer at the construction sites; the rest were located at the GOP and consultant engineer offices in Manila. Two of the 13 vehicles had been utilized for other than project purposes.



The van taken by the congressman

A \$38,000 van provided to the consultant engineer at one construction site was taken by a local congressman for his own use. The consultant engineer reported the incident to USAID/Philippines and the GOP. As a result, USAID/Philippines and the GOP exerted efforts to recover the vehicle and the vehicle was eventually recovered. Another vehicle at the same construction site was lent occasionally to the town mayor. The consultant engineer had maintained a record of its use. The consultant engineer explained that he lends the vehicle to the town mayor during important occasions. This decision was made after the mayor's bodyguard attempted to take the vehicle by use of force.

USAID/Philippines did not ensure that a periodic reporting system for vehicle use was established. Although the technical assistance and construction contractors provided USAID/Philippines with the initial distribution list for the vehicles, periodic reporting of vehicle usage was not performed. This occurred because the GOP did not require the contractor to establish such a system. Consequently, utilization has not been effective and maintenance costs have been paid or accrued for the vehicles not used for project purposes.

The Foreign Assistance Act of 1961, Section 641 requires programs carried out overseas to be identified as "American Aid." A.I.D. Handbook 15, Chapter 9 requires that AID-financed commodities be marked with the A.I.D. handclasp emblem and that a monitoring system be established to ensure compliance with this requirement. The intent of the marking requirement is to promote the goodwill of the American people in the recipient country.

We looked at \$1 million of the \$2.9 million of navigational aids equipment and found that those commodities were marked with the A.I.D. handclasp emblem. However, we looked at about \$900,000 of vehicles, computer equipment and office furniture and found that about \$800,000 of these commodities were not marked with the A.I.D. handclasp emblem.



Part of the AID-financed vehicles  
not marked with the A.I.D. handclasp emblem

Consultant engineer officials were not aware that project commodities were to be marked and the GOP had not required a reporting system for commodity marking. GOP project officials were aware that the vehicles should be marked but explained that the communist threat was a concern. The issue of security has merit, but waivers must be authorized by the Mission Director if compliance with the requirement is considered to be impractical. Since no waivers have been approved for the project, the marking requirement should be complied with.

Although USAID/Philippines project officials assured us that GOP, consultant engineer, and construction contractor officials are aware of the marking requirement, the USAID/Philippines' reporting system does not address this requirement. A USAID/Philippines project official added that the GOP has been given a reasonable time to comply with the A.I.D. marking requirement. Because this requirement has not been complied with, the goodwill of the American people is not being realized for about \$800,000 of commodities not marked with the A.I.D. handclasp emblem.

### **Management Comments and Our Evaluation**

Responding to Recommendation No. 4, USAID/Philippines agreed with the need to ensure proper utilization of vehicles. USAID/Philippines has begun to implement a system that requires routine periodic reporting from project consulting engineers. In addition, USAID/Philippines is developing a system that will address the marking of AID-financed commodities. These actions are responsive to Recommendations No. 4 which is resolved on report issuance and can be closed once the new systems have been implemented.

Responding to Recommendation No. 5, USAID/Philippines assured us that the issue on marking AID-financed commodities will be addressed in the fiscal year 1991 Mission internal control assessment. In addition, USAID/Philippines will report the matter to the Mission Internal Control Oversight Committee and AID/Washington's Management Control Review Committee. These actions are responsive to Recommendation No. 5 which is resolved upon report issuance and can be closed when the agreed to reporting has been completed.

---

**Did USAID/Philippines ensure that A.I.D.'s procedures were followed in obtaining (a) qualified and eligible technical assistance contractors at a fair price; (b) timely, effective and efficient contractor performance and (c) an accounting for the services rendered?**

For the items tested, USAID/Philippines ensured that A.I.D.'s procedures were followed in contracting for technical assistance and in the performance of the technical assistance contractors. However, A.I.D.'s procedures were not always followed in accounting for the services rendered.

A.I.D. financed two contracts with technical assistance valued at about \$11 million. The first, a joint venture of U.S. and Filipino consultant engineers, was a \$10.7 million host-country contract for architectural and engineering services. The contract was for cost reimbursement plus a fixed fee. The second, for \$300,000, was part of a direct A.I.D. contract with a U.S. firm for the procurement and installation of air navigational aids equipment at one international and 13 domestic airports.

We found that the GOP and USAID/Philippines followed A.I.D.'s procedures in obtaining qualified and eligible technical assistance contractors at a fair price. The host-country contract for architectural and engineering services was procured on a competitive basis. The interested firms were prequalified and negotiations were conducted with the most qualified and eligible bidders. Because the GOP and the most qualified and eligible bidder failed to agree on the price, the contract was awarded to the second most qualified and eligible bidder. The direct A.I.D. contract with a U.S. firm for procurement of air navigational aids equipment, that included technical assistance of about \$300,000, was awarded without full and open competition because the air navigational aids equipment was unique and available from only one source. The technical assistance portion of the contract was for equipment installation and maintenance training. Furthermore, we found that the contract for architectural and engineering services clearly defines the responsibilities of the contractor to ensure timely, effective and efficient contractor performance.

However, USAID/Philippines did not ensure that the fixed fee was computed in accordance with the terms of the contract. The amount of fixed fee allowable

for each billing was to be based on the ratio of the allowable cost of the billing for the period and the total contract cost. We reviewed about \$2 million in disbursements and found that about \$5,000 in fixed fee was erroneously paid to the contractor. Because USAID/Philippines did not reduce the allowable fee of the billings to reflect the cost disallowances, about \$5,000 in fixed fee was paid to the contractor before it was due. The total allowable fixed fee was not exceeded. In responding to our draft report, USAID/Philippines indicated that the fee payments to the contractor had been adjusted.

---

# **REPORT ON INTERNAL CONTROLS**

This section summarizes our assessment of USAID/Philippines internal controls for the audit objectives.

---

## **Scope of Our Internal Control Assessment**

We conducted our audit in accordance with generally accepted government auditing standards, which require that we plan and perform the audit to fairly, objectively and reliably answer the objectives of the audit. Those standards also require that we

- assess the applicable internal controls when necessary to satisfy the audit objectives and
- report on the controls assessed, the scope of our work and any significant weaknesses found during the audit.

We limited our assessment of internal controls to those applicable to the audit objectives. Our review was designed to answer the audit objectives and not to provide assurance on USAID/Philippines' overall internal control structure. We classified significant internal control policies and procedures applicable to each audit objective by categories. For each category, we obtained an understanding of the design of relevant policies and procedures and determined whether they have been placed in operation--and we assessed control risk. We have reported these categories as well as any significant weaknesses under the applicable section heading for each audit objective.

---

## **General Background on Internal Controls**

Under the 1982 Federal Managers' Financial Integrity Act and Office of Management and Budget implementing policies, A.I.D.'s management is responsible for establishing and maintaining adequate internal controls. Also, the General Accounting Office has issued "Standards for Internal Controls in the Federal Government" to be used by agencies in establishing and maintaining such controls.

The objectives of internal control policies and procedures for Federal foreign assistance programs are to provide management with reasonable--but not absolute--assurance that resource use is consistent with laws, regulations, and policies; resources are safeguarded against waste, loss, and misuse; and reliable data is obtained, maintained, and fairly disclosed in reports. Because of inherent limitations in any internal control structure, errors or irregularities may occur and may not be detected. Moreover, predicting whether a system will work in the future is risky because (1) changes in conditions may require additional procedures or (2) the effectiveness of the design and operation of policies and procedures may deteriorate.

---

## **Conclusions for Audit Objectives**

### **Audit Objective One**

The first audit objective was to determine whether USAID/Philippines followed A.I.D. procedures in providing project monitoring, reporting and evaluating. In planning and performing the audit for this objective, we considered the applicable internal control policies and procedures cited in A.I.D. Handbook 3. We reviewed USAID/Philippines internal controls relating to project monitoring, reporting and evaluating. We classified relevant procedures into the following categories and processes: project management, project implementation, contract monitoring, progress and site visit reporting and project evaluation. Our tests showed that USAID/Philippines internal controls were logically designed and consistently applied except that a system for monitoring host-country contributions was not in place. The USAID/Philippines' assessment of internal

controls for fiscal year 1990, as required by the Integrity Act, showed that reporting procedures for host-country contributions were not in place.

### **Audit Objectives Two and Four**

Audit objectives two and four were to determine whether A.I.D.'s procedures were followed in contracting, monitoring performance, accounting for services and accounting for the obligation and expenditure of A.I.D. funds for construction and engineering contracts. We considered the applicable internal control policies and procedures cited in A.I.D. Handbook 11. For purposes of this report, we classified policies and procedures into the following categories and processes: contractor prequalification, contractor selection, contract award and fund accountability. We reviewed USAID/Philippines internal controls for the acquisition of engineering and construction services. Our tests showed that USAID/Philippines internal controls were logically designed and consistently applied except that, in accounting for the obligation and expenditure of A.I.D. funds for engineering and construction services, voucher verification procedures and contractual requirements were not always followed. We conducted tests to conclusively determine that

- A.I.D.'s funds were committed and paid for host-country taxes,
- mobilization payments were not recouped in accordance with the requirements of the construction contracts and
- the fixed fee was computed erroneously for one technical services contract.

The USAID/Philippines' assessment of internal controls for fiscal year 1990, as required by the Integrity Act, did not identify the lack of verification procedures to preclude the payment of host-country taxes in construction contracts as an area of vulnerability.

### **Audit Objective Three**

**This audit objective was to determine whether A.I.D.'s procedures were followed in obtaining, safeguarding and accounting for commodities and in accounting for the obligation and expenditure of A.I.D. funds. In planning and performing the audit for this objective, we considered applicable internal control procedures in A.I.D. Handbook 15. We classified the relevant policies and procedures into the following categories and processes: procurement planning, specification development, arrival accounting and fund accountability. We reviewed USAID/Philippines internal controls for the procurement of commodities. Our tests showed that USAID/Philippines internal controls were logically designed and consistently applied except that a reporting system for the use of vehicles and the marking of commodities was not developed. The USAID/Philippines' assessment of internal controls for fiscal year 1990, as required by the Integrity Act, did not identify any weaknesses in its reporting system for tracking the use and marking of project commodities.**

---

# **REPORT ON COMPLIANCE**

This section summarizes our conclusions on USAID/Philippines' compliance with applicable laws and regulations under the Rural Infrastructure Fund Project.

---

## **Scope of Our Compliance Assessment**

We conducted our audit in accordance with generally accepted government auditing standards which require that we

- assess compliance with applicable requirements of laws and regulations when necessary to satisfy the audit objectives (which includes designing the audit to provide reasonable assurance of detecting abuse and illegal acts that could significantly affect the audit objectives) and
- report all significant instances of noncompliance and abuse and all indications or instances of illegal acts that could result in criminal prosecution that were found during or in connection with the audit.

We tested USAID/Philippines' compliance with the Foreign Assistance Act of 1961, as amended, the Federal Manager's Financial Integrity Act, the grant agreement and contracts as they could affect our audit objectives. However, our objective was not to provide an opinion on USAID/Philippines' overall compliance with such provisions.

---

## **General Background on Compliance**

Noncompliance is a failure to follow requirements or a violation of prohibitions contained in statutes, regulations, contracts, grants and binding policies and

procedures governing an organization's conduct. Noncompliance constitutes an illegal act when there is a failure to follow requirements of laws or implementing regulations, including intentional and unintentional noncompliance and criminal acts. Not following internal control policies and procedures in the A.I.D. Handbooks generally does not fit into this definition of noncompliance and is included in our report on internal controls.

Abuse is distinguished from noncompliance in that abusive conditions may not directly violate laws or regulations. Abusive activities may be within the letter of the laws and regulations but violate either their spirit or the more general standards of impartial and ethical behavior.

Compliance with Federal laws and regulations, the grant agreement and contracts is the overall responsibility of USAID/Philippines' management.

---

### **Conclusions on Compliance**

USAID/Philippines complied with the applicable provisions of the Foreign Assistance Act of 1961, as amended, the Federal Manager's Financial Integrity Act, the grant agreement and contractual provisions except that

- A.I.D. funds were used to pay for host-country taxes contrary to the provisions of the grant agreement and
- AID-financed commodities were not marked as being provided by the people of the United States as required by Section 641 of the Foreign Assistance Act of 1961.

**SCOPE AND  
METHODOLOGY**

---

**Scope**

We audited USAID/Philippines' Rural Infrastructure Fund Project in accordance with generally accepted government auditing standards. We conducted the audit from February 25 through May 6, 1991. We reviewed construction contracts for three road and two port subprojects, a contract for architectural and engineering services, and commodity procurements. The total reviewed was about \$53 million, or about 40 percent of the \$130 million A.I.D. had obligated as of March 1991. We also tested expenditures for construction services, architectural and engineering services and commodity procurements totaling about \$5 million, or about 30 percent of the \$18 million of A.I.D. expenditures as of March 1991. We conducted our audit work at the offices of USAID/Philippines, the GOP's Department of Public Works and Highways, the consultant engineer and the construction contractors. We inspected project commodities and visited sites of three road subprojects in Capiz, Iloilo and Quezon provinces and two port subprojects in Cebu and Masbate provinces.

---

**Methodology**

The methodology for each audit objective follows.

**Audit Objective One**

To accomplish the first audit objective, we determined A.I.D.'s procedures for project monitoring, reporting and evaluating. We reviewed (1) A.I.D. Handbook 3 requirements on project monitoring, reporting and evaluating (2) the project monitoring, reporting and evaluation plans in the project paper, grant agreement and project implementation letters and (3) USAID/Philippines' system for

monitoring, reporting and evaluating. We discussed with USAID/Philippines and GOP project officials methods and procedures established to monitor, evaluate and report on the status and progress of the project. To verify the information gathered, we (1) obtained copies of the monthly reports prepared by the consultant engineer to ascertain the progress of the project (2) reviewed minutes of weekly meetings held by USAID/Philippines, GOP, consultant engineer, and construction contractor officials and (3) reviewed site visit reports made by USAID/Philippines project officials.

To answer the audit objective, we concluded whether the system (1) identified implementation problems and recommendations for corrective actions, (2) provided procedures for addressing problems and for ensuring that recommendations were being implemented, (3) monitored host-country compliance with legislation and A.I.D. policies and procedures and (4) assured that AID-financed commodities and services were used effectively to produce the intended benefits.

#### **Audit Objectives Two and Four**

To accomplish the second and fourth audit objectives, we determined whether (1) allowable forms of contracts were selected, (2) proper competitive procedures were followed in choosing contractors, (3) contracts provided reasonable assurances that the necessary services would be provided on time and at a fair price, (4) contracts were expeditiously awarded, (5) contractors were capable of performing according to the contract terms, (6) contractors were performing in accordance with the contract's statement of work and (7) contracting and performance data were obtained, maintained and fairly disclosed in reports.

Moreover, we determined whether (1) payments were made in compliance with the Prompt Payment Act of 1982 and OMB implementing guidance provided in Circular A-125; (2) mobilization payments and recoupments were made in accordance with contractual provisions; (3) payments were properly authorized, made in accordance with the commitment documents, and charged to the commitment liquidation records of the subprojects; (4) contractors and the host government were billed for disallowed costs and refunded such costs to A.I.D. in an expeditious manner; (5) vouchers were promptly and properly recorded to appropriate commitment liquidation records and (6) reports were prepared in a timely manner and in accordance with A.I.D. procedures.

To accomplish these ends, we selected the three contracts with the highest dollar values, totaling about \$38 million, out of the nine construction contracts totaling about \$41 million. We also examined the two technical assistance contracts valued at about \$11 million. To determine the project procurement plans for technical and construction services, we examined the project paper, the grant agreement and amendments and project implementation letters. To determine whether A.I.D.'s procedures were complied with, we reviewed advertisements, notices to prospective offerors, lists of prequalified offerors, invitations for bids/requests for technical proposals, selection panel results, cost proposals, memoranda relating to contract negotiations, contracts, A.I.D. approvals, letters of commitment, contractor reports, site visit reports and consultant reports. To determine whether host-country taxes were included in the construction contracts, we analyzed the bid documents and cost analyses of the three construction contracts totaling \$38 million. We also held discussions with construction contractor, consultant engineer, USAID/Philippines and GOP project officials, and we visited the construction sites and assessed the progress of the subprojects.

In addition, we examined commitment liquidation records, cash advance schedules, comprehensive pipeline reports, and vouchers and their supporting documentation. Audit tests focused on the commitment, payment and disbursement processes. Judgmental sampling was used in the selection of vouchers to determine whether the vouchers had been administratively approved and properly certified for payment. In reviewing payments processed by USAID/Philippines, we tested about 60 percent of the payments for construction services listed in the commitment liquidation records, or \$1 million of the \$1.6 million. In addition, we tested 25 percent of the payments for technical services, or \$2 million of the \$8 million.

### **Audit Objective Three**

To accomplish the third objective, we determined whether (1) commodity needs and specifications were adequately reviewed, assessed and identified; (2) A.I.D. purchased any commodities which were ineligible or restricted; (3) commodities were received in accordance with plans and specifications and, if not, whether required actions were taken; (4) commodities were properly stored until needed; (5) commodities were used for the purposes intended and (6) the host country properly reported the receipt, storage and use of the commodities. We examined the project procurement plan, payment vouchers and accompanying documents, contracts, site visit reports, monthly progress reports and related correspondence.

19

To answer this objective, we reviewed 50 percent of the local procurements for office furniture, office equipment and computer equipment, or \$65,000 of the \$130,000 in expenditures. Also, we reviewed about 40 percent of the payment vouchers for navigational aids equipment recorded in the commitment liquidation records, or \$1 million of the \$2.9 million. We also physically inspected \$1.9 million in commodities, consisting primarily of vehicles, navigational aids equipment and computer equipment. These inspections were made at the construction sites of two road subprojects, an international airport, a domestic airport, the consultant engineer's office and GOP's offices. We also interviewed USAID/Philippines, GOP and contractor officials.

---

UNITED STATES GOVERNMENT

APPENDIX II

# Memorandum

TO : Mr. Dennis Smith  
Resident Auditor, RAO/M

DATE: OCT 4 1991

FROM : Malcolm Butler, Director  
USAID/Philippines *mb*

SUBJECT : Draft Report: Audit of Rural Infrastructure  
Fund Project - Project No. 492-0420

REF. : Your Memorandum dated July 19, 1991

We have reviewed the subject draft report and our comments on this report are as follows:

Page 5 - Recommendation No. 1.

"We recommend that USAID/Philippines develop a system for monitoring GOP contributions to the project, including verification of the validity of reported contributions."

In March, 1990 the Mission identified as a problem a lack of data covering counterpart contributions. Unfortunately, we did not have funds available under PD&S funding to fund a study until September, 1990. At that time we funded a study to a) determine the current status of host government counterpart contributions under Mission funded projects and programs and b) in consultation with the government, make recommendations for an appropriate periodic reporting system. The proposals exceeded the amount of funding available which required a reduction in the scope of work. When additional funds became available we funded an expansion of the study, which is currently in process. We anticipate completion during December, 1991. We believe this is responsive to Recommendation No. 1, ask that it be resolved upon issuance, and will request closure after the system is implemented.

Page 9 - Recommendation No. 2.

We recommend that USAID/Philippines:

- 2.1 determine the amount of host-country taxes that were included in host-country contracts and exclude commitments of A.I.D. funds for these amounts,



- 2.2 adopt verification procedures to preclude the payment of identifiable taxes in host-country contracts,
- 2.3 recover from the Government of the Philippines any payments for host-country taxes and
- 2.4 recover from construction contractors under-recouped mobilization payments of about \$110,000.

The Mission disagrees with the statement on page 9 that "USAID/Philippines did not follow review and verification procedures". We did, in fact, follow normal review and verification procedures on this project. We do agree, however, that your review of the detailed cost analyses indicated a problem with the existing procedures, and we are taking steps to improve the procedures accordingly.

Recommendation 2.1. We have begun the process of reviewing detailed cost analyses for contracts in place under the project, and will require this review as a part of procedures for new contracts proposed for financing. The review should be completed in November, 1991. When the review has been completed, we will adjust the amount of funds committed for financing of the contracts, and officially inform the Government of the Philippines and the involved contractors.

Recommendation 2.2. In addition to the steps outlined in response to recommendation 2.1 above, we will require a positive certification by the contractor on each invoice and by the Government of the Philippines on each voucher approval that "no identifiable host-country taxes are included in this request for payment". These certifications will be a new requirement in the voucher certification process.

Recommendation 2.3. Once the analysis proposed in response to recommendation 2.1 has been completed, we will analyze the payments processed under each of the contracts to determine the exact amount of any taxes which may have been included. We will then request reimbursement from the Government of the Philippines.

Recommendation 2.4. Our analysis of the contract in question indicates that the mobilization payment was not paid to the contractor until substantially after the date of the notice to proceed and in fact was within a few days of the processing of the first progress payment. As it was obviously the intent of the provision that the period from receipt of the mobilization to the date of the first recovery be approximately six months,

32

we have adjusted the recoupment, refunding the amounts recovered. We began recoupment again from recent payments which were six months after the date of receipt of the mobilization payment. The Government of the Philippines has now amended the contract to provide for recovery after 20% of the contract has been billed, and we have adjusted the payments accordingly.

We believe these steps are responsive to recommendations 2.1, 2.2, and 2.3 and request that they be closed upon issuance. We believe the GOP action amending the contract corrects the situation for Recommendation No. 2.4 and ask that it also be closed upon issuance.

Page 9 - Recommendation No. 3.

"We recommend that USAID/Philippines report to A.I.D. officials, responsible for internal control matters, that verification procedures did not preclude host-country taxes from being included in host-country construction contracts."

We understand that since taxes were included in the detailed cost analyses of the contracts, and the final contracts are in the same amounts as the totals of the cost analyses, we can reasonably assume that taxes are included in the contract amounts and therefore committed on USAID records. We will follow up with our own analyses of these documents. This recommendation will be referred to the Mission Internal Control Oversight Committee, and to the Management Control Review Committee (MCRC) in AID/Washington. As stated earlier, however, we feel that this is a recommendation which will result in an improvement to and expansion of existing procedures. Since we have agreed to implement the improvement, we do not believe it constitutes a situation which should require this special reporting. In our report to the MCRC, we will indicate our position on this matter, and will request their guidance. Once these reports have been completed, we will request closure of this recommendation.

Page 13 - Recommendation No. 4.

"We recommend that USAID/Philippines require the GOP to provide routine utilization reports that would track

the distribution and use of vehicles and

the marking of AID-financed commodities with the A.I.D. handclasp emblem."

In the discussion of the use of vehicles by Philippine Government officials on page 14, it is important to note that the Mission took timely, aggressive action immediately when we became aware of the situation. The vehicle was, in fact, recovered within less than a month. The requirement for utilization reports would probably not result in more timely action than that exerted in this case. The Mission is acutely aware of the requirements to assure proper utilization of vehicles, and our policy severely restricts the use of A.I.D. funds for vehicle procurement. We agree that improvements could be made to the system for tracking utilization of vehicles and are beginning to implement a system which requires routine periodic reports from the consulting engineers on these projects. We will provide a description of this system's improvement and will request resolution of the first part of Recommendation No. 4.

Earlier reviews of the tracking and control system on commodities indicated that each office had a tracking system which was satisfactory to their needs. These current systems did not effectively track the marking of AID-financed commodities. The Mission is considering alternatives for the development of new systems which will directly address commodity utilization, particularly the marking issue. Once we have agreed on the scope and content of these systems, we will advise you and request resolution of the second part of Recommendation 4.

Page 13 - Recommendation No. 5.

"We recommend that USAID/Philippines report to A.I.D. officials, responsible for internal control matters, that utilization reports have not tracked the marking of AID-financed commodities with the A.I.D. handclasp emblem."

Our comment here is similar to the comment on Recommendation No. 3. We have agreed that the current systems do not adequately address the marking issue, but have also agreed to explore alternative systems which resolve this issue. We believe it to be inappropriate to make interim ad hoc reports to the MCRC on internal control issues unless the Mission response to the issue is unsatisfactory. We have recently been advised that the Mission will be required to do an internal control assessment for 1991. In that assessment we will fully report the issues raised in this audit and the Mission responses, and make an overall determination of our vulnerability in these areas. However, as with our response to Recommendation No. 3, we will report this matter to the Mission Internal Control Oversight Committee, and to the MCRC in Washington, requesting their guidance on the matter. Once the reports have been transmitted, we will request closure of Recommendation No. 5.

Page 17 - Paragraph 2. Discussion of fixed fee.

The statements are correct. The fixed fee was not always adjusted to reflect the changed amount due to disallowances. However, our voucher examination staff is aware of this requirement, and usually makes these adjustments. The failure to properly adjust the amount is therefore a matter of errors, and not indicative of a systems failure. Given the number of payment transactions (about 25,000 annually), a certain level of errors is to be expected. USAID has adjusted the fixed fee payments to this contractor to the correct amount.

cc: Jack Winn , ENE/DP/F, AID/W  
IG/PPO, AID/W  
J. Rudasill-Bey, ENE/DP, AID/W

75

**REPORT DISTRIBUTION**

	<u>No. of Copies</u>
U.S. Ambassador to the Philippines	1
Mission Director, USAID/Philippines	5
Assistant Administrator, Bureau for Asia and Private Enterprise (AA/APRE)	2
Office of the Philippines, Cambodia, Afghanistan and Pakistan Affairs (APRE/PCAP)	2
Office of External Affairs (XA)	2
Office of Press Relations (XA/PR)	1
Bureau for Legislative Affairs (AA/LEG)	1
Office of the General Counsel (GC)	1
Assistant to the Administrator for Management Services (AA/MS)	2
Office of Financial Management (FM/FPS)	2
Center for Development Information and Evaluation (PPC/CDIE)	3

No. of Copies

**Office of the Inspector General**

<b>Inspector General (IG)</b>	<b>1</b>
<b>Assistant Inspector General for Audit (AIG/A)</b>	<b>1</b>
<b>Financial Audits (IG/A/FA)</b>	<b>1</b>
<b>Policy, Plans and Oversight (IG/A/PPO)</b>	<b>2</b>
<b>Programs and Systems Audits (IG/A/PSA)</b>	<b>1</b>
<b>Legal Counsel (IG/LC)</b>	<b>1</b>
<b>Resource Management (IG/RM)</b>	<b>12</b>
<b>Assistant Inspector General for Investigations (AIG/I)</b>	<b>1</b>

**Regional Inspectors General**

<b>RIG/A/Cairo</b>	<b>1</b>
<b>RIG/A/Dakar</b>	<b>1</b>
<b>RIG/A/Europe</b>	<b>1</b>
<b>RIG/A/Nairobi</b>	<b>1</b>
<b>RIG/A/Singapore</b>	<b>1</b>
<b>RIG/A/Tegucigalpa</b>	<b>1</b>
<b>RIG/I/Singapore</b>	<b>1</b>