

**Regional Inspector General for Audit
Singapore**

**AUDIT OF
ENGINEERING SCIENCE INC.
SRI LANKA**

**Report No. 5-383-92-09-N
January 17, 1992**



PD-A13D-695
ISN 75465

**AUDIT OF
ENGINEERING SCIENCE INC.
SRI LANKA**

AUDIT REPORT NO. 5-383-92-09-N

JANUARY 17, 1992

The auditors reported that the Fund Accountability Statement presents fairly Engineering Science Inc.'s income and expenditures under its contract with USAID/Sri Lanka, except that \$2.1 million in overhead was paid on the basis of provisional rates even though final rates were required. This was considered to be a material instance of non-compliance. While an additional \$10,000 was identified as being unallowable, no material internal controls weaknesses were disclosed and there were only a few other instances of non-compliance mentioned.

**CONTRACTOR INFORMATION CONTAINED IN
THIS REPORT MAY BE PRIVILEGED. THE
RESTRICTIONS OF 18 USC 1905 SHOULD BE
CONSIDERED BEFORE ANY INFORMATION IS
RELEASED TO THE PUBLIC.**

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT
OFFICE OF THE REGIONAL INSPECTOR GENERAL FOR AUDIT
— Singapore —

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January 17, 1992

MEMORANDUM FOR: Richard Brown
Mission Director, USAID/Sri Lanka

FROM: 
Alfred M. Clavelli, Acting RIG/A/Singapore

SUBJECT: Audit of Engineering Science Inc. - Sri Lanka
Audit Report No. 5-383-92-09-N

The audit firm of Coopers and Lybrand, Singapore performed a financial audit of USAID/Sri Lanka's contract with the Engineering Science Inc. in Sri Lanka. Five copies of the audit report are enclosed for your action.

Under the Water Supply and Sanitation Project, USAID/Sri Lanka contracted with Engineering Science Inc. to provide professional management, technical assistance, consulting services, training, commodities and other relevant services required to assist the Government of Sri Lanka in upgrading both the coverage and quality of Sri Lanka's water supply and sanitation. Activities under the project include the building of institutional capabilities, improving health education, and increasing community development. Engineering Science Inc. received \$6,030,735 from USAID/Sri Lanka under its contract during the audit period of April 1, 1985 through March 31, 1991.

The audit objectives were to: (1) determine whether Engineering Science Inc.'s Fund Accountability Statement presents fairly the income and expenditures incurred under its contract with USAID/Sri Lanka and whether the expenditures were allocable, allowable and reasonable; (2) report on Engineering Science Inc.'s system of internal controls; and (3) report on Engineering Science Inc.'s compliance with applicable laws, regulations and contract terms.

The auditors reported that the Fund Accountability Statement presents fairly Engineering Science Inc.'s income and expenditures under its contract with USAID/Sri Lanka, except that \$2.1 million in overhead was paid on the basis of provisional rates even though final rates were required. This was considered to be a material instance of non-compliance. While an additional \$10,000 was identified as being unallowable, no material internal controls weaknesses were disclosed. There were, however, other instances of non-compliance relating to air travel claims and tagging of non-expendable property.

Engineering Science Inc. officials agreed with the auditors' findings and recommendations except for the issue of non-negotiated overhead rates. Their comments are included as Appendix C to the report.

We are making the following recommendations to be included in the Inspector General recommendation follow-up system.

Recommendation No. 1: We recommend that USAID/Sri Lanka obtain the final overhead rates applicable to its contract with Engineering Science Inc., resolve the \$2,104,490 in questioned costs relating to overheads paid, and recover any amounts determined to be unallowable.

Recommendation No. 2: We recommend that USAID/Sri Lanka recover \$9,691 (\$938 and \$8,753) relating to rents and air travel paid to Engineering Science Inc.

Recommendation No. 3: We recommend that USAID/Sri Lanka obtain a complete list of all non-expendable property purchased under the contract from Engineering Science Inc., and on a sample basis, verify the existence, condition or proper disposition of these properties.

We appreciate the courtesies and cooperation the Mission and the Engineering Science Inc. extended to the auditors and our staff during the course of this audit.

Please advise me within 30 days of any actions planned or taken to close the above recommendations.

AUDIT OF
ENGINEERING SCIENCE INC.
AND ITS CONTRACT WITH
USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO 383-0088-C-00-5011-00)

AUDIT PERIOD APRIL 1, 1985 TO MARCH 31, 1991

Performed and prepared

by

Coopers & Lybrand
Singapore

AUDIT OF
ENGINEERING SCIENCE INC.
AND ITS CONTRACT WITH
USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO 383-0088-C-00-5011-00)

INDEPENDENT AUDITORS' REPORT

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your reference A6/PJW/9281
our reference

Mr James B Durnil
Regional Inspector General
for Audit, Singapore,
US Agency for International Development
#17-03 Peninsula Plaza
111 North Bridge Road
Singapore 0617

January 6, 1992

Dear Mr Durnil

This report presents the results of our audit of Engineering Science Inc. ("ESI") and its contract with the United States Agency for International Development, Sri Lanka ("USAID/SL") on the Water Supply and Sanitation Project ("WSSP") Contract No 383-0088-C-00-5011-00 for the period April 1, 1985 to March 31, 1991.

Background - Sri Lanka

Sri Lanka is an island, separated from the subcontinent of India by the Palk Strait. In 1985, the population stood at 15.2 million with a racial make-up of 74 percent Sinhalese, 12.6 percent Sri Lankan Tamils, 5.5 percent Indian Tamils, 7.1 percent Moors, and 0.8 percent "others". Topographically, Sri Lanka has a central mountain mass which is surrounded by broad plains, plateaus, and valleys. About 72 percent of the population live within the rural areas, concentrated in 25,000 villages spread throughout most parts of the island.

The quality of domestic water supply and sanitation in Sri Lanka has not been of a high standard for a less developed country. It ranks among the bottom third of such countries in the world. The Government of Sri Lanka ("GSL") endorsed a Decade Plan in 1980 to upgrade substantially both the coverage and quality of the nation's water supply and sanitation programs.

The National Water Supply and Drainage Board ("NWSDB") was designated the principal agency for administering the Decade Plan.

USAID's Involvement in the Project

In 1984, USAID/SL authorized the WSSP as part of the GSL's Decade Plan. The objectives of the project were to strengthen the NWSDB's institutional capabilities, improve health education, and increase community participation. Project outputs were to include a revised organizational structure for the NWSDB, construction and renovation of workshops, offices, and other facilities, and construction or rehabilitation of six water schemes.

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Mr James B Durnil
Regional Inspector General
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US Agency for International Development
Singapore

The total estimated cost of the project, which was to be completed by August 1989, was US\$19.6 million, with USAID/SL and the GSL providing US\$12.3 million and US\$7.3 million, respectively. Most of USAID/SL's funds, which comprised a US\$7.3 million loan and a US\$5 million grant, were to pay for technical assistance, construction/rehabilitation of water schemes, commodities, and facility construction.

Pursuant to the project, USAID/SL contracted with Engineering Science Inc. ("ESI"), an independent U.S. contractor, in April 1985 to provide professional management, technical assistance, consulting services, training and commodity procurement and other relevant services required to assist the GSL in attaining the objectives of the WSSP.

USAID/SL was to monitor project implementation to ensure effective use of AID funds, and compliance with the terms and conditions of the project.

ESI's contract

The ESI contract with USAID/SL was a cost plus fixed fee type contract which, including contract extensions and modifications up to June 1990, provided for US\$7,291,851 in estimated cost and fees covering a period of performance from April 1, 1985 through August 31, 1991.

Audit Objectives and Scope of Work

We conducted a financial audit of ESI's Fund Accountability Statement pertaining to its contract with USAID/SL for the period from April 1, 1985 through March 31, 1991. The Fund Accountability Statement comprises the income and expenditure statement for the period from April 1, 1985 to March 31, 1991 and the notes thereon. As stated in note 2 on page 10, it is not intended to present fairly the income and expenditure of ESI as a whole. The results of our work are reflected in the accompanying Independent Auditors' Reports on the following:

- (a) Fund Accountability Statement;
- (b) System of Internal Control; and
- (c) Compliance with Agreement Terms, Applicable Laws and Regulations.

Mr James B Durnil
Regional Inspector General
for Audit, Singapore
US Agency for International Development
Singapore

The objectives of our work were to determine whether:

- (a) the Fund Accountability Statement for ESI presents fairly the Company's costs incurred and fees covering the period from April 1, 1985 to March 31, 1991 in accordance with generally accepted accounting principles and the terms of the contract with USAID/SL. Any costs not fully supported with adequate records or which were not considered allocable, reasonable or allowable under the terms of the contract have been identified and questioned.
- (b) ESI's internal accounting controls are adequate to provide reasonable assurance that the assets of ESI are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with ESI management's authorization and are properly recorded to permit the preparation of vouchers or invoices in accordance with the contract.
- (c) ESI has complied with applicable laws, regulations and contract terms.

Our audit was conducted in accordance with generally accepted auditing standards and US Government Auditing Standards and, accordingly, included such tests as were considered necessary in order to determine whether expenditure charged to the contract was in accordance with the contract terms, or other applicable program documents, and the laws of Sri Lanka.

The scope of our work primarily included the following general procedures:

- (a) Holding meetings with USAID/SL, ESI and AID Regional Inspector General for Audit/Singapore ("RIG/S") officials;
- (b) Reviewing the contract between USAID/SL and ESI, including all amendments and modifications, action plans, pertinent sections of the AID standard provisions, and correspondence and minutes of meetings between USAID/SL and ESI; as well as project reports maintained by ESI and USAID/SL;

Mr James B Durnil
Regional Inspector General
for Audit, Singapore
US Agency for International Development
Singapore

- (c) Obtaining an understanding of the accounting, administrative and internal control systems of ESI using questionnaires, interviews, flowcharts and narrative descriptions;
- (d) Devising and performing appropriate tests on the transactions recorded in the Fund Accountability Statement;
- (e) Designing appropriate audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, and illegal acts that could have a direct and material effect on the results of our audit. We were also aware of the possibility of illegal acts that could have an indirect and material effect on the results of our audit; and
- (f) Testing the effectiveness of administrative controls applied by ESI's management in order to ensure compliance with applicable laws, regulations and agreement terms.

Audit Results

(a) Opinion on Fund Accountability Statement

ESI has not negotiated the final overhead rates with USAID/SL in accordance with section 52.216-7 of the Federal Acquisition Regulations. Furthermore, we are unable to review the reasonableness of the provisional overhead rates set out in the contract between USAID/SL and ESI as we have not been provided with adequate information on the determination of those rates. Consequently, we are unable to determine the reasonableness of the overheads charged to the Fund Accountability Statement by other auditing procedures. The overheads amounted to US\$2,104,490.

In our opinion, except for the effects of any adjustments which might have been determined to be necessary if the information referred to above were made available to us, the Fund Accountability Statement presents fairly, in all material respects, the income and expenditure of ESI for the period April 1, 1985 to March 31, 1991 in conformity with generally accepted accounting principles and the terms of the contract with USAID/SL.

Mr James B Durnil
Regional Inspector General
for Audit, Singapore
US Agency for International Development
Singapore

(b) System of Internal Controls

In planning and performing our audit of the Fund Accountability Statement of ESI, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the statement.

For all the significant internal control structure categories examined, we obtained an understanding of the design of relevant policies and procedures and whether they had been placed in operation, and we assessed control risk.

We noted no matters involving the internal control structure and its operation that we consider to be a material weakness. However, we noted certain other matters involving the internal control structure and its operation that we have reported to the management of ESI in a separate letter dated December 23, 1991.

(c) Compliance with Agreement Terms, Applicable Laws and Regulations

Our tests for compliance with agreement terms, applicable laws and regulations of selected transactions and records of ESI indicated that, for the items tested, ESI complied with those provisions of the agreement terms, as well as applicable laws and regulations, for the period under our review, except in the following areas:

- 1 Final overhead rates have not been agreed and negotiated in accordance with FAR 52.216-7 regulations. Furthermore, there was inadequate evidence that the provisional rates had been determined in accordance with the procedures prescribed by FAR 42.704(a).
- 2 Travel costs were overclaimed by US\$938, pertaining to travel by the dependent spouse of an employee who was not a "regular employee", in contravention of AID Acquisition Regulations ("AIDAR").
- 3 Property management provisions regarding the tagging of equipment procured with US Government funds have not been fully complied with.
- 4 Double payments totalling to US\$8,753 were erroneously claimed by ESI and paid by USAID/SL.

Mr James B Durnil
Regional Inspector General
for Audit, Singapore
US Agency for International Development
Singapore

The noted exceptions have been discussed further in both our detailed report, and in Appendix A (Questioned Costs as to Reasonableness, Allocability and Allowability). We consider the matter noted in (c) 1 above to be a material instance of non-compliance. This matter has also led to a qualification to our opinion on the Fund Accountability Statement as noted on page 4, subparagraph (a) above and in our detailed finding on pages 18 to 20 of this report. The overall result of the other non-compliance issues noted is not considered to have a material effect on the Fund Accountability Statement of ESI for the period under our review.

With respect to transactions and records not tested by us, nothing came to our attention that caused us to believe that ESI had not complied in all material respects with the necessary agreement terms, applicable laws or regulations.

Status of Prior Audit Reports

No prior audits were carried out of ESI's contract with USAID/SL.

Comments on Findings and Recommendations

Except for finding 1 on pages 18 to 20, the management of ESI have agreed to our findings and recommendations on both questioned costs and compliance issues. The details of these recommendations and findings are set out in Appendix A and pages 18 to 24, respectively. Steps have already been taken to rectify a number of the items.

Acknowledgements

We would like to take this opportunity to express our gratitude for the assistance given to us by the RIG/S office, USAID/SL and the management and staff of ESI during the course of our audit.

Yours truly



REPORT ON THE
FUND ACCOUNTABILITY STATEMENT

your reference A6/PJW/9281
our reference

Mr James B Durnil
Regional Inspector General
for Audit, Singapore,
US Agency for International Development
17-03 Peninsula Plaza
111 North Bridge Road
Singapore 0617

Dear Mr Durnil

ENGINEERING SCIENCE INC. AND ITS CONTRACT
WITH USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO. 383-0088-C-00-5011-00)

INDEPENDENT AUDITORS' REPORT ON THE FUND
ACCOUNTABILITY STATEMENT

We have audited the Fund Accountability Statement of Engineering Science Inc. ("ESI") pertaining to its contract with the United States Agency for International Development, Sri Lanka ("USAID/ SL") on the Water Supply and Sanitation Project for the period April 1, 1985 to March 31, 1991. The Statement, comprising the income and expenditure statement and the notes thereon, as set out on pages 9 and 10, is the responsibility of ESI's management. Our responsibility is to express an opinion on the Statement based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and US Government Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.



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ENGINEERING SCIENCE INC. AND ITS CONTRACT
WITH USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO. 383-0088-C-00-5011-00)

INDEPENDENT AUDITORS' REPORT ON THE FUND
ACCOUNTABILITY STATEMENT

As stated in note 2 on page 10, the Fund Accountability Statement presents only the transactions of ESI as they pertain to its contract with USAID/SL for the period April 1, 1985 to March 31, 1991 and is not intended to present fairly the income and expenditure of ESI as a whole.

ESI has not negotiated the final overhead rates with USAID/SL in accordance with section 52.216-7 of the Federal Acquisition Regulations (refer Finding 1 on page 18.) Furthermore, we are unable to review the reasonableness of the provisional overhead rates set out in the contract between USAID/SL and ESI as we have not been provided with adequate information on the determination of those rates. Consequently, we are unable to determine the reasonableness of the overheads charged to the Fund Accountability Statement by other auditing procedures. The overheads amounted to US\$2,104,490.

In our opinion, except for the effects of any adjustments which might have been determined to be necessary if the information referred to in the 4th paragraph above was made available to us, the Fund Accountability Statement referred to above presents fairly, in all material respects, the income and expenditure of ESI for the period April 1, 1985 to March 31, 1991 in conformity with generally accepted accounting principles.

This report is intended solely for the use of USAID/SL and should not be used for any other purpose. This restriction is not intended to limit the distribution of this report which, upon acceptance by the USAID Regional Inspector General for Audit, Singapore, is a matter of public record.


COOPERS & LYBRAND
Certified Public Accountants

January 6, 1992

ENGINEERING-SCIENCE INC.

FUND ACCOUNTABILITY STATEMENT

FOR THE PERIOD FROM APRIL 1, 1985 TO MARCH 31, 1991

US\$

INCOME

Funds received from USAID/Sri Lanka 6,030,735

EXPENDITURE

Salaries and Wages 1,965,218

Overheads 2,104,490

Consultants 2,831

Allowances 317,154

Travel and transportation 151,995

Non-expendable equipment and supplies 109,052

Participant training 176,920

Other direct costs 601,233

Sub-contracts 617,164

Fixed fee 412,225

6,458,282
=====

Funds to be reimbursed by USAID/Sri Lanka:

Difference between income and expenditure 427,547

Add back late payment interest received 15,328
and included above

USAID/SL owes ES 442,875
=====

C. J. G. Thompson
C.J.G. Thompson
Principal Officer

ENGINEERING SCIENCE INC.

Notes to the Fund Accountability Statement
for the period April 1, 1985 to March 31, 1991

1 Significant Accounting Policies

- (a) The Fund Accountability Statement, expressed in US dollars, is prepared in accordance with the historical cost convention.
- (b) Expenditure is accounted for on an accruals basis. Income relates to amounts actually received.
- (c) Transactions arising in foreign currencies are translated to US dollars at rates of exchange closely approximating those ruling on the transaction dates.

2 Component unit of ESI

The Fund Accountability Statement of ESI presents only the transactions pertaining to its contract with USAID/SL as they relate to services provided directly or indirectly, and are not intended to present fairly the income and expenditure of ESI as a whole.

3 Overhead Costs

Overhead costs are based on fixed rates in relation to direct salary costs. The rates are as follows:

	April 1, 1985 to September 30, 1988	October 1, 1988 to May 31, 1990	June 1, 1990 to September 30, 1990	October 1, 1990 to March 31, 1991
	%	%	%	%
Home office staff	120	130	130	135
Field staff (Professional)	105	118	123	123
Field staff (Non-professional)	25	40	65	65

These rates are unaudited provisional rates as stated in the contract.

REPORT ON THE SYSTEM OF INTERNAL CONTROLS

your reference A6/PJW/9281
our reference

Mr James B Durnil
Regional Inspector General
for Audit, Singapore,
US Agency for International Development
17-03 Peninsula Plaza
111 North Bridge Road
Singapore 0617

Dear Mr Durnil

ENGINEERING SCIENCE INC. AND ITS CONTRACT
WITH USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO. 383-0088-C-00-5011-00)

INDEPENDENT AUDITORS' REPORT ON THE SYSTEM OF
INTERNAL CONTROLS

We have audited the Fund Accountability Statement of Engineering Science Inc. ("ESI") pertaining to its contract with the United States Agency for International Development, Sri Lanka ("USAID/SL") on the Water Supply and Sanitation Project for the period April 1, 1985 to March 31, 1991. The Statement, and the notes thereon, are set out on pages 9 and 10. We have issued our report thereon dated January 6, 1992.

We conducted our audit in accordance with generally accepted auditing standards and the standards for financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Financial Statement is free of material misstatement.

In planning and performing our audit of the Fund Accountability Statement of ESI, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the statement and not to provide assurance on the internal control structure of ESI as a whole.



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ENGINEERING SCIENCE INC. AND ITS CONTRACT
WITH USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO. 383-0088-C-00-5011-00)

INDEPENDENT AUDITORS' REPORT ON THE SYSTEM OF
INTERNAL CONTROLS

The management of ESI is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that the assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of the statement in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

Accounting Controls:

- Cash receipts
- Cash disbursements
- Payroll
- General ledger
- Property and equipment

Administrative Controls:

- Cost allocation and allowability
- Monitoring
- Reporting

For all the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they had been placed in operation, and we assessed control risk.

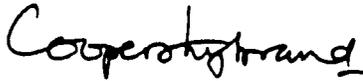
ENGINEERING SCIENCE INC. AND ITS CONTRACT
WITH USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO. 383-0088-C-00-5011-00)

INDEPENDENT AUDITORS' REPORT ON THE SYSTEM OF
INTERNAL CONTROLS

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of the specific internal control structure elements does not reduce, to a relatively low level, the risk that errors or irregularities, in amounts that would be material in relation to the Statement being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned tasks. We noted no matters involving the internal control structure and its operation that we consider to be material weaknesses as defined above.

However, we noted certain matters involving the internal control structure and its operation that we have reported to the management of ESI in a separate letter dated December 23, 1991.

This report is intended solely for the use of USAID/SL and should not be used for any other purpose. This restriction is not intended to limit the distribution of this report which, upon acceptance by the USAID Regional Inspector General for Audit, Singapore, is a matter of public record.


COOPERS & LYBRAND
Certified Public Accountants

January 6, 1992

REPORT ON COMPLIANCE WITH AGREEMENT
TERMS, APPLICABLE LAWS AND REGULATIONS

your reference **A6/PJW/9281**
our reference

Mr James B Durnil
Regional Inspector General
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US Agency for International Development
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Dear Mr Durnil

**ENGINEERING SCIENCE INC. AND ITS CONTRACT
WITH USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO. 383-0088-C-00-5011-00)**

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH
AGREEMENT TERMS, APPLICABLE LAWS AND REGULATIONS**

We have audited the Fund Accountability Statement of Engineering Science Inc. ("ESI") pertaining to its contract with the United States Agency for International Development, Sri Lanka ("USAID/SL") on the Water Supply and Sanitation Project for the period April 1, 1985 to March 31, 1991. The Statement, and the notes thereon, are set out on pages 9 and 10. We have issued our report thereon dated January 6, 1992.

We conducted our audit in accordance with generally accepted auditing standards and the standards for financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Financial Statement is free of material misstatement.

Compliance with laws, regulations, contracts, grants and binding policies and procedures applicable to ESI's contract with USAID/SL is the responsibility of ESI's management. As part of our audit, we performed tests of ESI's compliance with certain provisions of laws, regulations, contracts, grants and binding policies and procedures. However, it should be noted that, whilst we performed those tests of compliance as part of obtaining reasonable assurance about whether the Statement is free of material misstatement, our objective was not to provide an opinion on compliance with such provisions.



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ENGINEERING SCIENCE INC. AND ITS CONTRACT
WITH USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO. 383-0088-C-00-5011-00)

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH
AGREEMENT TERMS, APPLICABLE LAWS AND REGULATIONS

Material instances of non-compliance are violations of laws, regulations, contracts, grants, or binding policies and procedures that cause us to conclude that the aggregation of misstatements resulting from those violations is material to the financial statement. The results of our tests of compliance disclosed an instance of non-compliance which may have a material effect on the Fund Accountability Statement set out on page 9.

ESI has not negotiated final overhead rates with USAID/SL in accordance with Section 52.216-7 of the Federal Acquisition Regulations. Furthermore, we are unable to review the reasonableness of the provisional overhead rates set out in the contract between USAID/SL and ESI as we have not been provided with adequate information on the determination of those rates. This material instance of non-compliance with regulations is set out in detail on pages 18 to 20.

We considered this material instance of non-compliance in forming our opinion on whether ESI's Fund Accountability Statement for the period April 1, 1985 to March 31, 1991, and as set out on page 9, is presented fairly, in all material respects, in conformity with generally accepted accounting principles, and this report has led to a qualification of our report dated January 6, 1992 on the Fund Accountability Statement.

Our testing of transactions and records disclosed instances of non-compliance with laws and regulations. All instances of non-compliance that we found are identified in the accompanying schedules of findings and questioned costs on pages 18 to 24 and Appendix A respectively.

Except as described in the fifth paragraph of this report, the results of our tests indicate that with respect to the items tested, ESI complied, in all material respects, with the provisions referred to in the third paragraph of this report. With respect to items not tested, nothing came to our attention that caused us to believe that ESI had not complied, in all material respects, with those provisions.

ENGINEERING SCIENCE INC. AND ITS CONTRACT
WITH USAID, SRI LANKA
ON THE WATER SUPPLY AND SANITATION PROJECT
(CONTRACT NO. 383-0088-C-00-5011-00)

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH
AGREEMENT TERMS, APPLICABLE LAWS AND REGULATIONS

This report is intended solely for the use of USAID/SL and should not be used for any other purpose. This restriction is not intended to limit the distribution of this report which, upon acceptance by the USAID Regional Inspector General for Audit, Singapore, is a matter of public record.


COOPERS & LYBRAND
Certified Public Accountants

January 6, 1992

ENGINEERING SCIENCE INC.

SUMMARY OF AUDIT FINDINGS ON COMPLIANCE ISSUES

- 1 Final overhead rates have not been agreed and negotiated in accordance with FAR 52.216-7 regulations. Furthermore, there was inadequate evidence that the provisional rates had been determined in accordance with the procedures prescribed by FAR 42.704(a).
- 2 Travel costs were overclaimed by US\$938, pertaining to travel by the dependent spouse of an employee who was not a "regular employee", in contravention of AIDAR.
- 3 Property management provisions regarding the tagging of equipment procured with US Government funds have not been fully complied with.
- 4 Double payments totalling to US\$8,753 were erroneously claimed by ESI and paid by USAID/SL.

ENGINEERING SCIENCE INC.

SCHEDULE OF FINDINGS OF NON-COMPLIANCE

1 OVERHEADS

Condition

The contract between ESI and USAID/SL provides for overhead costs based on provisional overhead rates to be charged to the contract. The provisional overhead rates set out in the contract are as follows:

	April 1, 1985 to September 30, 1988	October 1, 1988 to May 31, 1990	June 1, 1990 to September 30, 1990	October 1, 1990 to March 31, 1991
	%	%	%	%
Home office staff	120	130	130	135
Field staff (Professional)	105	118	123	123
Field staff (Non-professional)	25	40	65	65

Final overhead rates have not been negotiated and agreed between ESI and USAID/SL for the fiscal years of the contractor falling within the period under our review. The latest available final overhead rate relates to the 1983 fiscal year of the contractor. Furthermore, we were unable to obtain adequate information on the detailed make up of the provisional overhead rates to enable us to review their reasonableness. Although some information was received concerning one of the nine rates, this was, however, in an unaudited form and in our opinion not adequate to determine the reasonableness of the provisional overhead rates to be used for the contract. We have also not seen evidence that the provisional overhead rates had been reviewed for their reasonableness by AID officers before being incorporated into the contract.

Criteria

Where a provisional overhead rate is applied in a contract, FAR 52.216-7 requires the contractor to submit within 90 days after its fiscal year end to the cognizant contract officer (or cognizant Government auditor) a proposed final indirect cost rate together with supporting documents so that a final indirect cost rate can be determined.

FAR 42.704(a) requires the cognizant contracting officer (or cognizant Government auditor) to establish the billing rate on the basis of information resulting from recent review, previous audits or experience, or similar reliable data or experience of other contracting activities. The term billing rate includes provisional rates established for interim reimbursement.

ENGINEERING SCIENCE INC.

SCHEDULE OF FINDINGS OF NON-COMPLIANCE

1 OVERHEADS (CONTINUED)

Effect

The reasonableness of the overhead costs, amounting to US\$2,104,490, charged to the ESI contract cannot be determined. The costs of US\$2,104,490 have therefore been questioned. Refer Appendix A.

Cause

We were informed by the project manager that the determination of the final overhead rates had not been carried out because the results of the audit of ESI in the US were not communicated to the contractor's employees in Sri Lanka.

Information of the detailed breakdown of eight of the provisional overhead rates was not available either at ESI or USAID/SL.

Recommendation

It is recommended that the final fixed overhead rates be determined in accordance with Sub 42.7 of the FAR and any excess overhead costs already paid should be recovered by USAID/SL. In future contracts, where provisional overhead rates are used, USAID/SL should specifically set out the procedures determining the finalization of the overhead rates in the contract and a cognizant contract officer be identified to negotiate the final overhead rates. All overhead rates (provisional or final) should be supported by proper documentation including a detailed breakdown to enable the review of their reasonableness by appropriate AID officers.

Management's Comments

ESI does a substantial volume of business with several federal agencies. Final overhead rates are submitted by the Company annually to our cognizant federal agency in accordance with Federal Acquisition Regulations, which, for the period of performance of the subject contract was USEPA. These overhead rates are audited periodically on behalf of USEPA and the results are made available to other government agencies including USAID.

Upon award of the subject contract and for each extension, breakdown details of the provisional home office overhead rates were presented to the responsible USAID Contracting Officer, discussed and agreed and included in the addendum signed by ESI and USAID.

In light of the above comments we believe ESI is in compliance with regulations regarding final and provisional overhead rates.

ENGINEERING SCIENCE INC.

SCHEDULE OF FINDINGS OF NON-COMPLIANCE

1 OVERHEADS (CONTINUED)

Auditor's Comments

Concerning ESI management's comments, regarding the availability of information supporting the overhead rates, we note that we were not provided with such information during our audit fieldwork. Upon requesting details from the USAID Contracting Officer, the only information provided was that noted in the comments above in the 2nd paragraph of this finding on page 18. Furthermore, ESI management in its comments above has made no mention of the availability or otherwise of details to support the provisional field staff overhead rates.

ENGINEERING SCIENCE INC.

SCHEDULE OF FINDINGS OF NON-COMPLIANCE

2 CLAIM FOR TRAVEL REIMBURSEMENT

Condition

In January 1986, ESI wrongly submitted a claim for travel expenses of the spouse of an employee who was not a "regular employee" (refer below for definition).

Criteria

Clause 752.7002(g) of the AIDAR states that "travel costs and allowances will be allowed only for dependents of regular employees". A regular employee is defined as "a contractor employee appointed to serve one year or more in the cooperating country". [AID Handbook 14 - AID Definition Clause. Supplemented for AID contracts involving performance overseas (December 1986)].

Effect

This has resulted in an overclaim by ESI, of US\$938, representing the travel costs of the spouse of the employee.

Cause

There was a misunderstanding on the part of the management of ESI on the definition of a regular employee.

Recommendation

USAID/SL should recover the amount of US\$938 overclaimed for reimbursement from ESI.

Management's Comments

ESI has strengthened its billing procedures in Sri Lanka to prevent recurrence and it is agreed the overbilled amount of US\$938 should be deducted from our final billing due to be submitted by the end of February 1992.

ENGINEERING SCIENCE INC.

SCHEDULE OF FINDINGS OF NON-COMPLIANCE

3 NON-TAGGING OF EQUIPMENT BOUGHT
WITH US GOVERNMENT FUNDS

Condition

ESI has not tagged the following equipment purchased under the project, to indicate that the property had been procured using US Government funds.

- Wang computer, Keyboard and CPU
- 2 STAG voltage regulators/stabilizers
- 1 Cellac inverter
- Acer computer, Keyboard and monitor

Criteria

Clause 752.7009 of the AIDAR requires the tagging of all equipment with distinguishing marks which identify its procurement using US Government funds.

Effect

USAID funded equipment has not been correctly identified to ensure it does not become co-mingled with other non-AID funded equipment, and is therefore susceptible to unauthorized disposition.

Cause

The non-tagging of the assets resulted from an oversight on the part of ESI management. Furthermore, periodic checks were not made to ensure compliance with the applicable regulations.

Recommendation

ESI should submit to USAID/SL a list of all assets under the contract. USAID/SL should ensure the proper disposition of all items, particularly those that were not tagged.

Management's Comments

ESI acknowledges that procedures for tagging of government property had not been fully implemented. Such tagging has now been fully implemented.

ENGINEERING SCIENCE INC.

SCHEDULE OF FINDINGS OF NON-COMPLIANCE

4 DOUBLE CLAIMS

Condition

We came across the following double claims of expenses:

	US\$
a) a double claim for house rental of an ESI employee was made in the month of January 1991	623
b) a double claim of cost of airfares for three National Water Sanitation and Drainage Board participants for overseas training courses in September and October 1987 was made	8,130

	<u>8,753</u>

Criteria

In accordance with Office of Management and Budget ("OMB") circular A-122 requirements, only reasonable amounts of expense should be claimed. Specifically, Sub-A 3(b) of the circular includes generally accepted sound business practices as a factor to consider in determining the reasonableness of a given cost. Such practice prohibits the double claiming of expenses.

Effect

Unauthorized expense reimbursements amounting to US\$8,753 have been claimed by ESI and paid by USAID/SL.

Cause

The double claim for rental arose because of a programming error (isolated case which only affected the specific rental transaction for that particular month).

The double claim for travelling expense arose because photocopies of original invoices, which were not cancelled after payment, were presented to USAID/SL for payment.

ENGINEERING SCIENCE INC.

SCHEDULE OF FINDINGS OF NON-COMPLIANCE

4 DOUBLE CLAIMS (CONTINUED)

Recommendation

It would appear that the double claim for rental was an isolated incident and arose from a human error in programming. It is recommended that the project officer review all new changes in programmed payments.

USAID/SL should require that contractors only submit original invoices for reimbursement of expenses and all invoices should be cancelled with a paid stamp after payment in order to ensure that they are not represented for reimbursement.

USAID/SL should recover the amount of US\$8,753 overclaimed for reimbursement from ESI.

Management's Comments

ESI has strengthened its billing procedures in Sri Lanka to prevent recurrence and it is agreed the overbilled amount of US\$8,753 should be deducted from our final billing due to be submitted by the end of February 1992.

ENGINEERING SCIENCE INC.

Appendix A

QUESTIONED COSTS AS TO REASONABLENESS, ALLOCABILITY AND ALLOWABILITY

Line item	Condition	Basis of questionability	Amount US\$
1 Overhead (Finding 1)	Final overhead rates have not been determined. There is also inadequate supporting information of the provisional overhead rates to ascertain the reasonableness of overheads charged for the period	Reasonableness - Cannot be determined	2,104,490
2 Travel and Transportation (Finding 2)	A claim for air-ticket expenses for spouse of non-regular employee professional staff	Allowability - Costs are not permissible under AID regulations	938
3 Other Direct Cost (Finding 4)	A double claim for rent in the month of January 1991	Reasonableness - Unable to claim for two recoveries in the same period	623
4 Participant Training (Finding 4)	Double claim of cost of airfares for 3 NWSDB participants in September and October 1987	Reasonableness - Unable to claim twice for same cost	8,130
		Total	----- 2,114,181 *****

-25-

Appendix B

12 December, 1991

Coopers & Lybrand
Orchard Point P.O. Box 285
Singapore 9123
9 Penang Road # 1200
Park Mall Singapore 0823

Attention: Mr. Philip Woodburn

Re: Audit Report - Water Supply and Sanitation Project, Sri Lanka

Dear Mr. Woodburn:

I apologize for the delay in furnishing an answer to the subject audit report which was caused by the fact that Mr. Tomasides was on leave and by the difficulties inherent in international communications. Our responses are as follows:

Engineering - Science does a substantial volume of business with several federal agencies. Final overhead rates are submitted by the Company annually to our cognizant federal agency in accordance with Federal Acquisition Regulations, which, for the period of performance of the subject contract was USEPA. These overhead rates are audited periodically on behalf of EPA and the results are made available to other government agencies including USAID.

Upon award of the subject contract and for each extension, breakdown details of the provisional home office overhead rates were presented to the responsible USAID Contracting officer, discussed and agreed and included in the addendum signed by ES and USAID.

In light of the above comments we believe ESI is in compliance with regulations, regarding final and provisional overhead rates.

The schedule of overhead rates shown on page 10 (notes to the Fund Accountability statement) is incorrect. There was an overlap of an old extension and a new extension, where different overhead rates were applicable during a particular period.

Letter to Coopers & Lybrand
Page 2
12 December, 1991

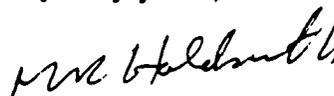
The table of agreed provisional rates should be as follows:

	<u>April 1, '85 to</u> <u>Sep. 30, '88</u> %	<u>Oct. 1, '88 to</u> <u>Sept. 30, '90</u> %	<u>June 1, '90 to</u> <u>March 31, '91</u> %
Home office staff	120	130	135
Field staff (Professional)	105	118	123
Field staff (Non-professional)	25	40	65

With respect to the overclaiming of travel costs and duplicate billing referred to in the compliance section, ES has strengthened its billing procedures in Sri Lanka to prevent recurrence and it is agreed that the overbilling amount of US\$9,691 should be deducted from our final billing due to be submitted by the end of February 1992.

ES acknowledges that procedures for tagging of government property had not been fully implemented. Such tagging has now been fully implemented.

Very truly yours,



M. K. Holdsworth
Controller

MKH/jmb
M916-313

Attachment

c.c. C. Tomasides
C. J. G. Thompson

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