PD-ABF-013

Regional Inspector General for Audit
Nairobi, Kenya

Audit of
USAID/Kenya's Management of Commodities

Report No. 3-615-93-01
November 12, 1992

INSPECTOR GENERAL
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

UNITED STATES OF AMERICA

AGENCY FOR INTERNATIONAL DEVELOPMENT
REGIONAL INSPECTOR GENERAL FOR AUDIT

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November 12, 1992

MEMORANDUM

TO : John R. Westley, Mission Director, USAID/Kenya

FROM : for Everette B. Orr, RIG/A/Nairobi Joseph Farinella

SUBJECT: Audit of USAID/Kenya's Management of Commodities

Enclosed are five copies of our audit report on USAID/Kenya's Management of Commodities, Report No 3-615-93-01.

We have considered your comments on the draft report and included them as an appendix to this report. Based on the actions taken by USAID/Kenya, Recommendations 1.2, 2.2, 2.3, and 2.8 are resolved and Recommendations 1.1, 2.1, 2.4, 2.5, 2.6, 2.7, 3.1, 3.2, and 3.3 are unresolved. In order to resolve Recommendations 2.4, 2.5, 2.6, 2.7 and 3.1 the Mission needs to make a final determination on the amounts involved. Recommendations will be resolved and closed when appropriate actions are completed. Please respond to this report within 30 days indicating any actions planned to implement the recommendations.

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

EXECUTIVE SUMMARY

Background

A.I.D. spends millions of dollars in commodity procurement to support project and non-project activities. As of January 31, 1992 USAID/Kenya's portfolio of active and recently completed projects consisted of $412.5 million and $321.7 million, respectively, in total obligations and expenditures. Of these amounts, USAID/Kenya obligated about $38.6 million and disbursed about $35.3 million for commodities such as computers, photocopiers, contraceptives, laboratory and agricultural equipments, motorcycles and motor vehicles (see pages 1 and 2).

USAID/Kenya procured commodities through technical assistance contractors and by direct A.I.D. procurement both locally and offshore. Procurement was usually made in accordance with the guidance provided in the procurement plans contained in the project papers. Items procured offshore were received through the sea port of Mombasa and Nairobi airport (see page 2).

Audit Objectives

We audited USAID/Kenya's management of commodities in accordance with generally accepted government auditing standards. The audit was carried out because of internal control weaknesses disclosed in an audit of USAID/Kenya Commodity Import Programs (see Scope and Methodology, page 46). Our field work was conducted from January through July 1992 to answer the following audit objectives:

1. Did USAID/Kenya follow A.I.D. policies and procedures in planning for commodity needs (see page 5)?

2. Did USAID/Kenya follow A.I.D. policies and procedures in monitoring the receipt, storage and use of commodities (see page 12)?

3. Did USAID/Kenya follow A.I.D. policies and procedures in monitoring the disposal of commodities at the completion of projects (see page 25)?

Summary of Audit

The following is a summary of the audit findings:

- Except for the effects, if any, on our conclusions from not obtaining certain written confirmations as later discussed in this report, USAID/Kenya followed A.I.D. policies and procedures in planning for commodity needs except that, in 3 of 11 audited projects, $1.3 million in commodity procurement was not coordinated with the availability of facilities, spare parts, supplies, and skills needed to ensure that the commodities were effectively used (see page 5).

- USAID/Kenya did not follow A.I.D. policies and procedures in monitoring the receipt, storage and use of $9.9 million in commodities (see page 12).

- USAID/Kenya did not follow A.I.D. policies and procedures in the disposal of $907,573 in commodities (see page 25).

Audit Findings

Planning for Commodity Needs

Except for the effects, if any, on our conclusions from not obtaining certain written confirmations as later discussed in this report, USAID/Kenya followed A.I.D. policies and procedures in planning for commodity needs except that, in 3 of 11 audited projects, commodity procurement was not coordinated with the availability of facilities, spare parts, supplies, and skills needed to ensure that the commodities were effectively used (see page 5).

Improvements Needed in Planning for Commodity Needs

A.I.D. policy requires realistic advance planning for commodity procurement. In planning for commodity procurement, sound management practices would require USAID offices to consider the conditions necessary to support the amounts and types of commodities procured. However, in 3 of 11 sampled projects, conditions such as facilities, spare parts, supplies and skills were not available to support the amounts and types of commodities procured and received. This occurred because, in planning for commodity procurement for the three projects, USAID/Kenya did not consider the conditions needed to support the commodities procured. As a result of failing to consider the conditions needed to support the amounts and types of commodities received, A.I.D.-financed laboratory equipment valued at $150,760 were still packed in their original containers, some almost two years after they were received, and there was not reasonable assurance that all of them were received in usable condition; contraceptives valued at $12,189 had expired and other contraceptives valued at $145,837 would also likely expire; and there was not reasonable assurance that computers, printers and uninterruptible power supply units valued at $970,521 would be properly maintained because of a lack of spare parts. Furthermore, the lack of facilities would also impact on an additional $161,000 in planned procurement of laboratory equipment (see page 6).

Receipt, Storage and Use of Commodities

USAID/Kenya did not follow A.I.D. policies and procedures in monitoring the receipt, storage and use of commodities (see page 12).

Improvements Needed in Monitoring the Receipt, Storage and Use of Commodities

According to A.I.D. policy, USAID offices are responsible for ensuring that a monitoring system is in place to give reasonable assurance that A.I.D.-financed commodities comply with the Agency's commodity procurement policies. However, USAID/Kenya did not ensure that grantees had adequate systems to monitor the receipt, storage, and use of commodities financed by A.I.D. This happened because USAID/Kenya officials were unclear about their responsibilities regarding the management of A.I.D.-financed commodities and did not give commodity management a high priority. As a result, USAID/Kenya did not have reasonable assurance that A.I.D.-financed commodities valued at approximately $9.9 million, were received, stored and used as intended (see page 12).

Disposal of Commodities

USAID/Kenya did not follow A.I.D. policies and procedures in monitoring the disposal of commodities at the completion of projects. USAID/Kenya did not maintain complete inventory records, as required by A.I.D. policies and procedures, that could be reconciled to what A.I.D. had paid for and received (see page 25).

Improvements Needed in Monitoring Commodity Disposal

A.I.D. policies require USAID offices to maintain a system to monitor the disposal of A.I.D.-financed commodities. However, USAID/Kenya had not established such a system. This occurred because USAID/Kenya project officers were unclear as to their responsibilities regarding the disposal of A.I.D.-financed commodities and did not give commodity management a high priority. As a result, USAID/Kenya did not have reasonable assurance that A.I.D.-financed commodities totaling at least $907,573 for the two terminated projects were disposed of in accordance with A.I.D. policies and procedures. Unless corrected, these weaknesses will also impact on commodities for the other on-going projects, with commodities valued at $9 million (see page 25).

Summary of Recommendations

The report contains three recommendations to correct the problem areas identified. The report recommends that USAID/Kenya establish procedures to ensure that commodity procurement is coordinated with the availability of facilities, spare parts, supplies and skills and suspend planned procurement of (a) $161,000 in laboratory equipment until the construction of laboratories are completed, and (b) intrauterine contraceptive device units until the problem of lack of supplies is addressed and an analysis of projected needs is done. Secondly, the report recommends that USAID/Kenya (a) ensure that contractors and grantees establish and implement a monitoring system for commodities, (b) include the requirement for commodity management in employee evaluation reports, (c) provide training to project officers, (d) obtain from the grantees and contractors commodity listings that reconcile with USAID/Kenya commodity records, (e) reconcile discrepancies between its shipping documents with the Government's receiving records for contraceptives and determine the allowability of $241,301, (f) obtain from the Government an accounting for contraceptives which could not be traced during the audit and determine the allowability of $379,792, and (g) determine the allowability of $53,340 paid for the rehabilitation of road maintenance equipment. Finally, the report recommends that the problems with the receipt, storage, use and disposal of commodities be reported as material weaknesses in the next Federal Managers' Financial Integrity Act reporting cycle to the Assistant Administrator, Bureau for Africa, if these problems are not corrected (see pages 7, 13, and 25).

Management Comments and Our Evaluation

USAID/Kenya reviewed the draft report and generally agreed with the findings. However, USAID/Kenya took exception to recommendations requiring grantees and contractors to submit current commodity listings and reconcile such listings with its accounting records. USAID/Kenya stated that the recommendations impose unnecessary requirements on the grantees and contractors and a burden on the Mission when the time can be more productively spent in monitoring. However, we do not agree that requiring the grantees and contractors to submit to USAID/Kenya commodity listings will involve requirements outside the A.I.D. policies and procedures. Also, we believe the recommended reconciliations will enable the Mission to more effectively monitor the receipt, storage, use and disposal of A.I.D.-financed commodities. USAID/Kenya's comments were considered in preparing the final report. Recommendations 1.2, 2.2, 2.3, and 2.8 are resolved and Recommendations 1.1, 2.1, 2.4, 2.5, 2.6, 2.7, 3.1, 3.2, and 3.3 are unresolved (see page 36 and Appendix II).

The Reports on Internal Controls and Compliance are found on pages 30 and 34, respectively.

Office of the Inspector General

Office of the Inspector General
November 12, 1992

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INTRODUCTION

Background

A.I.D. spends millions of dollars in commodity procurement to support project and non-project activities. As of January 31, 1992, USAID/Kenya's portfolio consisted of 26 active and recently completed bilateral development assistance projects with obligations of $412.5 million and expenditures of $321.7 million. A.I.D. assistance through these projects was targeted to the following sectors:

	Obligations '000	Expenditure '000
Commodity Import Programs	$109,820	$91,591
Agriculture	95,270	88,857
Health	69,468	39,473
Private Sector	58,305	41,024
Structural Adjustment	44,490	44,415
Other	35,156	16,320
Total	$412,509	$321,680

Seventeen of the 26 bilateral projects involved the procurement of commodities for which USAID/Kenya obligated $38.6 million and spent $35.3 million as of January 31, 1992. In addition to the amounts specifically obligated and disbursed for commodities, USAID/Kenya procured commodities under technical assistance contracts and grants. However, we could not determine the value of the commodities that were included in the technical assistance contracts and grants for the 17 projects because USAID/Kenya did not have documentation for these amounts. For example, for two projects in our audit sample -- the Agricultural Management Project No. 615-0221, and Institutional Development for Agricultural Training Project No. 615-0239 -- we could not determine the value of commodities included in their technical assistance components. The commodities procured included mostly computers, photocopiers, contraceptives, laboratory and agricultural equipment, motorcycles and motor vehicles. We audited 11 of the 17 projects with obligations of $12.6 million and expenditures of $9.9 million for commodities for the period between August 25, 1983 and January 31,

1992. Appendix III provides a complete listing of the projects which were audited.

USAID/Kenya procured commodities, through technical assistance contractors and by direct A.I.D. procurement, which included both local and offshore procurement. Commodity needs, specifications, source/origin and contracting modes were selected during project design and summarized in the project papers as the procurement plans which were used as the basis for preparing the project agreements and budgets for commodity procurement.

Procurement was usually made in accordance with the guidance provided in the procurement plan. For example, procurement by technical assistance contractors was approved by the appropriate USAID/Kenya project officers. Items procured offshore were received through the sea port of Mombasa and Nairobi airport. The commodities were cleared through customs and transported to project sites by the contractors, grantees or by clearing agents. Thereafter, it was the responsibility of USAID/Kenya project officers to monitor the receipt, storage, use and disposal of A.I.D.-financed commodities.

Audit Objectives

The Office of the Regional Inspector General for Audit, Nairobi audited USAID/Kenya's management of commodities because of internal control weaknesses disclosed in a recent RIG/A/N audit of USAID/Kenya Commodity Import Programs (A.R. No. 3-615-92-03). The audit was designed to answer the following audit objectives:

1. Did USAID/Kenya follow A.I.D. policies and procedures in planning for commodity needs?

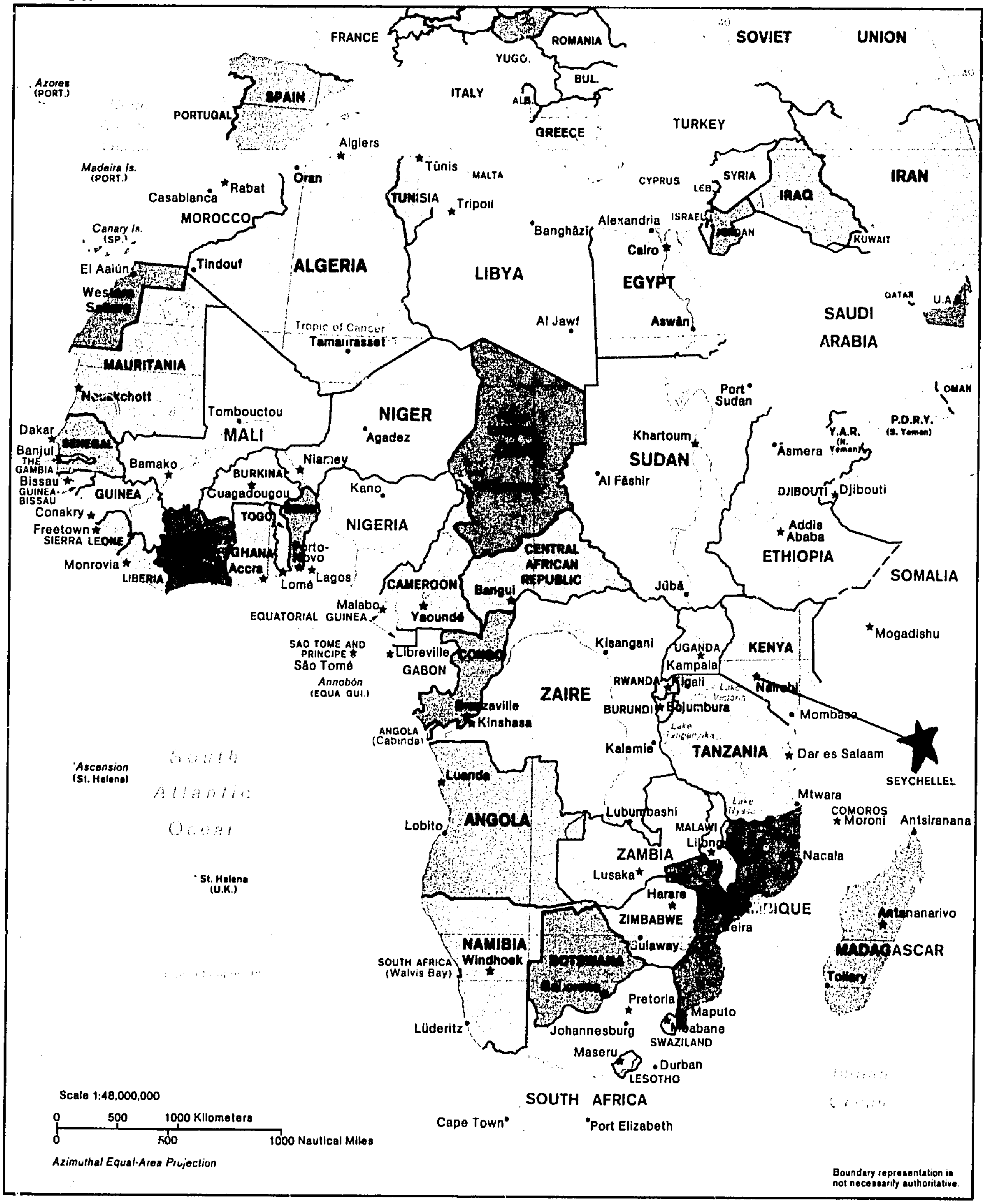
2. Did USAID/Kenya follow A.I.D. policies and procedures in monitoring the receipt, storage and use of commodities?

3. Did USAID/Kenya follow A.I.D. policies and procedures in monitoring the disposal of commodities at the completion of projects?

In answering these audit objectives, we tested whether USAID/Kenya (1) followed applicable internal control procedures contained in A.I.D. Handbooks 1B, 3, 11, 14 and 15 and (2) complied with certain provisions of laws, regulations, grants and contracts. Our tests were sufficient to provide reasonable assurance that our conclusions were correct. Where we found problems, we determined the cause and effect of the problems and developed recommendations.

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

Africa



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REPORT OF AUDIT FINDINGS

As the management official most responsible for the USAID/Kenya commodities program, the Mission Director confirmed in writing -- to the best of his knowledge and belief -- that USAID/Kenya had provided us with information essential for us to answer our audit objectives (see Appendix II). However, the management officials most knowledgeable about the program -- those USAID/Kenya officials who daily manage the commodities program -- would not provide such a written confirmation to either the Mission Director or us. Therefore, our answers to the audit objectives are qualified because the lack of such confirmations from the most knowledgeable management officials is a scope limitation on our audit.

Did USAID/Kenya follow A.I.D. policies and procedures in planning for commodity needs?

Except for the effects, if any, from not obtaining the written confirmations as previously discussed, USAID/Kenya followed A.I.D. policies and procedures in planning for commodity needs except that, in 3 of 11 audited projects, commodity procurement was not coordinated with the availability of facilities, spare parts, supplies, and skills needed to ensure that the commodities were effectively used.

A.I.D. Handbook 11 requires realistic advance planning for commodity procurement. It requires that a list of needed commodities and anticipated costs be prepared as the project is developed. The Handbook intends that approved project designs are to be adhered to unless conditions change to the degree wherein their continued pursuit would not, with factors and risks considered, result in appropriate use of resources or the practicable and effective achievement of agreed-upon objectives.

USAID/Kenya records showed that they reviewed, assessed and identified commodity needs and specifications, and this was documented in the project papers and grant agreements for the 11 projects audited. The project papers, project assistance approval documents, technical assistance contracts and/or grant agreements that were provided by USAID/Kenya contained descriptive listings of commodities which USAID/Kenya considered necessary in planning for the 11 projects. For example, commodities considered necessary for the

Institutional Development For Agricultural Training Project included personal computers, laser printers, uninterruptible power supply units, a telephone system, paper converters and processors. The National Agricultural Research Project included computer equipment, laser printers, irrigation equipment, tractors, plows, grinding mills, refrigerators, photometers, digesters, spectrophotometers, microscopes and calorimeters. The Family Planning Services and Support Project included contraceptives, gloves, computers and vehicles. The Agricultural Management Project included vehicles, photocopiers, typewriters, calculators and television sets.

In most cases, USAID/Kenya records showed that commodity specifications were rather general. For example, the listings in the project papers included provisions for motor vehicle and computer procurement but did not specify the types of motor vehicles and computers to be procured. However, considering the time lag between project planning and implementation, specifications are likely to change and, as implementation progresses, the time of commodities to be procured is better defined. Thus, USAID/Kenya records showed that lack of exact commodity specifications at the initial planning stages appears to have had no adverse effect on the purchases eventually made and was in line with A.I.D. Handbook 3 guidance.

However, in 3 of 11 sampled projects, USAID/Kenya did not consider the conditions needed to support the amounts and types of commodities received as discussed below.

Improvements Needed in Planning for Commodity Needs

A.I.D. policy requires realistic advance planning for commodity procurement. In planning for commodity procurement, sound management practices would require USAID offices to consider the conditions necessary to support the amounts and types of commodities procured. However, in 3 of 11 sampled projects, facilities, spare parts, supplies and skills were not available to support the amounts and types of commodities procured and received. This occurred because, in planning for commodity procurement for the three projects, USAID/Kenya did not consider the conditions needed to support the commodities procured. As a result of failing to consider the conditions needed to support the amounts and types of commodities received, A.I.D.-financed laboratory equipment valued at $150,760 were still packed in their original containers, some almost two years after they were received, and there was no reasonable assurance that all of them were received in usable condition. Also, contraceptives valued at $12,189 had expired and other contraceptives valued at $145,837 would also likely expire, and there was no reasonable assurance that computers, printers and uninterruptible power supply units valued at $970,521 would be properly maintained because of a lack of spare parts. Furthermore, the lack of facilities would also impact on an additional $161,000 in planned procurement of laboratory equipment.

<u>Recommendation No. 1:</u> We recommend that USAID/Kenya:

1.1 establish procedures to ensure that planning for commodity procurement includes an assessment of the availability of facilities, spare parts, supplies and skills including the necessary coordination with other donors, grantees and the Government of Kenya; and

1.2 suspend the procurement of (1) $161,000 in additional laboratory equipment under Phase II of Project Number 615-0229 until the construction of laboratories is completed, and (2) intrauterine contraceptive device units until (i) the problem of lack of supplies is addressed, and (ii) an analysis is done of the quantities available within the depot and the district stores versus the projected needs based on the past usage rates.

A.I.D. Handbook 11, Chapter 3, requires realistic advance planning for commodity procurement. A list of needed commodities and anticipated costs is to be prepared as the project is developed. A.I.D. Handbook 3, Chapter 13, states that A.I.D. policy supports the adjustments of project designs and implementation methods to maintain their relevance and effectiveness under changing conditions. Such flexibility is a critical tool for sound project management. This is not to imply that originally agreed upon project elements and objectives are to be taken lightly or altered without justification and prior approval. This policy intends that approved project designs are to be adhered to unless conditions change to the degree wherein their continued pursuit would not, with factors and risks considered, result in appropriate use of resources or the practicable and effective achievement of agreed-upon objectives. When problems are suspected or confirmed, the borrower/grantee or A.I.D. project committee members should evaluate the condition and, as appropriate, recommend alternative approaches and mechanisms, prepare justifications for the changes and obtain prompt approval to incorporate such changes into the project.

In planning for commodity procurement, sound management practices would require USAID offices to consider the conditions necessary to support the amounts and types of commodities procured. For the purposes of this audit, we defined such conditions to include the following:

- facilities for the operation of the equipment,

- spare parts for the maintenance of the equipment,

- supplies that are needed to use the commodities, and

- skills needed to operate the equipment.[1]

USAID/Kenya records showed that they reviewed, assessed and identified commodity needs and specifications, and this was documented in the project papers and grant agreements for the 11 projects audited. However, in 3 of 11 projects, conditions such as facilities, spare parts, supplies and skills were not available to support the amounts and types of commodities procured and received. This is demonstrated by the following examples.

- **National Agricultural Research Project No. 615-0229:** Under this project, laboratory equipment costing $240,800 was procured for research stations at Mtwapa, Kakamega, Katumani, Kitale and Embu. These commodities were received in the five research stations between March 1990 and October 1991. Good planning for commodity procurement would have required USAID/Kenya to consider the completion dates of the laboratories before the equipment was procured and received. However, except for the Kitale research station, equipment was procured and received before laboratories were completed. The construction of the laboratories started in April 1991 for three stations and April 1992 for the other station and was not expected to be completed until after September 1992. Consequently, laboratory equipment valued at about $150,760 was still in storage rooms in the original containers and had not been tested to determine whether it was received in usable condition. We were told by the contractor that if this equipment or some of it is found not usable, there will be no recourse since the equipment was supposed to be tested immediately upon arrival and claims lodged with the manufacturers. Also, any supplier warranties will have expired by the time laboratory facilities are completed and the equipment put to use. In addition, documents within USAID/Kenya and the contractor's office showed $161,000 in planned procurement of additional laboratory equipment.

- **Institutional Development for Agricultural Training Project No. 615-0239:** Under this project, 51 Kaypro computers, 34 IBM printers and 35 uninterruptible power supply units (UPSes) were procured at a cost of $183,364 for Egerton University. Good planning for commodity procurement would have required USAID/Kenya to consider the availability of spare parts and skills before computers, printers and UPSes were procured and received. However, there was no evidence that USAID/Kenya planned for spare parts and skills before computers, printers and UPSes were procured and received. We were told by the officials at Egerton

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[1] This definition is based on our interpretation of A.I.D. Handbook 13 Chapter 1 on "Project Modifications". We believe it is a reasonable criteria that ensures effective use of A.I.D.-financed commodities.

University that spare parts for this equipment were not locally available which made it very difficult to maintain them. In addition, those officials stated that staff were not knowledgeable about computers.

Also, under the Institutional Development For Agricultural Training Project, a telephone system was installed at a cost of $787,157 at Egerton University. However, there was no evidence that the availability of spare parts was considered before the system was procured and installed. We were told by the University officials that spare parts to maintain the system were not locally available. In fact, a number of receivers were not being used because they had broken down and spare parts were not locally available. Also, the printer head, for which we could not determine the value, had broken down and could not be repaired. In addition, a paper converter camera could not be used because the required spare parts were not available and an automatic processor was not needed. We could not determine the values of the camera and processor. Furthermore, Egerton University did not have technicians with the necessary skills to repair the telephone system.

- **Family Planning Services and Support Project No. 615-0232:** Under this project, 305,000 Intrauterine Contraceptive Device units (IUCDs) valued at $326,412 were procured between September 1989 and February 1992. Sound procurement planning would have required USAID/Kenya to consider the availability of supplies such as gloves and disinfectants before the IUCDs were procured and received. However, the procurement of the IUCDs was not coordinated with the availability of the supplies. The audit found that at least 11,390 IUCDs valued at $12,189 had expired and another 125,771 IUCDs valued at $145,837 would expire in the next two years if the problem of lack of supplies was not solved.

The above problems occurred because, in planning for commodity procurement for three projects, USAID/Kenya did not consider the conditions needed to support the amounts and types of commodities procured as demonstrated below.

- Regarding the National Agricultural Research Project, USAID/Kenya was funding the procurement of the laboratory equipment and the World Bank was funding the construction of the laboratory buildings. There was no coordination between USAID/Kenya and the World Bank to ensure that laboratory equipment valued at $240,800 coincided with the construction of the laboratory buildings. The result was that USAID/Kenya financed laboratory equipment valued at $150,760 started arriving almost two years before the laboratory buildings were expected to be completed.

- Regarding the Family Planning Services And Support Project, USAID/Kenya was to supply the contraceptives including the IUCDs and the Government of Kenya (Government) was to provide supplies such as gloves and disinfectants. However, USAID/Kenya procured the IUCDs and did not ensure that the Government provided the required supplies. The result was that A.I.D.-financed IUCDs valued at $158,026 had either expired or would expire in the next two years because they could not be used without the supplies.

- Under the Institutional Development for Agricultural Training Project, the availability of spare parts and skills was not considered when planning for commodity procurement. If the availability of spare parts locally was considered, the 51 Kaypro computers, 34 IBM printers and 35 UPSes would not have been procured. Other types of computers, printers and UPSes for which spare parts and maintenance would have been readily available locally would have been procured instead. Also, another type of telephone system would have been installed instead of the current system.

As a result of the foregoing, A.I.D.-financed laboratory equipment valued at $150,760 were procured and received under the National Agricultural Research Project about two years before the laboratory buildings were due to be completed. This equipment has not been tested and should they be found later to be unusable, there will be no recourse against the suppliers since the equipment was supposed to be tested immediately upon arrival. Furthermore, the lack of facilities would also impact on an additional $161,000 in planned procurement of laboratory equipment under this project.

In addition, 305,000 IUCDs valued at $326,412 were procured between September 1989 and February 1992. At least 11,390 IUCDs valued at $12,189 expired and USAID/Kenya did not have reasonable assurance that another 125,771 IUCDs valued at $145,837 would not expire if the problem of lack of supplies was not solved.

Under the Institutional Development For Agricultural Training Project, 51 Kaypro computers, 34 IBM printers and 35 UPSes valued at $183,364 were procured for Egerton University. However, five Kaypro computers and ten printers valued at $22,820 could not be repaired because the spare parts were not available. USAID/Kenya did not have reasonable assurance that spare parts would be available to repair the other 46 Kaypro computers and 24 printers valued at $136,574 if they broke down. Also, the 35 UPSes procured for Egerton University at a cost of $29,630 could not be used because batteries were not locally available. Furthermore, there was no reasonable assurance that Egerton University would be able to maintain the telephone system that was installed at a cost of $787,157 due to the unavailability of spare parts locally.

Based on the above, we concluded that USAID/Kenya needed to establish procedures to ensure that planning for commodity procurement includes an assessment of the availability of facilities, spare parts, supplies and skills. Because facilities, supplies, and training might be funded by other donors, grantees and the Government, the procurement of commodities by A.I.D. should be coordinated with such donors, grantees and the Government. In addition, USAID/Kenya needed to suspend planned procurement of $161,000 in additional laboratory equipment under Phase II of Project Number 615-0229 until the construction of the laboratories is completed. Furthermore, USAID/Kenya needed to suspend the procurement of IUCDs until the problem with lack of supplies is addressed and an analysis is done of the quantities of IUCDs available versus projected usage under Project Number 615-0232.

Did USAID/Kenya follow A.I.D. policies and procedures in monitoring the receipt, storage and use of commodities?

USAID/Kenya did not follow A.I.D. policies and procedures in monitoring the receipt, storage and use of commodities.

Regarding the receipt of commodities, USAID/Kenya did not ensure that grantees, contractors or the Government of Kenya ("the Government") compared quantities ordered against what was actually paid for, shipped and received in country. For storage of commodities, project officers did not ensure that physical inventories were made by the grantees, contractors or the Government, the results of the physical inventories were submitted to USAID/Kenya and reconciled to what A.I.D. had paid for. Regarding use of the commodities, USAID/Kenya did not have a system to ensure that A.I.D.-financed commodities were used for intended purposes by the grantees, contractors and the Government.

USAID/Kenya was responsive to the auditors' request to provide commodity listings for the projects audited. However, those listings were incomplete and did not include the required information such as identifying serial numbers, dates of arrival, locations and unit costs. Moreover, neither USAID/Kenya nor the auditors could determine the extent of the information missing from these inventory lists since prior inventories had either not been provided or had not been done by the contractors and grantees. Problems with USAID/Kenya's management of commodities are discussed below.

Improvements Needed in Monitoring the Receipt, Storage and Use of Commodities

According to A.I.D. policy, USAID offices are responsible for ensuring that a monitoring system is in place to give reasonable assurance that A.I.D.-financed commodities comply with the Agency's commodity procurement policies. However, USAID/Kenya did not ensure that grantees had established systems to monitor the receipt, storage, and use of commodities financed by A.I.D. This happened because USAID/Kenya officials were unclear about their responsibilities regarding the management of A.I.D.-financed commodities and did not give commodity management a high priority. As a result, USAID/Kenya did not have reasonable assurance that A.I.D.-financed commodities valued at approximately $9.9 million, were received, stored and used as intended.

Recommendation No. 2: We recommend that USAID/Kenya:

2.1 Establish and implement a monitoring system, which includes evaluating borrower/grantee systems for the receipt, storage and use of A.I.D.-financed commodities and reconciling USAID/Kenya records with those of the borrower/grantee on a periodic basis for all on-going and future projects.

2.2 Include the requirement for commodity management in the project officers' employee evaluation reports as appropriate.

2.3 Provide commodity management training for project officers.

2.4 Obtain from the grantees and contractors current commodity listings for Project Numbers 615-0238, 615-0245, 615-0251, 615-0221, 615-0229, 615-0232, 615-240.01, 615-0240.02 and 615-0253, reconcile those listings with USAID/Kenya commodity records and determine the allowability of the quantities and amounts that cannot be reconciled.

2.5 Reconcile discrepancies in USAID/Kenya shipping documents with the receiving records at the Government of Kenya's Medical Supplies Coordinating Unit for 3,180,000 condoms valued at $150,309, 5,400 IUCDs valued at $8,559 and 825,800 foaming tablets valued at $82,433, and determine the allowability of quantities and amounts that cannot be reconciled.

2.6 Obtain from the Government of Kenya's Medical Supplies Coordinating Unit an accounting for contraceptive issues of 6,028,000 condoms valued at $284,944, 47,600 intrauterine contraceptive device units valued at $50,942 and 459,600 foaming tablets valued at $43,906 which could not be traced during the audit, and determine the allowability of the quantities and amounts that cannot be reconciled.

2.7 Determine the allowability of, and collect as appropriate, $53,340 paid for the rehabilitation of road maintenance equipment at Tsavo East and Mount Elgon National Parks.

2.8 Report in the next Federal Managers' Financial Integrity Act reporting cycle to the Assistant Administrator, Bureau for Africa, the internal control weaknesses associated with USAID/Kenya's commodity monitoring systems, if these weaknesses are not corrected.

A.I.D. Handbook 15, Chapter 10, states that A.I.D. offices are responsible for ensuring that A.I.D. financed commodities are properly accounted for regarding receipt, storage and use. For A.I.D. assistance to be used effectively, commodities financed by A.I.D. must reach the ultimate user on time, in a usable condition and must be used for the purpose intended within a prescribed time period. The USAID is responsible for the review of project progress reports to verify that A.I.D.-financed commodities are being effectively used in the project. Specifically, the guidance requires USAIDs to:

- monitor the borrower/grantees' systems by reviewing progress reports on the use of commodities;

- require submission by the borrower/grantee of periodic reports which identify the utilization, cost/value of goods shipped and/or any claims made;

- require periodic reports of commodities held in customs and borrower/grantees' warehouses;

- perform periodic port checks to ensure that cargo that goes astray is located and that cargo is safely and expeditiously cleared through the customs; and

- perform periodic end-use checks to evaluate the continued effectiveness of the borrower/grantees' systems and for taking meaningful corrective action.

A.I.D. Handbook 1B, Chapter 24, states that USAID offices are responsible for ensuring that the borrower/grantee's commodity management systems are operating effectively. USAIDs are required to maintain a current description of those systems, and its evaluation of them, as well as the monitoring procedures established by the USAID office. The Handbook further states that project officers have ultimate responsibility for ensuring that A.I.D. funded commodities are effectively used for project purposes. It requires the project officers to continuously monitor their projects and give periodic end-use reports to the Mission Director.

In addition, the Federal Managers' Financial Integrity Act requires Agency's internal controls to provide reasonable assurance that funds, property and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation.

At the time of audit in January 1992, USAID/Kenya's accounting records and documents within the contractors and grantees' offices showed that at least $9.9 million had been disbursed for procurement of project commodities for 11 projects. Commodities purchased for projects included computers, vehicles, farm machinery, contraceptives and laboratory equipment. However, USAID/Kenya did not ensure that the contractors and grantees had established systems that determined the exact amount and condition of project commodities that were received, stored and put into use.

During the audit, we intended to select a sample of commodities from each project we reviewed and trace these to ensure that they were received, stored and used as intended. Since USAID/Kenya did not ensure that the contractors and grantees established systems to monitor the receipt, storage and use of the commodities, we were unable to do this. Specifically, USAID/Kenya did not receive from the contractors and grantees information needed to monitor the receipt, storage and use of A.I.D.-financed commodities. For the purposes of this audit, we defined information needed in monitoring commodities to include:

- receiving and inspection reports,

- commodity listings indicating types of commodities, locations of commodities, dates of acquisition, amounts paid and condition of the commodities, and

- progress reports on the use of commodities.[2]

Regarding the monitoring of the receipt of commodities, USAID/Kenya relied on contractors' and grantees' systems. However, there was no evidence that USAID/Kenya evaluated those systems to determine whether they were adequate to ensure that quantities ordered agreed with what was actually paid for, shipped and received in country. Thus USAID/Kenya was relying on systems whose effectiveness was not known. In addition, USAID/Kenya did not ensure that the contractors and grantees submitted receiving and inspection reports to be used in monitoring the receipt of the commodities. USAID/Kenya's involvement upon arrival of commodities in country was limited to helping the grantees and contractors obtain duty exemption letters. As long as recipients did not complain, USAID/Kenya assumed that there was no problem with the receipt of the commodities.

Furthermore, USAID/Kenya did not ensure that the grantees and contractors inspected the commodities upon receipt to ascertain that they were received in the quantities and condition ordered. Also, USAID/Kenya project officers were not aware of how contractors and grantees resolved discrepancies in the amounts ordered and the amounts received. The

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[2] This definition is based on our interpretation of the commodity monitoring responsibilities of A.I.D. offices as outlined in A.I.D. Handbooks 15, Chapter 10 and 1B Chapter 24. While this definition is not authoritative, we believe it is a reasonable criterion that ensures effective monitoring of the receipt, storage and use of A.I.D.-financed commodities.

following examples in 4 of 11 projects audited demonstrate the problems relating to the receipt of A.I.D.-financed commodities.

- **Family Planning Services and Support Project No. 615-0232:** USAID/Kenya was relying on the Government's inventory control system to account for the receipt of the contraceptives. However, during our visit to the Government's Medical Supplies Coordinating Unit (MSCU) on May 29, 1992, we found numerous discrepancies between the amount of contraceptives shown as received by the MSCU records and contraceptives received per the shipping documents within USAID/Kenya. Between June 1989 and May 1992, shipping documents within USAID/Kenya indicated that 65,904,000 condoms valued at $3,115,077 had been received. The MSCU receiving records showed receipts of 62,724,000 condoms valued at $2,964,768 during this period. Furthermore, the shipping documents within USAID/Kenya showed receipts of 26,688,000 condoms valued at $1,261,459 which were not recorded by MSCU. On the other hand, MSCU receiving records for the same condom shipments showed receipts of 23,508,000 condoms valued at $1,111,150 which could not be traced to the shipping documents within USAID/Kenya. Thus, the shipping documents within USAID/Kenya showed that 3,180,000 more condoms valued at about $150,309 were received than indicated by MSCU receiving records. In addition, between September 1989 and May 1992, shipping documents within USAID/Kenya showed that 305,000 IUCDs valued at $326,412 were received. However, the receiving records at the MSCU showed 310,400 IUCDs valued at $334,971 had been received during the same period. Furthermore, the shipping documents within USAID/Kenya showed receipts of 87,400 IUCDs valued at $90,756 which were not recorded by MSCU. On the other hand, the MSCU receiving records showed receipts of 92,800 IUCDs valued at $99,315 which could not be traced to the shipping records within USAID/Kenya. Thus, MSCU records showed that 5,400 more IUCDs valued at $8,559 were received than indicated by shipping documents within USAID/Kenya.

  Finally, between January 1990 and August 1991, receiving records within USAID/Kenya showed 4,742,400 foaming tablets (VFTs) valued at $473,399 were received. However, MSCU receiving records showed that 3,916,600 VFTs valued at about $390,965 were received. Furthermore, the shipping documents within USAID/Kenya included receipts of 3,297,600 VFTs valued at $329,175 which were not recorded by MSCU. On the other hand, the MSCU records included receipts of 2,471,800 VFTs valued at $246,742 which could not be traced to the shipping documents within USAID/Kenya. Thus, the shipping documents within USAID/Kenya showed that 825,800 more VFTs valued at $82,433 were received than indicated by MSCU receiving records.

- **Private Enterprise Development Project No. 615-0238:** The accounting records showed that $149,434 had been disbursed for commodities under the Kenya National Chamber of Commerce and Industry, $20,369 under the Investment Promotion Center, $8,769 under the Kenya Association of Manufacturers and $5,147 under the Advisors components of this project. However, at the time of audit, the project officer did not have inventories of the items procured under these components. Therefore, there was no way of relating what was procured to what was actually received and on hand.

  Also under the same project, a listing with commodities valued at $61,014 was submitted by the contractor for the International Executive Service Corps component. However, during our physical inspection, the contractor officials told us that the list included items funded by other donors and could not distinguish which items were funded by A.I.D.

- **Structural Adjustment Assistance Program No. 615-0240:** The accounting records at USAID/Kenya indicated that $121,454 had been disbursed for commodities under the Resource Management for Rural Development component of this project. However, a list of commodities given to us by the contractor did not have the cost of the individual items and as such we could not relate it to the $121,454 shown by the USAID/Kenya accounting records.

- **Park Rehabilitation and Management Project No. 615-0253:** USAID/Kenya was relying on the Government's inventory control system to account for the receipt of the commodities. However, the audit determined that the Government's system could not be relied upon to control the receipt of the commodities under this project. For example, according to the records of the Government's Kenya Wildlife Services (KWS), a Komatsu motor grader at Tsavo East National Park was rehabilitated at a cost of KSh.1,141,875 ($41,919).[3] However, the official in charge of Tsavo East National Park stated on May 11, 1992 during our site visits that the Komatsu had never been grounded and he was not aware of any rehabilitation that was done to it. This official stated that a USAID/Kenya funded contractor -- Pan African Equipment -- had painted the Komatsu and fitted a rear wheel drum whose cost could not have been anywhere near the KSh.1,141,875 ($41,919) paid by USAID/Kenya.

  In addition, the records at Kenya Wildlife Services indicated that a Komatsu motor

[3] The average exchange rate from January 1991 to December 1991 of Kenya Shillings (KSh.) 27.24 = 1 U.S. dollar is used throughout the report.

grader at Mount Elgon National Park was repaired by Pan African Equipment at a cost of KSh.311,108 ($11,421). However, the park officials stated on May 26,1992 during our site visit that the Komatsu was never grounded and could not understand how such an amount could have been spent on their motor grader. Thus, the validity of the KSh.311,108 ($11,421) in repair cost for that equipment was questionable.

Regarding the storage of commodities, USAID/Kenya did not ensure that (1) physical inventories of A.I.D.-financed commodities were made by the contractors, grantees, or the Government, (2) results of physical inventories were submitted to USAID/Kenya on a periodic basis, and (3) reconciliations of physical inventories and the book amounts were performed. In addition, USAID/Kenya did not ensure that contractors, grantees and the Government established systems to track and thus identify the location of commodities. The following examples in 8 of 11 projects demonstrate the problems relating to the storage of A.I.D.-financed commodities.

- **National Agricultural Research Project No. 615-0229:** According to the contractor's records -- Mid America International Agricultural Consortium -- laboratory and farm equipment valued at $63,670 were supplied to research stations at Mtwapa, Kakamega, Kitale and Embu. However, the officials at those locations stated during the audit site visits that they had not received that equipment at their stations. In addition, there was an unreconciled difference of $859,327 million between the contractor's list of commodities and USAID/Kenya's accounting records. USAID/Kenya accounting records indicated that commodities valued at $2.2 million had been procured while the contractor's listing of commodities on hand was valued at $1.3 million.

- **Structural Adjustment Assistance Program No. 615-0240:** According to USAID/Kenya's accounting records, $535,946 had been expended for commodities under the Resource Management for Rural Development component of this project. However, the list submitted by the contractor contained commodities valued at $100,080. Thus, there was an unreconciled difference of $435,866 between USAID/Kenya's accounting records and the contractor's commodity listing.

- **Family Planning Services and Support Project No. 615-0232:** USAID/Kenya was relying on the Government's system for distributing contraceptives from the MSCU to the sub-depots and the districts. However, during our site visits between May 11, 1992 and June 10, 1992, we found that various quantities of contraceptives shown as issued by MSCU to the sub-depots and districts did not appear in their receiving records. For example, 6,028,000 condoms valued at $284,944, 47,600 IUCDs valued at $50,942 and 459,600 VFTs valued at $43,906 shown by MSCU records as issued to two sub-depots and 18 districts were not on hand in the respective sub-depots and districts.

- **Kenya Contraceptives Social Marketing Project No. 615-0251:** USAID/Kenya's accounting records indicated that $83,655 had been disbursed for commodities under this project. However, the contractor's listing included commodities valued at KSh.1,604,482 ($58,902). Thus, there was an unreconciled difference of $24,753. In addition, the contractor's listing included a calculator and a fax machine valued at KSh.45,650 (about $1,676) which did not exist.

- **Park Rehabilitation and Management Project No. 615-0253:**: The cost of $291,785 worth of rehabilitating equipment indicated by USAID/Kenya accounting records had not been reconciled to the amount of $485,163 shown in the contractor's records.

- **Agricultural Management Project No. 615-0221:** USAID/Kenya's accounting records showed that $98,296 had been disbursed for commodities under this project while the listing given by the contractor indicated that $125,863 had been spent on commodities. Thus, there was an unreconciled difference of $27,567.

- **Kenya Health Care Financing Project No. 615-0245:** USAID/Kenya's accounting records showed that $82,386 had been disbursed for commodities under this project while the listing given by the contractor showed that $103,771 had been spent on commodities. Thus, there was an unreconciled difference of $21,385.

- **Private Enterprise Development Project No. 615-0238:** USAID/Kenya's accounting records showed that $59,040 was disbursed for commodities for the Kenya Management Assistance Program component of this project. However, the listing of commodities provided to us by USAID/Kenya included commodities valued at KSh.524,802 ($19,266). Thus, there was an unreconciled difference of $39,774. In addition, during our physical inspection, we observed items financed by A.I.D. such as furniture, a franking machine and a motor vehicle which were not included on the commodity listings.

Regarding the use of the commodities, USAID/Kenya did not ensure that contractors and grantees effectively used A.I.D.-financed commodities for their intended purposes. For example, USAID/Kenya did not require contractors, grantees and the Government to submit progress reports on the use of commodities. Also, USAID/Kenya did not perform end-use checks on a regular basis to ensure that the commodities were being used as intended. The following examples in 4 of 11 projects demonstrate the problems relating to the use of the commodities.

- **National Agricultural Research Project No. 615-0229:** As discussed under Audit Objective No. 1, laboratory equipment valued at $150,760 was not being used because the laboratories had not been constructed. In addition, laboratory equipment valued at $22,420 could not be used at Kitale station because they were received with missing parts, wrong components or were inappropriate.

- **Park Rehabilitation and Management Project No. 615-0253:** A Komatsu motor grader at Tsavo West National Park was rehabilitated at a cost of KSh.1,564,780 ($57,444) in September 1991. However, it was not being used because of lack of a lowloader.

- **Institutional Development for Agricultural Training Project No. 615-0239:** As discussed under Audit Objective No. 1, five Kaypro computers valued at $12,030, 10 IBM printers valued at $10,790, 35 UPSes valued at $29,630, a paper converter camera, an automatic processor, and five telephone receivers, whose values we could not determine, could not be used because the spare parts were not available.

- **Family Planning Services and Support Project No. 615-0232:** As discussed under Audit Objective No. 1, 11,390 IUCDs valued at $12,189 expired because of lack of gloves and disinfectants and thus were not used for their intended purposes.

The following pictures further demonstrate the problems of usage of A.I.D.-financed commodities.

Figure 1: Laboratory Equipment at Embu research station which were not being used because the laboratories had not been constructed.

Figure 2: IUCDs at the Kisumu sub-depot which expired because the Government did not supply lotions and gloves.

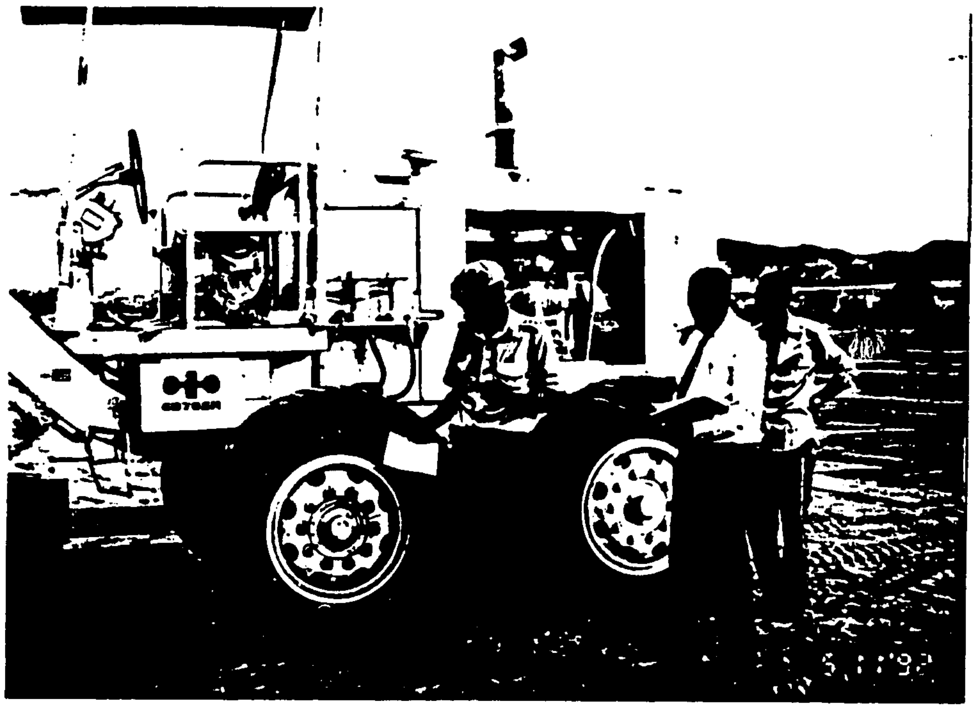

Figure 3: A Komatsu motor grader at Tsavo East National Park. About $41,919 was paid for repairing this grader but the park officials stated that no repairs were made.

Figure 4: Uninterruptible power supply units at Egerton University valued at $29,630 could not be used because batteries were not available locally.

The problems with commodities occurred because of five factors. First, USAID/Kenya project officers, though aware of requirements in the A.I.D. Handbooks, did not have specific knowledge of their duties and responsibilities regarding project commodities. The project officers were unclear as to who was responsible for maintaining complete listings and monitoring commodities ordered, received, stored, used, and disposed. For example, some project officers believed that their monitoring responsibilities did not extend to commodities procured under host country contracts. However, A.I.D. regulations are clear that project funded commodities should be monitored. The project officers also stated that they had not been asked by the management to monitor commodities. We were told that the responsibility for commodity management as described in A.I.D. Handbooks was not included in the project officers' employee evaluation reports (EERs).

Second, USAID/Kenya gave other areas priority and did not consider commodity management to be a high priority. The project officers stated that most of their time was taken up with preparing Project Implementation Letters, Project Implementation Orders and other related project management paperwork. Therefore, they stated that they did not have the time to make site visits, prepare trip reports, test inventory records and perform end-use reviews.

Third, USAID/Kenya relied on the borrower/grantees' systems to track the receipt, storage and use of A.I.D.-financed commodities without evaluating and documenting their commodity management systems, as required in A.I.D. Handbook 1B, Chapter 24. However, without evaluating and documenting those systems, we concluded that USAID/Kenya was relying on systems whose effectiveness was not known.

Fourth, most of the project officers had not received training in commodity management.

Fifth, USAID/Kenya did not report weaknesses relating to the receipt, storage and use of A.I.D.-financed commodities in its last Federal Managers' Financial Integrity Act reporting cycle. Thus, the weaknesses identified above continued to exist.

--- *USAID/Kenya did not have reasonable assurance that A.I.D.-financed commodities, totaling at least $9.9 million, were received, stored and used as intended.*

As a result of the foregoing, USAID/Kenya did not have reasonable assurance that A.I.D.-financed commodities, totaling at least $9.9 million, were received, stored and used as intended. In cases where documentation did exist, the audit determined problems in several projects. For example, USAID/Kenya commodity records did not reconcile with commodity lists submitted by the grantees and contractors. In addition, commodities worth $63,671 under the National Agricultural Research Project, and $379,792 under the Family Planning Services And Support Project, could not be located. Also, USAID/Kenya needed to determine the allowability of, and collect as appropriate, $53,340 paid for the rehabilitation of road maintenance equipment at Tsavo East and Mount Elgon National Parks. Furthermore, $295,263 worth of commodities were not being used under the National Agricultural Research Project, Park Rehabilitation Project, Family Planning Services and Support, and Institutional Development For Agricultural Training Project.

Based on the foregoing, we concluded that USAID/Kenya needed to establish and implement a system to monitor the receipt, storage and use of A.I.D.-financed commodities, include the requirement for commodity management in employee evaluation reports, and provide commodity management training for project officers. Also, USAID/Kenya needed to obtain from the grantees and contractors commodity listings that reconcile with USAID/Kenya's commodity records for project numbers 615-0238, 615-0245, 615-0251, 615-0221, 615-0229, 615-0232, 615-240.01, 615-0240.02 and 615-0253. In addition, USAID/Kenya needed to reconcile the quantities of contraceptives contained in the shipping documents with the receiving records at the MSCU. Furthermore, the problems with the receipt, storage and use of commodities should be reported in the next Federal Managers' Financial Integrity Act reporting cycle as material weaknesses if they remain uncorrected.

Did USAID/Kenya follow A.I.D. policies and procedures in monitoring the disposal of commodities at the completion of projects?

USAID/Kenya did not follow A.I.D. policies and procedures in monitoring the disposal of commodities at the completion of projects. USAID/Kenya did not maintain complete records, as required by A.I.D. policies and procedures, that could be reconciled to what A.I.D. had paid for and received.

As discussed under Audit Objective Two, USAID/Kenya did not maintain complete records of commodities ordered, received, stored and used. Without complete records, we could not determine if the A.I.D.-financed commodities in our sample were disposed of in accordance with A.I.D. policies and procedures at the completion of the projects.

However, using other information such as the Mission Accounting and Control System (MACS) reports, purchase orders and contractors' financial reports available at USAID/Kenya and the contractor and grantees' offices, we determined that USAID/Kenya did not obtain complete commodity listings to be used for disposal purposes. For example, the commodity listings provided to USAID/Kenya were incomplete and did not include the required information. Furthermore, USAID/Kenya did not reconcile commodities disposed of in the two terminated projects to what had been paid for and received. Problems with commodity disposal are discussed in more detail below.

Improvements Needed in Monitoring Commodity Disposal

A.I.D. policies require USAID offices to maintain a system to monitor the disposal of A.I.D.-financed commodities. However, USAID/Kenya had not established such a system. This occurred because USAID/Kenya project officers were unclear as to their responsibilities regarding the disposal of A.I.D.- financed commodities and did not give commodity management a high priority. As a result, USAID/Kenya did not have reasonable assurance that A.I.D.-financed commodities totaling at least $907,573 for the two terminated projects were disposed of in accordance with A.I.D. policies and procedures. Unless corrected, these weaknesses will also impact on commodities for the other on-going projects with commodities valued at $9 million.

Recommendation No. 3: We recommend that USAID/Kenya:

3.1 Obtain from the contractors and grantees a complete and accurate accounting for the commodities disposed under project numbers 615-0220 and 615-0241,

reconcile the inventories to the disbursements made by USAID/Kenya and account for any discrepancies and make recoveries for any improperly disposed commodities.

3.2 **Establish and implement a system for monitoring commodity disposal to include the requirement that contractors and grantees take and submit to USAID/Kenya annual inventories of commodities procured under each project, reconcile inventories to the disbursements, account for any differences and take appropriate action for the discrepancies.**

3.3 **Report in the next Federal Managers' Financial Integrity Act reporting cycle to the Assistant Administrator, Bureau for Africa, the internal control weaknesses associated with USAID/Kenya's commodity disposal monitoring system, if these weaknesses are not corrected.**

A.I.D. Handbook 1B, Chapter 24, states that USAID offices are responsible for ensuring that the borrower/grantee's commodity management systems are operating effectively. Handbook 15, Chapter 10, requires USAIDs to monitor the disposition of A.I.D.-financed commodities. According to the Handbook, each USAID office is responsible for maintaining a current description, approved by the controller, of the borrower/grantee's commodity disposition system(s) and the monitoring procedures established by the USAID. Furthermore, Chapter 11 of the Handbook requires commodity disposal arrangements to follow adequate audit trace principles.

In managing commodity disposal by recipients, good management practice dictates that USAID offices monitor recipients to ensure that they comply with applicable agreements, laws and regulations. This includes ensuring that recipients comply with Federal Acquisition Regulation 45.508 and A.I.D. Handbook 14 requirement for periodic inventories and finalization of inventory reports for commodities at the completion of contracts and grants.

A.I.D. Handbook 14, which is based on Federal Acquisition Regulations Part 45.508, requires USAID offices to obtain listings to be used for commodity disposal purposes which, at a minimum, should identify discrepancies disclosed by physical inventories and signed certifications. The Handbook further requires USAIDs to approve a program prepared by the borrower/grantee for the receipt, use, maintenance, protection, custody and care of A.I.D.-financed commodities. The Handbook requires borrower/grantees to submit an annual report on non-expendable property in a form and manner acceptable to A.I.D. An acceptable report includes: descriptions of the property, acquisitions (purchases and transfers from various sources), disposals (returns to A.I.D., transfers to various parties and other disposal), and value of the property as of the closing date.

In addition, the Federal Managers' Financial Integrity Act (the Integrity Act) requires Agencies' internal controls to provide reasonable assurance that funds, property and other assets are safeguarded against waste, loss, unauthorized use or misappropriation. The implementation of the Integrity Act requires USAID offices to report any internal control weaknesses to the Assistant Administrator as an annual certification.

For the projects audited, USAID/Kenya did not establish a system to ensure that the borrower/grantee systems were operating effectively. As discussed under Audit Objective Two, USAID/Kenya did not maintain complete inventory records of commodities ordered, received and used. Thus, it was not possible to identify all commodities which should have been available for disposal at the completion of projects. According to the information available at USAID/Kenya, $907,573 worth of commodities were procured under completed project numbers 615-0220 and 615-0241. However, USAID/Kenya did not have reasonable assurance that these commodities were disposed of in accordance with A.I.D. policies and procedures as follows:

- **Rural Private Enterprise Project No. 615-0220:** The contractor's -- World Education Incorporation -- final report dated June 1991 indicated that $273,790 was spent on commodities. The contractor submitted to USAID/Kenya on June 30,1991 a listing with commodities valued at KSh.15,264,935 ($560,387). However, that listing was not reconciled with $273,790 contained in contractor's final report. In another contract under this project -- the Deloitte Haskins and Sells contract --$42,546 was spent on commodities. This amount was not reconciled to the Deloitte's statement of costs to ensure that it was complete and accurate, and we could not determine how $27,610 of these commodities were disposed of. Furthermore, we could not determine how commodities valued at $73,412 appearing in MACS report PO7A were disposed. Also, we could not determine how commodities valued at $219,015 procured by the local banks were disposed. These commodities included vehicles, computers and photocopiers.

- **CORAT Child Survival and Family Planning Project No. 615-0241:** The MACS PO7A report at January 31, 1992 showed that $298,810 had been disbursed for commodities under this project. USAID/Kenya on January 13, 1992 requested the grantee to submit a list of A.I.D.-financed commodities. This was the first listing submitted by the grantee and neither the auditors nor USAID/Kenya could determine whether any items were missing because information to make such a determination was not available. Furthermore, the listing contained commodities valued at KSh.6,367,615 ($233,760) which was not reconciled to the $298,810 shown in USAID/Kenya's records.

The causes of the problems with commodity disposal are similar to the problems with receipt, storage and use of commodities discussed under Audit Objective Two. First, USAID/Kenya project officers, though generally aware of A.I.D. Handbooks requirements, did not have specific knowledge of their duties and responsibilities regarding project commodities. The project officers believed that it was not their responsibility to monitor commodity disposal. The project officers believed the grantees were responsible for monitoring the commodities under their control.

Second, USAID/Kenya did not give commodity management a high priority. USAID/Kenya project officers stated that most of their time was taken up preparing Project Implementation Letters, Project Implementation Orders and other related project management paperwork. Therefore, the project officers stated that they did not have the time to make site visits, prepare trip reports, test inventory records and perform end-use checks.

Third, most of the project officers had not received training in commodity management.

Fourth, USAID/Kenya did not report the weaknesses associated with the disposal of commodities in its last Federal Managers' Financial Integrity Act reporting cycle. Thus, the weaknesses identified above continued to exist.

--- *USAID/Kenya did not have reasonable assurance that A.I.D.-financed commodities totaling at least $907,573 for the two terminated projects were disposed of in accordance with A.I.D. policies and procedures.*

As a result of the above problems, USAID/Kenya did not have reasonable assurance that A.I.D.-financed commodities totaling at least $907,573 for the two completed projects were disposed of in accordance with A.I.D. policies and procedures. Since it could not reconcile commodities disposed of at the completion of projects to what A.I.D. paid for and received, USAID/Kenya could not account for the disposal of $907,573 worth of commodities disposed under the two completed projects. Unless corrected, these weaknesses will also impact on commodities for the nine on-going projects with commodities valued at $9 million.

Based on the above, we concluded that USAID/Kenya needed to (1) obtain from contractors and grantees a complete and accurate accounting for the commodities disposed under projects numbers 615-0220 and 615-0241, reconcile inventories to disbursements made by USAID/Kenya, and account for any discrepancies, and (2) establish and implement a system for monitoring commodity disposal to include, among other things, ensuring that contractors and grantees take annual inventories, reconcile inventories to disbursements, account for the discrepancies and take appropriate action for any discrepancies. Furthermore, we considered this to be a material weakness and a reportable condition under the Federal Managers' Financial Integrity Act if the problems remain uncorrected.

REPORT ON INTERNAL CONTROLS

This section provides a summary of our assessment of 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 assess the applicable internal controls when necessary to answer the audit objectives. Those standards also require that we report on the controls assessed, the scope of our work, and any significant weaknesses found during the audit.

In planning and performing our audit, we considered A.I.D.'s internal control structure to determine our auditing procedures in order to answer the audit objectives and not to provide assurance on USAID/Kenya's overall internal control structure.

For the purposes of this report, we have classified significant internal control policies and procedures applicable to the audit objectives by categories. For each category, we obtained an understanding of the design of relevant policies and procedures, determined whether they were placed in operation, and assessed control risk.

General Background on Internal Controls

Under the Federal Managers' Financial Integrity Act (the Integrity Act) and implementing policies issued by the Office of Management and Budget (OMB), A.I.D. is responsible for establishing and maintaining adequate internal controls. The General Accounting Office (GAO) has issued a document entitled "Standards For Internal Controls In The Federal Government" to be used by agencies in establishing and maintaining internal 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 not be detected. Moreover, predicting whether a system will work in the future is risky because changes in conditions may require additional procedures or the effectiveness of the design and operation of policies and procedures may deteriorate.

In performing this audit, we found certain problems which we consider reportable under the Integrity Act and OMB's reporting requirements. Reportable conditions are those which in our judgement could adversely affect A.I.D.'s ability to ensure that resource use is consistent with laws, regulations and policies; that resources are safeguarded against waste, loss and misuse; and that reliable data is obtained, maintained, and disclosed in reports.

Conclusions for Audit Objective One

Audit objective one sought to establish whether USAID/Kenya followed A.I.D. policies and procedures in planning for commodity needs. In planning and performing our audit work, we considered the applicable internal control policies and procedures cited in A.I.D. Handbook 11 chapter 3 and Handbook 3 chapter 13. For the purposes of this report, we have classified the relevant policies and procedures into the following processes: (i) commodity needs assessment, (ii) commodity specifications, and (iii) coordination of commodities with the availability of facilities, spare parts, supplies and skills.

Based on the information that USAID/Kenya did provide and the tests we performed, we can report that, in 3 of 11 projects, commodity procurement was not coordinated with the availability of facilities, spare parts, supplies and skills. For the purposes of this audit objective, we considered this a significant reportable condition. However, for the purposes of the Integrity Act, we did not consider this problem a material reportable condition.

Conclusions for Audit Objective Two

Audit objective two sought to establish whether USAID/Kenya followed A.I.D. policies and procedures in monitoring the receipt, storage and use of A.I.D.-financed commodities. In planning and performing our audit work, we considered the applicable internal control policies and procedures cited in A.I.D. Handbook 15 Chapter 10, Handbook 1B Chapter 24 and the Federal Managers' Financial Integrity Act requirements.

For the purposes of this report, we have classified the relevant policies and procedures into the following processes: (i) commodity inspection, (ii) comparison of quantities ordered against what was paid for and received, (iii) physical inventories and reconciliations, (iv) reporting on the use of A.I.D.-financed commodities, and (v) accounting for commodities during the life of the project. Our review of internal controls related to these processes showed that internal controls were not properly implemented and therefore we could not rely on these controls in performing the audit. We conducted extensive tests, described in Appendix 1, to answer this audit objective.

The following are the significant reportable weaknesses noted:

- Controls were not implemented to ensure that (1) commodities paid for were received in the nature and quantities for which the payment was made, (2) inventories of A.I.D.-financed commodities were periodically taken by the contractors and grantees and reported to USAID/Kenya, (3) reconciliations were made between the physical inventories and the book quantities, and (4) commodities were accounted for during the life of the project or contract.

These internal control weaknesses were not included in USAID/Kenya 1991 internal control assessment. Therefore, we recommended that these weaknesses be included in the next assessment if they are not corrected.

Conclusions for Audit Objective Three

Audit Objective three sought to establish whether USAID/Kenya followed A.I.D. policies and procedures in monitoring the disposal of commodities at the completion of projects. In planning and performing our audit work, we considered the applicable internal control policies and procedures cited in A.I.D. Handbooks 14 and 15 and the Federal Managers' Financial Integrity Act requirements.

For the purposes of this report, we have classified the relevant policies and procedures into the following processes: (i) physical inventories, (ii) inventory reporting, (iii) reconciliations between physical and book inventories, and (iv) accounting of commodities at the completion of projects or contracts. Our review of internal controls related to these processes showed that internal controls were not properly implemented and therefore we could not rely on these controls in performing the audit. We conducted extensive tests, described in Appendix 1, to answer this audit objective.

The following are the significant reportable weaknesses noted:

- Controls were not implemented to ensure that (1) inventories of A.I.D.-financed commodities were periodically made by contractors and grantees and reported to USAID/Kenya, (2) reconciliations were made between physical inventories and book quantities, and (3) commodities were accounted for at the close of projects or contracts.

These internal control weaknesses were not included in USAID/Kenya's 1991 Internal Control Assessment. Therefore, we recommended that they be included in USAID/Kenya's next assessment if not corrected.

REPORT ON COMPLIANCE

This section summarizes our conclusions on USAID/Kenya's compliance with the:

- Federal Managers' Financial Integrity Act which requires each mission to comply with the Act as set forth by binding policies in Department of State cables sent to the missions each year, and

- Federal Acquisition Regulations Sub-Part 45.508.

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. Those standards also require that we report significant instances of noncompliance and abuse and indications or instances of illegal acts that could result in criminal prosecution that we found during or in connection with the audit.

We tested USAID/Kenya's compliance with certain provisions of the Federal Manager's Financial Integrity Act of 1982 which requires each mission to comply with the Act as set forth by binding policies in Department of State cables sent to missions each year. Also, we tested USAID/Kenya's compliance with Part 45.508 of the Federal Acquisition Regulations relating to commodity disposal.

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 entity's conduct. Noncompliance constitutes an illegal act when the source of the requirement not followed or prohibition violated is a statute or implementing regulation, 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 and is included in our report on internal controls. Abuse is distinguished from noncompliance in that abusive conditions may not directly violate laws and 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 the Federal Managers' Financial Integrity Act is the overall responsibility of A.I.D. which, in turn, requires each mission to comply with the Act as set forth by binding policies in Department of State cables sent to missions each year.

Conclusions on Compliance

We reviewed USAID/Kenya's compliance with the general assessment cable guidance for 1991. Based on the information that USAID/Kenya did provide to us and the tests we were able to perform, we can report that USAID/Kenya performed an internal control assessment (which included project commodities) for the year ending September 30, 1991, and that no irregularities or instances of violations of laws and regulations came to our attention. However,USAID/Kenya did not dispose of commodities in accordance with Sub-Part 45.508 of the Federal Acquisition Regulations relating to the disposal of A.I.D.-financed commodities, which is discussed as an internal control problem under Audit Objective No. 3.

MANAGEMENT COMMENTS AND OUR EVALUATION

The following is a summary of management's comments on our draft report and our evaluation of the comments. This section is organized by the report's recommendations which is in the same order that management presented their comments. The complete text of management comments, together with the representation letter they provided, is included as Appendix II to this report.

Recommendation No. 1.1

In response to Recommendation No. 1.1, USAID/Kenya stated that it was not sure why a recommendation was needed since only 3 of 11 projects had problems. It believed that planning for commodity procurement under the three projects was done, but problems arose in the implementation. USAID/Kenya asked that this recommendation be deleted from the report.

RIG/A/N believes that the problems identified in the three projects were systemic and that the recommended procedures are needed to ensure that similar problems do not occur in future. For example, such procedures would have enabled USAID/Kenya to adjust its procurement plan for laboratory equipment under the National Agricultural Research Project. Laboratory equipment under this project were received in four research stations from as early as March 1990 while construction of facilities did not begin until April 1992 in one station and April 1991 in the other three stations. Also, the three projects represent 27 percent of the projects audited which we consider significant.

Thus, Recommendation No. 1.1 is unresolved. This recommendation will be resolved when USAID/Kenya communicates to this office its agreement with the recommended actions. It will be closed upon receipt of documentar evidence that the recommended procedures have been established.

Recommendation No. 1.2

USAID/Kenya agreed with the finding and recommendation and stated that it had instructed the prime contractor to defer the procurement of additional laboratory equipment under Phase II of the NARP project until the construction of laboratories is completed. Also, USAID/Kenya states they will not consider procurement of IUCDs until future analyses are conducted as part of the mission's annual contraceptive estimates, and until gloves and other supplies are made available.

Based on these comments by USAID/Kenya, Recommendation No. 1.2 is resolved and can be closed when RIG/A/N receives documentary evidence supporting the actions mentioned in USAID/Kenya's comments.

Recommendation No. 2.1

Regarding Recommendation No. 2.1, USAID/Kenya agreed with the finding, but did not believe that it was necessary to reconcile borrower/grantees' commodity records with its accounting records and wanted us to delete references to reconciliations from this recommendation. USAID/Kenya stated that it could not find any policy or procedure that requires the recommended reconciliations. In addition, USAID/Kenya stated that the commodities line item in Mission records may include items such as expendable supplies, spare parts, maintenance contracts and training that relate to the commodity procurement. USAID/Kenya further stated that the commodities line item sometimes contains commodity procurement for several grantees and contractors under the same project.

RIG/A/N believes that the recommended reconciliation under Recommendation No. 2.1 is an important control procedure to ensure the receipt, existence and use of commodities paid for by A.I.D. Unless such reconciliations are performed, USAID/Kenya cannot reasonably assure itself that A.I.D.-financed commodities, as recorded in its accounting records, were received, stored and used as intended. In addition, A.I.D. Handbook 19 Chapter 1 Appendix D, which is consistent with the Standards For Internal Control In The Federal Government requires periodic comparisons of existing assets with the recorded accountability and appropriate actions taken with respect to any differences. We believe that the recommended reconciliation will satisfy this requirement.

Thus, Recommendation No. 2.1 is unresolved. This recommendation will be resolved when USAID/Kenya communicates to this office its agreement to establish and implement the recommended commodity monitoring system. Recommendation No. 2.1 will be closed upon receipt of documentary evidence that the recommended system has been established and implemented.

Recommendation No. 2.2

USAID/Kenya agreed with Recommendation No. 2.2 and stated that beginning with the next employee evaluation report cycle, it will include a requirement for commodity management in the appropriate project officers' continuing responsibilities.

Based on USAID/Kenya's comments, Recommendation No. 2.2 is resolved. It will be closed when this office receives documentary evidence or certification by the Mission Director that requirements for commodity management are included in the appropriate employee evaluation reports.

Recommendation No. 2.3

Concerning Recommendation No. 2.3, USAID/Kenya agreed with the finding and recommendation and stated that it had asked the REDSO/ESA Commodity Management Officer to conduct a commodity management course for project officers in November 1992.

Based on these comments by USAID/Kenya, Recommendation No. 2.3 is resolved. It will be closed when RIG/A/N receives documentary evidence that a commodity management course for project officers was conducted.

Recommendation No. 2.4

USAID/Kenya did not concur with Recommendation No. 2.4 and asked that it be re-written to remove references to reconciliations. USAID/Kenya stated that the recommendation imposes requirements on the grantees/contractors that are not contained in the mandatory provisions of Handbooks 3 and 13 or in the standard contract provisions. Also, USAID/Kenya stated that this recommendation imposes a burden on the Mission when the time could be more productively spent in monitoring. In addition, USAID/Kenya stated that the methodology that was used to compare MACS records to recipient/contractor records was faulty because the auditors used an average exchange rate while the MACS system uses the exchange rate on the day the transaction was processed. Thus, USAID/Kenya concluded that it did not find it productive to duplicate contractors' records or reconcile exchange rate differences that really did not exist. USAID/Kenya made specific comments on the unreconciled differences under 7 of 11 sampled projects as follows:

- **Agricultural Management Project No. 615-0221:** USAID/Kenya stated that the difference of $27,567 was because commodities procured by the contractor were charged to the technical assistance component in MACS whereas commodities procured by USAID/Kenya for other grantees/contractors were charged to the commodity component.

- **National Agricultural Research Project No. 615-0229:** USAID/Kenya stated that the difference of $859,327 was because commodities procured by the contractor were charged to the technical assistance component in MACS whereas commodities procured by USAID/Kenya for other grantees/contractors were charged to the commodity component. Also, USAID/Kenya stated that it has instructed the contractor to ascertain the whereabouts of unlocated commodities valued at $63,670.

- **Private Enterprise Development Project No. 615-0238:** USAID/Kenya stated that it has asked for commodity listings from the International Executive Service Corps (IESC), Kenya National Chamber of Commerce and Industry (KNCCI), and Kenya Management Assistance Program (KMAP). USAID/Kenya acknowledged that the listing given to the auditors did not include A.I.D.-financed commodities such as furniture, a franking machine and a motor vehicle under the KMAP component of this project. USAID/Kenya further stated that it had PILs and proforma invoices for the commodities under the Kenya Association of Manufacturers (KAM) and Investment Promotion Center (IPC) components of this project.

- **Structural Adjustment Assistance Program No. 615-0240:** USAID/Kenya stated that it would ensure that the contractor for the Resource Management for Rural Development (Project No. 615-0240.01) complies with contract requirements with regard to an inventory of the property. Under the Micro Computerization component of this project (Project No. 615-0240.02), USAID/Kenya stated that the contractor had submitted two additional commodity listings without values which would explain the unreconciled difference of $435,866.

- **Kenya Health Care Financing Project No. 615-0245:** USAID/Kenya stated that the unreconciled difference of $21,385 was a result of the auditors using an average exchange rate.

- **Kenya Contraceptive Social Marketing Project No. 615-0251:** USAID/Kenya stated that the unreconciled difference of $24,753 was a result of the auditors using an average exchange rate. USAID/Kenya further stated that the list of commodities given to the auditors inadvertently included a fax machine and a calculator which were sold and stolen, respectively.

- **Park Rehabilitation and Management Project No. 615-0253:** USAID/Kenya stated that the unreconciled difference of $198,378 was entirely due to the auditors using an average exchange rate.

We do not agree that Recommendation No. 2.4 imposes requirements on the grantees and contractors that are not contained in A.I.D. Handbooks 3 and 13 and standard contract provisions. A.I.D. Handbook 13 Chapter 4 page 4C-61 clearly requires grantees to maintain accurate commodity records which include among other information: commodity description, identifying serial numbers, source of the commodity, date of acquisition, cost, location, use and condition of the commodity. Also, the Federal Acquisition Regulations Part 45-508 requires contractors to perform physical inventories of Government property which consists of sighting, tagging or marking, describing, recording, reporting, and reconciling the commodities with inventory records. The contractors are required to promptly submit to A.I.D. commodity listings that identify all discrepancies disclosed by the physical inventory. We believe that to be useful in monitoring the receipt, existence and use of A.I.D.-financed commodities, the grantee/contractor commodity listings should be checked against independent records which, in this case, are the accounting records maintained by USAID/Kenya. In addition, we believe that the accounting records maintained by USAID/Kenya would not be useful for monitoring A.I.D.-financed commodities if such accounting records were not reconciled with the grantee/contractor commodity listings. For example, if such a reconciliation was performed, USAID/Kenya would have known that A.I.D.-financed commodities such as furniture, a franking machine and motor vehicle were not included in the commodity listing submitted by KMAP.

Furthermore, the auditors used an average exchange rate in 4 of 11 sampled projects because USAID/Kenya provided commodity listings whose values were in Kenya Shillings while its accounting records are in U.S. dollars. As stated on page 19, the commodity listings provided by USAID/Kenya did not include information such as dates of acquisition/arrival which would have enabled us to use specific, rather than an average, exchange rate. However, we do not agree with USAID/Kenya's assertion that the unreconciled differences for the 4 projects are entirely due to exchange rate differences since there is nothing to support this. The recommended commodity listings and reconciliations will enable USAID/Kenya to determine extent of the differences due to exchange rate and other factors such as missing commodities. In addition, USAID/Kenya's comments on the specific projects show that the recommended commodity listings and reconciliations are necessary and possible.

Thus, Recommendation No. 2.4 is unresolved. The recommendation can be resolved when USAID/Kenya communicates to this office its agreement to obtain from the grantees and contractors current commodity listings, reconciles those listings with USAID/Kenya commodity records and, for quantities and amounts that cannot be reconciled, makes a final determination of the amounts that are allowable/unallowable. The recommendation can be closed upon receipt of documentary evidence that USAID/Kenya has obtained from grantees and contractors current commodity listings and, for those quantities and amounts that cannot be reconciled, (1) made a formal written determination that the costs are allowable and/or (2) issued a bill for collection for the amount that is determined not to be allowable.

Recommendation No. 2.5

For Recommendation No. 2.5, USAID/Kenya stated that it would initiate steps in cooperation with the Division of Family Health and Medical Supplies Coordinating Unit (MSCU) to reconcile the discrepancies in USAID/Kenya's shipping documents with the receiving records at the MSCU and determine the allowability of amounts that cannot be reconciled.

Based on USAID/Kenya's comments, Recommendation No. 2.5 is unresolved. To resolve Recommendation No. 2.5, USAID/Kenya needs to make a final determination on the amount that is allowable/unallowable, as the case may be. The recommendation can be closed when RIG/A/N receives documentary evidence that the Mission has (1) made a formal written determination that the costs are allowable and/or (2) issued a bill for collection for the amount that is determined to be unallowable.

Recommendation No. 2.6

Concerning Recommendation No. 2.6, USAID/Kenya stated that it did not view attempts to obtain an accounting of unlocated contraceptives or determining their allowability feasible or cost-effective. USAID/Kenya stated that it acknowledged the likelihood of record keeping laxity in the sub-depots and districts visited during the audit. However, USAID/Kenya believed that the audit report did not go far enough in describing the implications of this finding because the fact that the commodities were not logged-in at the receiving facility might suggest that they did not arrive as intended and this was not the case. In addition, USAID/Kenya stated that it believed that neither record keeping laxity nor any other observable conditions necessarily suggested diversion of commodities away from the intended recipient facility. Thus, USAID/Kenya requested that Recommendation No. 2.6 be closed.

RIG/A/N believes it is inappropriate for USAID/Kenya to assert that there was no diversion of commodities away from the intended recipient facility and that the commodities which could not be traced during the audit were purely as a result of record keeping laxity. In addition, we do not agree with USAID/Kenya's assertion that it is neither feasible nor cost-effective to obtain an accounting of contraceptives that could not be traced during the audit and to determine the allowability of the quantities and amounts that cannot be reconciled. It is feasible because A.I.D. policies and procedures require project records to be maintained throughout the life of a project and for at least 3 years after the completion of the project. The commodities in question relate to the most recent period of an on-going project. Thus, in accordance with A.I.D. policies and procedures, records should be available to account for the unlocated contraceptives. If they are not, the allowability (or liability) for quantities and amounts that cannot be accounted for must be determined. Furthermore, we believe the recommended action is cost-effective because, as part of its monitoring responsibility, USAID/Kenya must ensure that A.I.D.-financed commodities are received, stored and used as intended.

Thus, Recommendation No. 2.6 is unresolved. The recommendation can be resolved when USAID/Kenya (1) communicates to this office its agreement to obtain from the Government of Kenya's Medical Supplies Coordinating Unit an accounting for contraceptive issues of 6,028,000 condoms valued at $284,944; 47,600 intrauterine contraceptive device units valued at $50,942; and 459,600 foaming tablets valued at $43,906 which could not be traced during the audit, and (2) makes a final determination on the allowability of the quantities and amounts that cannot be reconciled. The recommendation can be closed when RIG/A/N receives documentary evidence that USAID/Kenya has obtained an accounting for those contraceptives and, for those quantities and amounts that cannot be reconciled, (1) made a formal written determination that the costs are allowable and/or (2) issued a bill for collection for the amounts that are unallowable.

Recommendation No. 2.7

Regarding Recommendation No. 2.7, USAID/Kenya disagreed with the findings and the conclusion upon which the recommendation was based because of an August 17, 1992 letter from Kenya Wildlife Services (KWS). The KWS letter states that the grader at the Tsavo East National Park was repaired at a cost of KSh.1,141,875 which was approved by KWS. Also, according to USAID/Kenya, an August 20, 1992 letter from the workshop manager of Tsavo East National Park confirmed that the grader had been repaired. In addition, the August 17, 1992 letter from KWS stated that Pan African Equipment had repaired the motor grader at Mount Elgon National Park and an August 18, 1992 stated that the auditors must have obtained information from an unreliable source. Thus, USAID/Kenya asked us to delete Recommendation No. 2.7.

We believe that USAID/Kenya's comments further support the need to establish and implement a commodity monitoring system. For example, we do not believe that USAID/Kenya should have based its comments regarding Recommendation No. 2.7 on letters from KWS. The KWS letters were from the same official who provided the listing used by the auditors and which contained the questioned costs. The auditors physically inspected the motor graders at both Tsavo East and Mount Elgon National Parks and discussed their condition with the users. At Tsavo East National Park, the auditors were told by the warden responsible for use of the grader that the grader had never been grounded and was not aware of any rehabilitation that was done to the grader. We believe that the user at the Tsavo East National Park is more knowledgeable about the grader than the official at the KWS Headquarters. Also, at Mount Elgon, the auditors did not obtain information from an unreliable source as asserted by KWS, and accepted as correct by USAID/Kenya. We obtained the information from the Park Warden and a workshop official. RIG/A/N believes USAID/Kenya should likewise independently verify the information from the parks in order to ensure A.I.D.-funded commodities were used for their intended purposes.

Thus, Recommendation No. 2.7 is unresolved. The recommendation can be resolved when USAID/Kenya makes a final determination on the amounts that are allowable/unallowable. It can be closed upon receipt by RIG/A/N of documentary evidence of (1) a formal written determination that the costs are allowable and/or (2) issuance of a bill for collection for the amount that is determined to be unallowable.

Recommendation No. 2.8

Regarding Recommendation No. 2.8, USAID/Kenya agreed with the finding and recommendation and stated that it was reviewing the internal controls in place during 1992 to determine weaknesses to report to AA/AFR.

Based on the above comments by USAID/Kenya, Recommendation No. 2.8 is resolved and can be closed upon receipt of documentary evidence that the weaknesses regarding the monitoring of receipt, storage and use of project commodities have been corrected, or reported to AA/AFR in USAID/Kenya's next Internal Control Assessment.

Recommendation No. 3.1

Regarding Recommendation No. 3.1, USAID/Kenya requested that it be re-written to remove references to reconciliations. In addition, USAID/Kenya made specific comments regarding the two projects audited under Audit Objective No. 3 as follows:

- **CORAT Child Survival and Family Planning Project No. 615-0241:** USAID/Kenya wants references to this project deleted, stating that the unreconciled difference of $65,041 is a result of using an average exchange rate rather than the rate used when the voucher was processed. However, when we requested commodity listings, USAID/Kenya provided to us listings in Kenya Shillings. We could not convert the unit costs to U.S. dollars since the auditors are not responsible for preparing commodity lists.

- **Rural Private Enterprise Project No. 615-0220:** USAID/Kenya stated that the contractor -- World Education Incorporation -- was in the process of compiling lists of commodities for submission to USAID/Kenya. Also, USAID/Kenya stated that it would verify the disposal of commodities valued at $27,610 under the Deloitte Haskins and Sells contract. In addition, USAID/Kenya stated that it had received a listing of commodities procured by the banks and was in the process of reviewing it.

As stated under Audit Objective Two above, the auditors used an average exchange rate for this project because USAID/Kenya provided commodity listings whose values were in Kenya Shillings while its accounting records are in U.S. dollars. As stated on page 19, those commodity listings did not include information such as dates of acquisition/arrival which would have enabled us to use specific, rather than an average, exchange rate. However, we do not agree with USAID/Kenya's assertion that the unreconciled difference of $65,041 for CORAT is entirely due to exchange rate differences since there is nothing to support that. The recommended commodity accounting and reconciliation will enable USAID/Kenya to determine the extent of the differences due to exchange rate as well as other factors such as missing commodities.

Thus, Recommendation No. 3.1 is unresolved. It will be resolved when USAID/Kenya (1) communicates to this office its agreement to obtain from the contractors and grantees a complete and accurate accounting for the commodities disposed under project numbers 615-0220 and 615-0241, (2) reconciles the inventories to the disbursements made by USAID/Kenya, and (3) makes a final determination on the allowability of any unreconciled differences. The recommendation can be closed upon receipt by RIG/A/N of documentary evidence that USAID/Kenya has obtained from grantees and contractors the recommended accounting for the commodities and, for any improperly disposed commodities, (1) made a formal determination that the amounts are allowable and/or (2) issued a bill for collection for any amount determined to be unallowable.

Recommendation No. 3.2

Regarding Recommendation No. 3.2, USAID/Kenya asked that it be deleted because it planned to incorporate the requirements of this recommendation under the planned actions for Recommendation No. 2.1. Also, USAID/Kenya did not believe it was necessary to reconcile project commodities at the completion of projects to the disbursements made by A.I.D. However, Recommendation No. 2.1 relates to the systems for receipt, storage and use rather than the disposal of commodities. RIG/A/N is not opposed to USAID/Kenya using the same Mission Order for the two recommendations, but for the purposes of the audit report, we believe the two recommendations should be kept separate. Also, we believe that the recommended procedures are necessary to effectively monitor the disposal of A.I.D.-financed commodities.

Thus, Recommendation No. 3.2 is unresolved. This recommendation will be resolved when

USAID/Kenya communicates to this office its agreement to establish and implement the recommended system to monitor commodity disposal. The recommendation will be closed upon receipt of documentary evidence that the recommended system has been established and implemented.

Recommendation No. 3.3

Regarding Recommendation No. 3.3, USAID/Kenya asked that it be combined with Recommendation No. 2.8. However, Recommendation No. 2.8 relates to the systems for receipt, storage and use rather than the disposal of commodities. Thus, RIG/A/N believes that the two recommendations should be kept separate.

Thus, Recommendation No. 3.3 is unresolved. This recommendation will be resolved when USAID/Kenya communicates to this office its agreement to report, to the AA/AFR, the internal control weaknesses associated with its commodity disposal monitoring system if the weaknesses are not corrected. Recommendation No. 3.3 can be closed upon receipt of documentary evidence that the weaknesses regarding the monitoring of receipt, storage and use of project commodities have been corrected, or reported to AA/AFR in USAID/Kenya's next Internal Control Assessment.

SCOPE AND METHODOLOGY

Scope

We audited USAID/Kenya's management of project commodities in accordance with generally accepted government auditing standards. As the management official most responsible for the USAID/Kenya commodities program, the Mission Director confirmed in writing -- to the best of his knowledge and belief -- that USAID/Kenya had provided us with information essential for us to answer our audit objectives (see Appendix II). However, the management officials most knowledgeable about the program -- those USAID/Kenya officials who daily manage the commodities program -- would not provide such a written confirmation to either the Mission Director or us. Therefore, our answers to the audit objectives are qualified because the lack of such confirmations from the most knowledgeable management officials is a scope limitation on our audit.

We carried out the audit from January 7, 1992 to July 23, 1992 in the offices of USAID/Kenya. In performing our audit, we obtained documentary and testimonial evidence in the offices of technical assistance contractors, grantees and various Government of Kenya institutions and non-governmental organizations in Kenya. This is discussed in detail under the methodology for each audit objective. The audit covered the systems and procedures relating to (1) planning for commodity needs, (2) receipt, storage and use, and (3) disposal of commodities at the completion of projects financed by A.I.D. from August 25, 1983 to January 31, 1992.

Total obligations for USAID/Kenya's portfolio of 17 projects with commodity procurement amounted to $339.3 million as of January 31, 1992. Our audit sample of 11 projects had total obligations of $197.6 million which represented 58 percent of the total obligations for the 17 projects. The audit covered project commodity obligations and disbursements of $12.6 million and $9.9 million, respectively.

Our audit did not include commodities under the Commodity Import Programs with obligations and disbursements of $110 million and $92 million, respectively[4]. Commodity Import Programs were the subject of an earlier RIG/A/N audit -- Audit Report No. 3-615-92-03 dated November 29, 1991. Also, we did not examine operating expenses funded commodities that were purchased by USAID/Kenya. Furthermore, we excluded the recently started projects from our sample for which commodity procurement had not been completed.

As part of this audit, we reviewed USAID/Kenya's internal control assessment for 1991 in light of the internal control weaknesses identified in the Report on Internal Controls (see page 19) and found they had not been reported. We also reviewed three prior RIG/A/N audit reports -- Audit Report Nos. 3-615-89-11 (Kenya Rural Private Enterprises), 3-615-91-08 (USAID/Kenya Compliance With Audit Requirements), 3-615-92-03 (USAID/Kenya Commodity Import Programs), and 3-698-92-06 (Nairobi Regional Financial Management Center's System of Internal Controls as They Relate to MACS).

Methodology

Our criteria for selection of the audit sample were projects that had total obligations in excess of $1 million as of January 31, 1992 with a termination date of December 31, 1990 and later. As a result, our sample of 11 projects had total obligations of $197.6 million which represented 58 percent of the total obligations for USAID/Kenya's portfolio of 17 projects with commodity procurement. Of the 11 projects in our sample, 2 projects had been terminated and 9 projects were active. Our audit sample represented 33 percent of project commodity obligations and 28 percent of project commodity disbursements at USAID/Kenya. Therefore, we concluded that our sample was representative of USAID/Kenya's commodity portfolio. We used the audit sample for the three audit objectives. The specific methodology for each audit objective follows:

Audit Objective One

To accomplish the first audit objective, we used the criteria established in A.I.D. Handbook 11 chapter 3, Handbook 3 chapter 13, the Federal Managers' Financial Integrity Act of 1982 and its implementing guidance set forth in Department of State cables sent to missions every year to determine whether USAID/Kenya followed A.I.D. policies and procedures in planning for commodity needs. We determined whether (1) project papers and grant agreements included evidence of planning for commodity needs at the project development

[4] The source of these amounts was MACS Report No. PO6B as of January 31, 1992. RIG/A/N Audit Report No. 3-698-92-06 dated February 14, 1992 found the system of internal controls relating to MACS to be reliable.

stage, (2) project papers and grant agreements included listings of eligible commodities and prescribed geographic codes, and (3) commodity procurement was coordinated with the availability of facilities, spare parts, supplies and skills. We obtained an understanding of USAID/Kenya's internal control environment for this objective through interviews with USAID/Kenya officials as well as officials representing contractors and the Government of Kenya.

To make the above determinations, we selected 11 projects out of 17 projects with commodity procurements in USAID/Kenya's portfolio as of January 31, 1992. We examined procurement plans included in the project papers, program assistance approval documents and grant agreements for the commodities planned. In examining these documents, we determined whether the commodity needs were justified and documented, and that commodity needs were not inflated. In addition, we determined whether the procurement of commodities was coordinated with the availability of facilities, spare parts, supplies and skills.

Audit Objective Two

To accomplish the second objective, we used the criteria established in A.I.D. Handbook 15 chapter 10, Handbook 1B chapter 24, the Federal Managers' Financial Integrity Act of 1982 and its implementing guidance set forth in Department of State cables sent to missions every year to determine whether USAID/Kenya followed A.I.D. policies and procedures in monitoring the receipt, storage and use of A.I.D. -financed commodities. We determined whether USAID/Kenya established monitoring procedures to ensure that commodities paid for by A.I.D. were (1) received in the nature and quantities for which payments were made, (2) properly stored to safeguard them against waste, loss and theft, and (3) used for intended purposes.

To make the above determinations, we examined 11 projects in USAID/Kenya's portfolio with commodity obligations of $12.6 million as of January 31, 1992. We held discussions with USAID/Kenya officials to establish whether internal control systems were in place for monitoring the receipt, storage and use of A.I.D.-financed commodities. In addition, we examined available documents and reports on A.I.D.-financed commodities from USAID/Kenya, contractors, grantees and the Government. Also, we conducted site visits to physically inspect commodities, test the accuracy of inventory records and interview contractors, grantees and Government officials who were responsible for the mechanics of the receipt, storage and use of commodities. The physical inspections covered the following project sites:

- four Agricultural research stations at Mtwapa, Kakamega, Kitale and Embu,

- eight national parks at Tsavo East, Tsavo West, Ruma, Aberdares, Mount Elgon, Simba Hills, Hell's Gate and Meru,

- twenty seven Ministry of Health facilities -- three medical depots and 24 hospitals,

- the Kenya Health Care Financing Project offices in Nairobi,

- the Kenya Contraceptives Social Marketing Project in Nairobi,

- the Kenya Rural Private Enterprise Program offices in Nairobi,

- the Kenya Management Assistance Program offices in Nairobi,

- the International Executive Service Corps offices in Nairobi,

- the Kenya National Chamber of Commerce and Industry offices in Nairobi,

- the Egerton University in Nakuru,

- the Resource Management for Rural Development Project offices in Nairobi, and

- the Micro Computerization Project offices in Nairobi.

Audit Objective Three

To accomplish the third objective, we used the criteria established in A.I.D. Handbook 14 Subchapter H, Handbook 15 chapter 10, Handbook 1B Chapter 24, the Federal Managers' Financial Integrity Act of 1982 and its implementing guidance set forth in Department of State cables sent to missions every year to determine whether USAID/Kenya followed A.I.D. policies and procedures to monitor the disposal of A.I.D.-financed commodities at the completion of projects. We determined whether (1) physical inventories were conducted at the completion of contracts/projects, (2) contractors submitted to USAID/Kenya listings of commodities to be disposed of at the end of contracts/projects, and (3) USAID/Kenya reconciled the inventory lists with the amounts disbursed for commodities.

To make the above determinations, we reviewed the only two projects which were completed at the time of audit and for which commodities valued at $907,573 were disposed of. We obtained and analyzed (1) information on commodities procured under the two projects, (2) commodity listings from contractors and grantees, and (3) how commodities were disposed of. We also interviewed responsible contractor and USAID/Kenya officials.

RECEIVED
23 OCT 1992
RIG/A/N

MEMORANDUM

To: Everette B. Orr, RIG/A/Nairobi

From: John W. Westley, Mission Director, USAID/Kenya

Subject: Mission Comments on the Draft Audit Report on USAID/Kenya's Management of Commodities

Date: October 22, 1992

As the Mission plans to provide you with a representation letter, our response is based on the representation letter version of the draft audit report.

The Mission has the following comments on the subject audit report.

Recommendation No. 1.1 requests the Mission to establish procedures to ensure the planning for commodity procurement includes an assessment of the availability of facilities, spare parts, supplies and skills including the necessary coordination with other donors, grantees and the Government of Kenya (GOK).

Response: We note that the audit stated the USAID/Kenya did follow A.I.D. policies and procedures except for three projects; thus we are unsure why a recommendation that we establish procedures is included. We believe that planning was done for the three projects cited, but problems arose in the implementation phase. In the National Agricultural Research Project (NARP) unforeseen construction delays meant that the equipment arrived before the buildings were ready. In the Institutional Development For Agricultural Training Project (IDAT), as the letter from Egerton University (copy attached) indicates, an assessment was made for the facilities, spare parts, supplies and training needs for the computers and the telephone system before these commodities were procured. As more fully explained in our response to Recommendation No. 1.2(2), the Mission believes that planning for contraceptive procurement was adequate in the Family Planning Services and Support Project (FPSS). We ask that this recommendation be deleted from the final report.

Recommendation No. 1.2 requests the Mission to suspend the procurement of (1) $161,000 in additional laboratory equipment under phase II of Project Number 615-229 until the construction of laboratories is completed, and (2) intrauterine contraceptive devices (IUCDs) until the problem of the gloves is addressed and an analysis is done of the quantities available within the depot and the district stores versus the projected needs based on the past usage rates.

Response: The Mission agrees with Recommendation No. 1.2, but wishes to clarify the findings upon which this recommendation is based.

1.2(1). The procurement of additional laboratory equipment under Phase II of the NARP project is planned for FY 1994 which is after the estimated completion date of the laboratories. In any case the Mission will not undertake any procurement unless these laboratories are fully constructed.

1.2(2). Based on the annual Contraceptive Procurement Tables, an exercise carried out jointly with the GOK/Ministry of Health (MOH), USAID/Kenya, A.I.D./W and contractors under the USAID-funded Logistics Management Support Project, the Office of Population/Health (O/PH) can accurately determine the levels of A.I.D.-financed contraceptives required by the national family planning program. The Mission does not believe that the underutilization of IUCD stock observed during the RIG/A audit is the result of overstocking due to poor planning, or oversight in identifying related inputs to ensure that the commodities would be effectively used. The current situation is due to an unforeseen circumstance in which the GOK was not able to keep its commitment to supply the essential examining room expendable supplies (such as latex gloves) which are part of the GOK's recurrent cost responsibilities, and should be routinely available in all health facilities.

The requirement for certain prerequisite inputs to support the use of IUCDs is well understood both by the Mission and the GOK. In the past, USAID has purchased gloves on an emergency basis for the Government of Kenya specifically for family planning-related physical examinations and for insertion of IUCD's. The GOK was to resume supplying gloves needed for family planning procedures as part of its procurement of general medical supplies with effect from January, 1990. However due to financial constraints within the GOK/MOH, this did not happen. To temporarily relieve the gloves shortage, the United Nations Fund for Population Activities (UNFPA) has agreed to provide an interim 36-month supply, but the GOK is expected to find a permanent supply source for gloves within that period of time.

Action taken: (A) The prime contractor under Project 615-0229 has been instructed to defer the procurement of additional laboratory equipment under phase II until the construction of the laboratories is completed and has been directed to ensure that the warranties on the equipment yet to be unpacked at the facilities of the Kenya

Agricultural Research Institute (KARI) is valid until such time as the equipment is put into use.

(B) Based on information being generated by the Contraceptive Logistics Management Information System (CLMIS), and on-going MOH Division of Family Health monitoring of field operations, the problem of under-utilization of IUCDs had already been identified by O/PH and the GOK during 1991. No procurement of IUCDs was initiated in 1992. In 1992 the Division of Family Health began a field-based assessment (currently on-going), to determine the IUCD pipeline situation and future requirements. The Mission has no current commitment for resupply of IUCDs, and will not consider further procurement of IUCDs until future analyses are conducted as part of the Mission's annual contraceptive procurement estimates, and until gloves and other essential examining room expendable supplies are routinely available at service sites.

Based on the foregoing, we request that Recommendation No. 1.2 be resolved and closed upon issuance of the final report.

Recommendation No. 2.1 requests the Mission to establish and implement a monitoring system, which includes evaluating borrower/grantee systems for the receipt, storage and use of AID-financed commodities and reconciling USAID/Kenya records with those of the borrower/grantee on a periodic basis for all on-going and future projects.

Response: The Mission concurs with the recommendation in part. We note that the recommendation refers to borrower/grantee systems, but that the audit findings are based on the commodity management of both grantees and direct and host country contractors. We agree there is confusion on the part of Mission personnel on project commodity management in part because monitoring requirements are more explicit for Handbook 3 grants than for Handbook 13 and are less clear when it comes to contractors.

We believe that this confusion is reflected in the audit report as well. For example, the audit says that commodity listings for the projects audited were incomplete because they did not include the required information such as identifying serial numbers, dates of arrival, and locations. This required information is applicable to Handbook 13 grant commodities, but there is no requirement for this information on the report on property which a contractor submits upon completion of the contract.

We also do not concur that our monitoring system should include a requirement that A.I.D.-financed commodities be reconciled to USAID/Kenya records. The handbooks and standard provisions require that recipients/contractors periodically reconcile their physical inventories with their records, but we can find no policy or procedure that requires that these inventories be reconciled to the Mission records. The Commodities line item in Mission records may include such items as expendable supplies, spare parts, maintenance contracts and training that relate to the commodity procurement. In addition, the Commodity line time sometimes contains commodity procurement for several grantees and contractors under the same project.

The Mission does evaluate borrower/grantee systems as part of its financial review of implementing agencies.

The Mission would concur with a recommendation such as the following:

We recommend that USAID/Kenya establish and implement a monitoring system, which includes evaluating borrower/grantee systems for the receipt, storage and use of A.I.D.-financed commodities, to ensure that project commodities are received, used and disposed of in compliance with all applicable rules and regulations.

The draft Mission Order referred to above addresses these issues by compiling the guidance contained in a number of Handbooks to clarify the responsibilities of and within the Mission. We ask that the recommendation be revised as suggested and resolved upon issuance of the final report.

Recommendation No. 2.2 requires the Mission to include the requirement for commodity management in the project officers' employee evaluation reports as appropriate.

Response: The Mission concurs.

Action taken: Beginning with the next EER cycle, the Mission will include a requirement for commodity management in appropriate project officers' continuing responsibilities. Therefore, we request that this recommendation be resolved and closed upon issuance of the final report.

Recommendation No. 2.3 requires the Mission to provide commodity management training for project officers.

Response: The Mission concurs in the recommendation, although we believe that project officers are generally aware of their responsibilities. Training will enable them to carry them out more effectively.

Action Taken: The Mission has asked the Regional Commodity Management Officer, REDSO/ESA, and he has agreed, to conduct a commodity management course for project officers in November 1992. This recommendation should therefore be closed upon issuance of the final report.

Recommendation No.2.4 requests the Mission to obtain from the grantees and contractors commodity listings that reconcile with USAID/Kenya's commodity records for Projects 615-221, 615-229, 615-0232, 615-0238, 615-0240.01, 615-0240.02 615-0245, 615-0251 and 615-0253.

Response: The Mission does not concur with this recommendation as it imposes requirements on the grantees/contractors that are not contained in the mandatory provisions of Handbooks 3 and 13 nor in the standard contract provisions. It also imposes a burden on the Mission when the time could be more productively spent in monitoring. The Mission is not aware of any policy or procedures that require this reconciliation to the MACS records. And, for reasons that were discussed in our response to Recommendation 2.1, an accurate inventory listing might very well not agree with MACS. Furthermore, the methodology that was used in comparing MACS records to recipient/contractor records was faulty. The auditors used an average exchange rate to determine the value of inventories/records stated in shillings while the MACS system uses the exchange rate on the day the transaction is processed. While we agree that there is a Mission responsibility for oversight and monitoring of the contractor's policies and procedures, we find it not productive to duplicate contractors records nor reconcile exchange rate differences that really do not exist. Comments on specific projects cited in the report follow:

Project 615-0221, Agricultural Management: The differences between the contractor and the Mission's records are due to the fact that commodities procured by the contractor (Price Waterhouse) were charged to the technical assistance component in MACS whereas the commodities procured by USAID/Kenya for other grantees/contractors were charged to the Commodity component. Therefore, the comparison of the two data bases was erroneous.

Project 615-0229, National Agricultural Research: The differences arise because of the same circumstances as noted in Project 615-0221 above.

With regard to the missing laboratory equipment in the research stations, the Mission has instructed the MIAC to liaise with the Director of the Kenya Agricultural Research Institute (KARI) to take the necessary steps to ascertain the whereabouts of the equipment. We will advise you of the results.

Project: 615-0238, Private Enterprise Development: The commodities purchased for Kenya Association of Manufacturers (KAM) were components for a computer system which KAM is using. See letter attached.

The Private Enterprise Office (PEO) has the $7,285 voucher and the PIL and pro forma invoice which matches the $13,084 voucher which account for the $20,369 in commodities purchased for the Investment Promotion Center (IPC).

The amount in question in the Advisors component was for the computer hardware and software purchased for a former advisor and currently being used by her successor in the PEO.

The International Executive Service Corps (IESC) has been requested to submit an accurate inventory for A.I.D.-funded commodities to USAID/Kenya as required in Handbook 13.

The Private Enterprise Office will obtain a commodity listing when the close-out audit of the Kenya National Chamber of Commerce and Industry (KNCCI) is completed.

The Kenya Management Assistance Program (KMAP) is undergoing a close-out audit. Once the audit is completed, they will forward a copy of the completed inventory. The furniture, a franking machine, and a motor vehicle were inadvertently not included in the inventory given to the auditors in spite of being marked with USAID emblems.

Project 615-0240.01, Resource Management for Rural Development: This is a host country contract with Harvard University. The contract expired June 30, 1991. The Mission, together with the GOK, is in the process of initiating close-out procedures which will include turning over the project NXP to the GOK. The Mission will ensure that Harvard complies with contract requirements with regard to an inventory of the property.

Project: 615-0240.02, Micro Computerization: The discrepancy identified arises from miscommunications between USAID (PRG and RIG/A) and the contractor. The inventory originally provided by Thunder & Associates, Inc. (TAI) related only to their present contract and did not include the commodities they procured during the prior two contracts (now closed) under the project.

Thunder's July 20 letter (attached) included three attachments. Attachment 1 is the inventory initially provided to RIG/A; it reflects only the commodities procured under TAI's third and current contract and it adds up to the $100,080 indicated as verifiable by RIG/A. Attachments 2 and 3, which do not include values, represent the commodities procured under the two prior contracts. The Mission will review to ensure that the contractor was in compliance with all provisions of the host country contract with regard to reporting on the non-expendable property.

Project 615-0245, Kenya Health Care Financing: The unreconciled difference of $21,385 between the Mission's accounting ($82,386) and the contractors ($103,771) records for disbursements for commodities is a result of the auditors using an average exchange rate as discussed above. Any reference to this project should be deleted from the final report.

Project 615-0251, Kenya Contraceptive Social Marketing: The unreconciled difference of $24,753 is also a result of the auditors using the average exchange rate. Any reference to this project should be deleted from the final report. As per the letter from Population Services International (copy attached), the inventory list inadvertently included a calculator and a fax machine. The fax machine was sold to Continental Industry Ltd. and the calculator was written off after it was reported stolen.

Project 615-0253, Park Rehabilitation (PRAM): The Mission disagrees with the assumption that we relied on the GOK's inventory control system to account for the receipt of commodities. The Kenya Wildlife Service (KWS) is an autonomous parastatal body with its own management control systems which were designed by Price Waterhouse. The Mission had reviewed their systems and found them to be adequate. The Mission compared the invoices submitted for the rehabilitation of equipment and found that the shilling amount reimbursed was in agreement with KWS records. The $198,378 discrepancy mentioned in the audit report was entirely due to the auditors use of an average exchange rate rather than the actual rate on the date the invoice was processed. Any reference to this project should be deleted from the final report.

Any reference to discrepancies caused by the auditors use of an average exchange rate should be deleted from the final report. This recommendation should be re-written to reflect the information contained within, and in conformance with applicable policies, procedures and provisions contained in the Handbooks, rather than with the RIG interpretation of such requirements.

Recommendation No. 2.5 requests the Mission to reconcile discrepancies in USAID/Kenya shipping documents with the receiving records at the MSCU for 3,180,000 condoms valued at $171,938; 5,400 IUCD's valued at $8,559 and 825,800 vaginal foaming tablets (VFT's) valued at $88,694, and determine the allowability and quantities and amounts that cannot be reconciled.

Response: Project: 615-0232, Family Planning Services and Support: All the contraceptives purchased by the Mission are for the GOK national family planning program. Transportation of these contraceptives from the GOK main warehouse (MSCU) to various sub-depots and district warehouses is solely a GOK responsibility. In fact the GOK previously cleared these contraceptives on their own at the Mombasa port using the Government Clearing Agency. However, due to long clearing delays USAID in 1989 decided to contract with a private clearing and freight forwarding firm to clear and deliver the contraceptives shipments directly to the MSCU in Nairobi. This action has not only expedited the clearance process but also ensures that receipts of contraceptive shipments are recorded properly. In addition, through the USAID-funded Logistics Management Support Project, the Mission has dedicated space at the MSCU specifically for contraceptives. This space ensures that contraceptives are received, recorded and despatched in an orderly manner. The record keeping at MSCU has been computerized and reports of stock on hand and expiration dates of stock by lot number are available.

However, the Mission believes that other acceptable documentation may be made available at the MSCU in order to reconcile the discrepancies in USAID/Kenya shipping documents with the receiving records at the MSCU. Among these may be backup computerized records from the MSCU's central data management center (separate from Bin Card records), and actual clearing documents which may be kept in offices other than the MSCU, as for example, the Division of Family Health. USAID/Kenya will initiate further steps in cooperation with the Division of Family Health and the MSCU to determine the allowability of amounts that can be reconciled based on the additional data sources. We request that this recommendation be considered resolved.

Recommendation No. 2.6 requests the Mission to obtain from the GOK's MSCU an accounting for contraceptive issues of 6,028,000 condoms valued at $284,944; 47,600 IUCD's valued at $50,942 and 459,600 VFT's valued at $43,906 which could not be traced during the time of the audit, and determine the allowability of the quantities and the amounts that can not be reconciled.

Response: The Mission acknowledges the likelihood of record keeping laxity as observed by the A.I.D. Auditors in the 2 sub-depots and district facilities sampled. This problem was one among several which prompted USAID to initiate the Logistics Management Support Project, funded under the FPSS, in mid-1991. As of September, 1991, the USAID-funded Logistics Management Support Project is being systematically implemented in all sub-depots and district stores in the country and involves direct commodities delivery by a newly-created special unit within the MSCU coupled with frequent supervision of record keeping at receiving facilities by the Logistics Management Support Unit team dispatched from Ministry of Health headquarters, Division of Family Health. These measures have already greatly improved the GOK's auditable documentation so as to be consistent with USAID requirements in connection with receipt of USAID-funded contraceptives.

In noting the discrepancies, the Mission believes the audit report did not go far enough in describing the implications of this finding. Prima facie, the fact that the items were not logged-in at the receiving facility might suggest that they did not arrive as intended. However, MSCU issuances are in all cases based on a GOK S12 Requisition Form signed by an officer of the requesting facility whose signature is on file at the MSCU and routinely verified before issues are made. In addition, 6-7 other personnel are involved in checking that the issuance is correct. The staff person collecting the issue from MSCU is a staff member of the requesting facility. Although not foolproof, the Mission believes the GOK's procedures provide some degree of control in that if widespread diversion of commodities occurred, the large numbers of individuals involved in a single transaction would substantially increase the probability that such irregularity would be detected. The Mission believes that neither the observed record keeping laxity nor any other observable conditions necessarily suggested the intentional diversion of commodities away from the intended recipient facility. If the RIG/A agrees with this position, the Mission requests that the audit report so state.

Furthermore, it is the opinion of the Mission that identification of additional historical GOK records at 2 sub-depots and 15 district facilities are not possible at this time. In the absence of recordings that should have been made at the time of the receiving event, there is no other auditable source of data that might be found to verify the transactions. The Mission therefore does not view any attempts at reconstruction of historical GOK records or attempts to otherwise determine the allowability of the items in question, to be either feasible or cost-effective.

The Mission is unable to reconcile any of the discrepancies in record keeping noted in Recommendation 2.6, but since September, 1991 has taken appropriate steps to assist the GOK in improving its record keeping practices. Based on the foregoing, the Mission requests that Recommendation 2.6 be closed.

Recommendation No. 2.7 requests the Mission to determine the allowability of, and collect as appropriate, $53,340 paid for rehabilitation of road maintenance equipment at Tsavo East and Mount Elgon National Parks.

Response: The Mission disagrees with the findings and the conclusion upon which this recommendation is based. The following response has been obtained from KWS letter reference KWS/308/(224) of August 17, 1992 (copy attached).

1. Komatsu Motor Grader at Tsavo East

   (i) The machine broke down, and was subsequently grounded in 1987.

   (ii) An assessment report of the equipment was carried out in November 1990, by a USAID funded contractor (Mr. D. Griffiths).

   (iii) Pan African Equipment ferried the machine to their Nairobi workshop on a low loader on September 23, 1991.

   (iv) Repair of the equipment was completed in January 1992 and the machine returned to Tsavo East National Park.

   (v) The machine has been in use since then.

   The workshop manager for Tsavo East National Park by letter reference KWS/TE/1100(19) of August 20, 1992 (copy attached) has confirmed that the grader GK A 207 had indeed been repaired and the repair estimate of KShs. 1,141,875 had been approved by KWS.

2. Komatsu Motor Grader at Mount Elgon National Park.

KWS in letter reference KWS/308/(224) of August 17, 1992, states the following:

March 24, 1991 - Technicians from Pan African Equipment travelled to Mt. Elgon and inspected the equipment.

May 6, 1991 - Pan African Equipment travelled to Mt. Elgon and repaired the equipment.

August, 1991 - Pan African Equipment completed electrical repairs not done in May.

The warden for Mt. Elgon National Park in a letter reference KWS/ELG/1041(28) of August 18, 1992 (copy attached) asserts that the auditors must have obtained information from an unreliable source.

3. Komatsu Motor Grader at Tsavo West National Park.

KWS in letter reference KWS/308(224) of August 17, 1991 believes the auditors must have been referring to the wrong machine as a motor grader is not usually ferried with a low loader for short distances (within the park). The actual machine the Auditors could have been referring to is a crawler which was ferried to Nairobi for repair on September 19, 1991 and returned to Tsavo West on February 25, 1992. This machine therefore, has not been idle since September 1991.

KWS believes the auditors did not make a sufficient effort to cross check the correctness of their information.

In view of the above information, recommendation 2.7, and any references thereof, should be deleted upon issuance of the final audit report.

Recommendation No. 2.8 requests the Mission to report in the next FMFIA reporting cycle to the AA/AFR the internal control weaknesses associated with USAID/Kenya's commodity monitoring systems, if these weaknesses are not corrected.

Response: Mission concurs.

Action Taken: The Mission is reviewing the internal controls procedures that were in place during FY 1992 with a view to determining weaknesses which may be reported to AA/AFR. We request that this recommendation be resolved and closed upon issuance of the final audit report.

Recommendation No.3.1 requests the Mission to obtain from the contractors and grantees a complete and accurate accounting for the commodities disposed under Projects 615-0241 and 615-0220, reconcile the inventories to the disbursements made by USAID/Kenya and account for any differences.

Response: Project 615-0241 CORAT Child Survival and Family Planning Project ended on December 31, 1991. The final financial audit was completed in May, 1992, with a unqualified opinion from the CPA firm of Carr Stanyer Gitau. The final voucher is currently being processed by the Mission. Since project inception there has been no disposal of any commodities as per CORAT's letter dated September 28, 1992. The unreconciled difference of $65,041 is a result of the use of an average exchange rate rather that the actual exchange rate used when the voucher was processed. As title to and the property will remain with CORAT, we request that any reference to CORAT be deleted from the final report.

Project 615-0220, Rural Private Enterprise Project (RPE): World Education Incoporation, through their local affiliated NGO, the Kenya Rural Enterprise Program, is in the process of compiling a list of commodities for submission to the Mission. The Mission will ensure that the grantee complied with HB 13 provisions with respect to transfer and disposal of project non-expendable property.

The PEO will work with the Contracts Office to verify the disposal of the $27,610 of Deloitte Haskins and Sells commodities.

The PEO has received a list of commodities purchased under RPE by the banks and we are in the process of reviewing their list with our records to assure compliance with HB 3 provisions with respect to loan-funded non-expendable property.

Additionally, the RPE project is currently being audited. The Mission will ensure that required close-out procedures are followed, however, the Mission is unable to identify specific language in the mandatory standard provisions in A.I.D. Handbooks 3, 11, 13 and 14, for which the grantees/contractors are held accountable, which requires that their inventories be reconciled to the USAID/Kenya reports, nor, given the differing data bases, would it be productive.

Based on this explanation we request that this recommendation be re-written in compliance with applicable Handbook provisions and resolved upon issuance of the final audit report.

Recommendation No. 3.2 requests the Mission to establish and implement a system for monitoring commodity disposal to include the requirement that contractors and grantees take and submit to USAID/Kenya annual inventories of commodities procured under each project, reconcile inventories to the disbursements, account for any differences and take appropriate actions for the discrepancies.

Response: The Mission will include commodity disposal in the Mission Order now in clearance. However, the MO will be in compliance with current guidance/provision of contracts and will not hold grantees/contractors to requirements that are not now contained in standard provisions or mandatory clauses. If RIG/N wishes to change these provisions, i.e. require annual inventories from contractors for host country titled property, they should direct their recommendation to the Office of Procurement in A.I.D./W. We ask that this recommendation be deleted as it is covered in our suggested re-write of Recommendation 2.1 above.

Recommendation No. 3.3 requests the Mission to report in the next FMFIA reporting cycle to the AA/AFR the internal control weaknesses associated with USAID/Kenya's commodity disposal monitoring systems, if these weaknesses are not corrected.

Response: This recommendation should be combined with Recommendation 2.8 and deleted from the final report.

If you wish to discuss the contents of this memo before you issue a final report, please advise.

Drafted: PH:GKathurima/MHoward/GLeinen
PEO:ABrewer
PRJ:MSmith
AGR:DMcCarthy
PRG:EMartella
CONT:JOndigi
CONT:ECAdams

Clearance: PH:CJJohnson/GNewton (draft)
PEO:SBaker (draft)
AGR:MMullei/JKigathi (draft)
PRG:KToh (draft)
REDSO/RCMO:BVHorn (substance)

Attachments

1. Egerton University Letter dated September 23, 1992
2. Brewer/Ondigi Memo w/attachments Dated September 30, 1992
3. Brewer/Ondigi Memo w/attachments Dated October 1, 1992
4. TAI Letter w/attachments dated Septeber 20, 1992
5. PSI Letter dated September 28, 1992
6. KWS Letter Dated August 17, 1992
7. KWS Letter Dated August 28, 1992
8. CORAT Letter dated September 28, 1992

OIG Comment

These attachments were considered in preparing the final report, but have not been included as part of this report.

Mr. Everette B. Orr
Regional Inspector General, Audit
P.O. Box 30261
Nairobi, Kenya

22 OCT 1992

Dear Mr. Orr:

This is in regard to the audit which your staff completed in July 1992 on "USAID/Kenya Management of Commodities."

I was away from post on Home Leave during much of the time the audit was performed. However, I understand the Acting Director, Roger Simmons, asked the most knowledgeable members of our staff (i.e., the relevant project managers and the staff of the Office of the Controller) to make available to you all records in our possession for the purpose of this audit. Based on the representations made by those individuals to me, I believe that those records are accurate and complete, and that they constitute a fair representation as to the status of the management of project commodities.

Specifically, I confirm that:

A. USAID/Kenya is responsible for the monitoring and management of project commodities, for the internal control system, for compliance with applicable rules and AID regulations, and for the completeness and accuracy of accounting and management information;

B. To the best of my knowledge and belief, USAID/Kenya has made available to you all the financial and management information related to the audit objectives;

C. The draft audit report states that USAID/Kenya should report problems with the receipt, storage, use and disposal of commodities as material internal control weaknesses. I reserve judgment on these RIG/Nairobi assertions until I have had an opportunity to fully review and comment on the final audit report. With the exception of these possible weaknesses, to the best of my knowledge and belief, USAID/Kenya is not aware of any known irregularities which we consider material involving Mission management and employees with internal control responsibilities; to the best of my knowledge and believe, USAID/Kenya is not aware of any known irregularities which we consider material involving other organizations which could affect the management of project commodities, and has made available to you any relevant communications from other organizations concerning noncompliance with or deficiencies in the management of project commodities;

D. To the best of my knowledge and belief, USAID/Kenya is not aware of any material instances relevant to project commodity management where management information has not been properly and accurately recorded or reported, other than the findings in the audit report, or where financial information has not been properly and accurately recorded and reported;

E. The draft audit report states that USAID/Kenya is not in compliance with A.I.D. policies and procedures with regard to implementation of controls to monitor the receipt, storage, use and disposal of commodities. I reserve judgment on these RIG/Nairobi assertions until I have had an opportunity to fully review and comment on the final audit report. With the exception of these possible instances of non-compliance, and to the best of my knowledge and belief as a layman, and not as a lawyer, USAID/Kenya is not aware of other instances of material non-compliance with A.I.D. policies and procedures or violations of U.S. laws and regulations;

F. To the best of my knowledge and belief, USAID/Kenya has complied, except in those instances noted in the audit report, with all aspects of contractual agreements that would materially affect the management of project commodities; and

G. Following our review of your draft audit report and further consultation with my staff, I know of no other facts as of the date of this letter (other than those expressed in our comments on the draft report) which, to the best of my knowledge and belief, would materially alter the conclusions reached in the draft report.

I request that this Representation Letter be included as a part of the official USAID/Kenya comments on the draft report and that it be published therewith as an annex to the report.

Sincerely,

John R. Westley,
Mission Director

Summary of Commodity Obligations and Expenditures
for Projects Audited

Project Number	Project Description	Commodity Obligations	Commodity Expenditures
1. 615-0220	Rural Private Enterprise	$608,763	$608,763
2. 615-0232	Family Planning Services and Support	4,798,014	3,887,159
3. 615-0238	Private Enterprise Development	450,606	407,249
4. 615-0241	CORAT Child Survival and Family Planning	349,500	298,810
5. 615-0245	Kenya Health Care Financing	727,917	82,386
6. 615-0251	Contraceptives Social Market	97,595	83,655
7. 615-0221	Agricultural Management	104,000	98,296
8. 615-0229	National Agricultural Research	2,288,725	2,172,600
9. 615-0239	Institutional Development for Agricultural Training	1,343,370	1,333,267

Summary of Commodity Obligations and Expenditures for Projects Audited

Project Number	Project Description	Commodity Obligations	Commodity Expenditures
10. 615-0240	Structural Adjustment Assistance Program	720,830	657,400
11. 615-0253	Park Rehabilitation and Management	1,120,000	291,785
	Total	12,609,320	9,921,370

Source: MACS Report No. PO6B as of January 31,1992.

Appendix IV

Report Distribution

American Ambassador to Kenya	1
Administrator, AID	2
Director, USAID/Kenya	5
AA/AFR	1
AFR/EA/KR	1
AFR/CONT	1
XA/PR	1
LEG	1
GC	1
AA/OPS	1
AA/FA	1
FA/FM/FPS	2
FA/FM	1
AA/R&D	1
POL/CDIE/DI	1
FA/MCS	2
REDSO/ESA	1
REDSO/RFMC	1
REDSO/Library	1
IG	1
AIG/A	1
D/AIG/A	1
IG/A/PPO	3
IG/LC	1
IG/RM	12
AIG/I	1
RIG/I/N	1
IG/A/PSA	1
IG/A/FA	1
RIG/A/C	1
RIG/A/D	1
RAO/M	1
RIG/A/S	1
RIG/A/T	1
RIG/A/EUR/W	1
RIG/A/V	1