

PD-ABF-245
80832

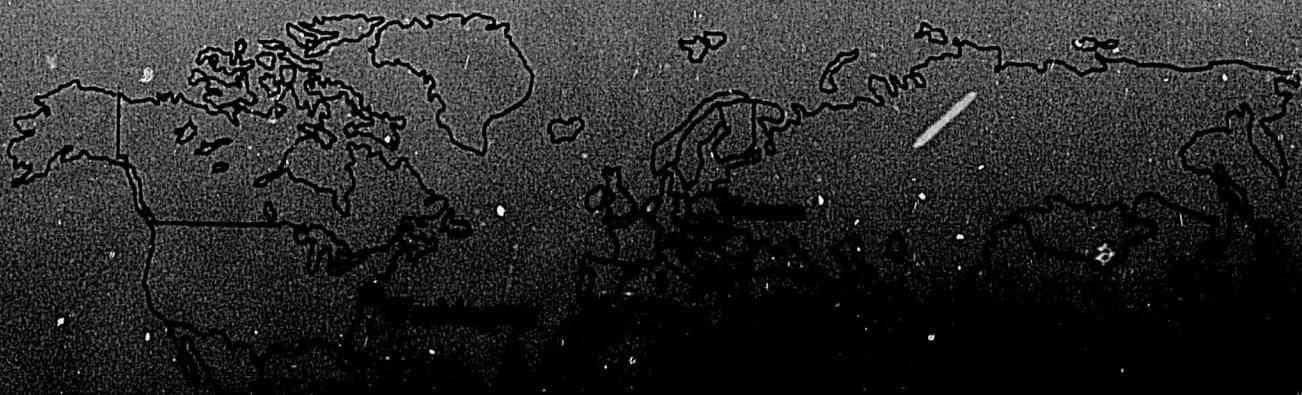
Regional Inspector General for Audit
Tegucigalpa, Honduras

**Award Survey of the
Administration for Machinery and Equipment's
Capability to Manage Activities
Under USAID/El Salvador's
Public Services Improvement Project**

B810

Audit Report No. 1-519-93-06-N
January 19, 1993

2051



U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

AGENCY FOR INTERNATIONAL DEVELOPMENT

U. S. MAILING ADDRESS:
RIG/T
APO. MIAMI 34022

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

TELEPHONES:
32-9987 - 32-3120
FAX No. (504) 31-4465

January 19, 1993

MEMORANDUM

TO: D/USAID/El Salvador, John Sanbrailo

FROM: RIG/A/T, Lou Mundy 

SUBJECT: Award Survey of the Administration for Machinery and Equipment's Capability To Manage Activities Under USAID/El Salvador's Public Services Improvement Project

This report presents the results of an award survey of the Administration for Machinery and Equipment's (the Administration's) capability to manage activities under the Public Services Improvement Project (USAID/El Salvador Project No. 519-0320). The firm of Arthur Andersen & Co. prepared the report dated November 30, 1992.

The approved budget for the Public Services Improvement Project (Project) provides for \$75 million in A.I.D. grant funds and \$60 million in Government of El Salvador counterpart contributions. The Administration, a Directorate of the Government of El Salvador's Ministry of Public Works (Ministry), is responsible for providing maintenance and repair services for the Ministry's machinery and equipment acquired with A.I.D. funds under the Project. The Ministry is currently budgeted to receive \$4.3 million in A.I.D. funding during the life of the Project to finance both the activities of the Administration and the Ministry's rural road deferred maintenance and repair program.

The objectives of the award survey were to report on the Administration's: (1) managerial and financial capability to manage Project activities, (2) internal control structure with respect to Project operations, and (3) compliance with terms of the agreement and applicable laws and regulations. The scope of the award survey included an examination of Administration activities and transactions to the extent considered necessary to issue a report thereon.

The auditors concluded that, except for: (1) certain administrative deficiencies noted in the central maintenance and repair shop, (2) a lack of approval and authorization by the Ministry of its draft internal work regulations, and (3) a lack of a well defined conflict of interest policy, the Administration has sufficient managerial capability to manage the activities of the Project. Also, the auditors concluded that the Administration has the financial capability to carry out Project activities.

The auditors identified three reportable conditions in the Administration's internal control structure related to Project activities. Two of these conditions were reported as material weaknesses. Specifically, these weaknesses disclosed that the Administration needs to establish: (1) employee responsibility cards for the control, custody, and safekeeping of goods acquired, and (2) a policy regarding the storage and subsequent disposal of obsolete materials and spare parts.

With respect to the Administration's compliance with agreement terms and applicable laws and regulations, the auditors found two material instances of noncompliance. Specifically, the Administration has not: (1) maintained separate records to account for Project commodities acquired with A.I.D. funds, and (2) included all information required by the Project Agreement in its Project evaluation reports.

The auditors also performed a follow-up on recommendations made to the Administration in two separate evaluations performed on its host country contracting and commodities management system. As the Administration had not taken corrective actions to implement all recommendations we suggest USAID/El Salvador review the open recommendations (pages 8 to 10 of the Arthur Andersen & Co. report) and ensure the Administration corrects the deficiencies noted.

We are including the following recommendation in the Office of the Inspector General's audit recommendation follow up system:

Recommendation No. 1

We recommend that USAID/El Salvador obtain evidence that the Administration for Machinery and Equipment has:

- 1.1 established a plan to provide for additional work space to attend to its present and future repairs and maintenance demands, to segregate work space based on the type of repair and maintenance being performed, and to designate an area for the storage of obsolete materials and spare parts;**

- 1.2 established a policy for the disposal of obsolete material and spare parts;**
- 1.3 obtained the Ministry of Public Works' approval and authorization of its draft internal work regulations;**
- 1.4 established procedures requiring that: (a) key officers complete a conflict of interest disclosure questionnaire; (b) employee responsibility cards be utilized for the control, custody, and safekeeping of goods acquired under the Project; (c) separate records be maintained to account for Project commodities acquired with A.I.D. funds; (d) Project evaluation reports be prepared in accordance with Article 5, Section 5.1 of the Project Agreement and Project Implementation Letter No. 3.**

Recommendation No. 1 can be resolved when the Mission presents an acceptable firm plan of action to correct the reported deficiencies and can be closed when the Mission presents acceptable evidence that the required plans, policies, or procedures have been established.

The report was discussed with representatives from the Administration who expressed general agreement with its contents. Management's comments are included in Annex I to the Arthur Andersen & Co. report.

This final report is being transmitted to you for your action. Please advise this office within 30 days of actions planned or taken to resolve and close the recommendations.

**Regional Inspector General for Audit
Tegucigalpa, Honduras**

**Award Survey of the
Administration for Machinery and Equipment's
Capability to Manage Activities
Under USAID/El Salvador's
Public Services Improvement Project**

**Audit Report No. 1-519-93-06-N
January 19, 1993**

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

AS OF JUNE 23, 1992

TABLE OF CONTENTS

	<u>Page No.</u>
I. TRANSMITTAL LETTER AND SUMMARY	
Background	3
Survey objectives and scope	5
Results of survey	7
Management comments	10
II. MANAGEMENT/FINANCIAL CAPABILITY	
Independent auditor's report- management capability	11
Findings	12
Independent auditor's report- financial capability	15
III. INTERNAL CONTROL STRUCTURE	
Independent auditor's report	16
Findings	18
IV. COMPLIANCE WITH AGREEMENT TERMS AND APPLICABLE LAWS AND REGULATIONS	
Independent auditor's report	21
Findings	22
V. FOLLOW UP TO PREVIOUS YEAR'S CONSULTING RECOMMENDATIONS	
Independent auditor's report	24
Findings	25
VI. LIST OF REPORT RECOMMENDATIONS	28

ANNEX I - MANAGEMENT COMMENTS'

ARTHUR ANDERSEN & Co.

Edificio Centro Gerencial Las Margaritas
Diagonal 6, 10 - 65 Zona 10, 5o. Nivel
P.B.X.: 327939, FAXES: 316914, 316916
Guatemala, C.A

November 30, 1992

Mr. Lou Mundy
Regional Inspector General for Audit
U.S. Agency for International Development
Tegucigalpa, Honduras, C. A.

Dear Mr. Mundy:

This report presents the results of our award survey of the ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME) in the management of the Public Services Improvement Project, USAID/El Salvador Project 519-0320, as of June 23, 1992.

BACKGROUND

On August 30, 1989, USAID/El Salvador approved The Public Services Improvement Project, USAID/El Salvador Project No.519-0320, which provided the amount of US\$ 75,000,000 in grant funds to the Government of El Salvador (GOES) acting through the Ministry of Planning and Coordination for Social and Economic Development. It was agreed that the Government of El Salvador would provide a counterpart contribution of no less than US\$ 60,000,000, which might include Economic Support Funds, and PL 480 generated local currency. The Project Assistance Completion Date is estimated to be September 30, 1994 .

The purpose of the project is to:

1. Support restoration of services interrupted and facilities damaged or destroyed as a result of insurgent activity or natural disaster.
2. Assist in performance of deferred maintenance and repair of indirect damages to primary rural roads, and maintenance of A.I.D. financed construction equipment for road maintenance.
3. Construct and repair small rural water systems and sanitary facilities, and provide health education in rural communities, and
4. Provide technical assistance in project management, enhance the implementing institutions' capability to perform their functions (including policy analysis), sustain project activities, and perform evaluations and audits.

The project has the following four major components:

1. Public services restoration

This component provides the financial support, principally foreign exchange, needed by the public services agencies to repair direct and indirect damages caused by guerrilla actions and, if required, by natural disasters. This component continues restoration assistance provided under the Public Services Restoration Project, USAID/EL SALVADOR Project No. 519-0279. Implementing entities are: Lempa River Hydroelectric Executive Commission (CEL), Ministry of Public Works (MOP), Autonomous Executive Port Commission (CEPA), and National Water and Sewer Administration (ANDA).

Project funds will be used to finance imported commodities, typical of which are electrical distribution and transmission equipment and material; electric motors and switch gear; pumps and valves; navigation and communication equipment; light equipment; repair parts for any of the above and diesel locomotives; and bridge materials. In addition to the importation of electrical machinery and spare parts for the public services agencies, this component will fund helicopter services for use primarily by CEL in the repair of electrical transmission and distribution lines and towers.

2. Secondary, Tertiary, and Lower Class Rural Road Deferred Maintenance and Repair

This component will finance a major effort to repair deteriorated rural roads together with Institutional strengthening in component (4) and will supplement the capability of the MOP to plan and manage road maintenance. The Administration for Machinery and Equipment (AME) will receive support to maintain A.I.D. purchased equipment. The implementing entity is the MOP through its divisions for equipment AME, and for roads, the management for the project in the division of roads.

3. Potable Water Supply, Sanitation and Health

This component provides support to restore or install water supply and sanitation systems, in association with community organization and health education activities, in small rural communities. The implementing entities are the Ministry of Health (MSPAS) and ANDA.

4. Institution Strengthening, Project Support, Monitoring and Evaluation

This component finances technical assistance, training and commodities to enhance project implementing entity capability, to promote policy analysis and reform, and to perform evaluations and audits. A.I.D. will contract directly for technical assistance on behalf of and for the Government of El Salvador (GOES) utilizing project funds and customary competitive procedures.

History of the Administration for Machinery and Equipment (AME)

The Administration for Machinery and Equipment (AME) is a Directorate of the Ministry of Public Works of the Government of El Salvador. It was created on July 1, 1987, and its principal function is to provide maintenance and repair services for the Ministry's machinery and equipment bought with A.I.D. funds under component II of the Public Services Improvement Project, USAID/El Salvador Project No. 519-0320.

At present, AME has four maintenance and repair shops, two in the central region (San Salvador), one in the western region (Santa Ana) and one which does not have adequate facilities in the eastern region (San Miguel).

SURVEY OBJECTIVES AND SCOPE

The objectives of our award survey of AME were to determine whether:

1. AME has sufficient management and financial capabilities and span of control to administer the components under its responsibility for the Public Services Improvement Project, considering its current and future projects workload, staffing levels and past performance in developing other USAID/El Salvador projects;
2. AME's internal control structure including the control environment, accounting system and control procedures (specifically related to the procurement and accounting for commodities) is adequate to manage the project's operations;
3. AME is complying with agreement terms, project implementation letters, and applicable laws and regulations.

The scope of our survey included the following steps:

A. Preliminary steps

We reviewed the following documents and applied criteria to the different items tested in performing our work.

1. The statement of work
2. The "Projects Papers"
3. Grant Agreement for the Public Services Improvement Project, USAID/El Salvador Project No. 519-0320 including amendments.
4. The budgets, project implementation letters (PILs), and written procedures approved by USAID/El Salvador to manage the projects.
5. Office of Management and Budget (OMB) Circular A-122 "Cost Principles for Nonprofit Organizations".

6. A.I.D. Handbook 11, Country Contracting, specifically Chapter 4, Cost Principles.
7. A.I.D Handbook 15, Commodities, specifically Chapter 10, Commodity Arrival and Disposition.
8. DEVRES INC. Report, dated August 23, 1991.
9. RIG/A/T Commodity Audit Report, dated May, 1992.
10. USAID/El Salvador Mission Order Manual (MOM), Sub-Chapter 7030, Monitoring of Receipt and End-Use of Program and Project Commodities.

B. Management and financial capability

In assessing the management and financial capability of AME, we evaluated:

1. The actual organization chart and the proposed allocation of responsibilities for project activities.
2. The staffing levels of capacity in terms of expertise and experience managing similar USAID/El Salvador or other projects.
3. The actual and proposed workload of key personnel to be in charge of project activities.
4. AME's policies regarding administration of personnel, administration of funds and assets, and other related policies such as segregation of duties, conflict of interests.
5. The accuracy and timeliness of submission of reports and other project documentation, and past performance in terms of attainment of project goals.
6. Whether AME has adequate systems to plan, procure, account for and use commodities.

C. Internal control structure

We evaluated the actual internal control structure (control environment, accounting system and control procedures) in accordance with generally accepted auditing standards and the U.S. Comptroller General's "Government Auditing Standards". The internal controls evaluated included, but were not limited, to the adequacy of the accounting and information systems (specifically related to procurement and accounting for commodities), procurement procedures and practices, fixed equipment/supplies controls, controls on counterpart contributions, and controls to assure that charges to the project are proper and supported. Also we evaluated: whether AME has established policies for planning and evaluating project activities and accomplishments, the input and output procedures for the electronic data processing (EDP) system, and past audit reports to determine whether AME has implemented the recommendations.

D. Compliance with agreement terms and applicable laws and regulations

Our work in this area consisted of monitoring whether AME has complied with agreement terms, project implementation letters, and applicable laws and regulations, and assessing possible risks for the project resulting from noncompliance.

E. Follow up to previous year's consulting recommendations

We performed the follow up to findings and recommendations included in the following documents: (1) Report on Host Country Contracting Assessment performed by Louis Berger International Inc. on May, 1991 (Contract No. 519-0320-C-00-01103-00) and (2) Report on Evaluation of the Commodity Management System performed by DEVRES INC. on August, 1991 (Contract No. 519-0349-C-00-1111).

Such follow up was made of findings and recommendations which could have a material effect on our evaluation, to determine if AME has taken adequate corrective measures.

RESULTS OF SURVEY

In this section we present a summary of the survey results, briefly describing the most significant issues and problems found.

1. Management and Financial Capabilities

AME has sufficient management and financial capability and span of control to adequately manage the activities of the Project. However, our evaluation in this area revealed the following deficiencies:

- The central repairs and maintenance workshop has the following administrative deficiencies:
 - . It does not have sufficient space to attend to present and future demands for repairs and maintenance.
 - . There is obsolete and unusable machinery and equipment taking up space which could be used for maintenance of equipment in use. In addition, AME's action plan for 1992 does not contain the measures to be taken to dispose them.
 - . There is no physical segregation by type of repairs and maintenance, for example: shop, for heavy vehicles, for light vehicles, electricity, welding, lubrication and greasing, etc.
- The internal work regulations applicable to the offices and departments of the Ministry of Public Works have not been authorized by the Directorate for Planning.

- Principal officers do not fill out a disclosure form to show that they are not involved in situations giving rise to conflict of interests for AME.

2. Internal Control Structure

AME'S internal control structure is adequate, although we detected reportable conditions which should be corrected to strengthen controls for project purposes.

- Lack of responsibility cards per employee
- There are obsolete materials and spare parts in the central warehouse, which have not been written off and which are taking up space necessary for usable goods.
- There is no document for control of materials and spare parts transferred from the central warehouse to the regional warehouses.

3. Compliance with agreement terms and applicable laws and regulations

The result of our evaluation indicates that AME has complied with the terms of the agreement and with applicable laws and regulations, except for the following:

- There are no separate auxiliary records for goods (machinery, equipment, spares and supplies) bought with project funds and no Equipment/Supplies Accountability Statement is prepared.
- Project evaluation reports prepared by AME do not include problems detected and possible solutions.

With respect to items not tested, nothing came to our attention that caused us to believe that AME had not complied in all material respects with those provisions.

4. Follow up to previous year's consulting recommendations

The result of our evaluation to follow up of recommendations of consultancies carried out the year before indicates that AME has implemented the recommendations, except for the following.

- a) Recommendations of Louis Berger Report on Host Country Contracting Assessment.
- Maintain updated records of inventories and other equipment acquired under the project. These records should be reconciled on a monthly basis with the general ledger and periodically with physical inventories in the warehouse. (Recommendation No. 4)

- Require that the Evaluation Committee prepare a table to compare the technical specifications for each item required with those proposed by the vendors and assign an expert/technician to review bid compliance with technical specifications. (Recommendation No. 6)
- Request and purchase commodities according to the annual plan and set limits for warehouse stock. The warehouse should report on a monthly basis which commodities are below the minimum. (Recommendation No. 8)
- The minutes from the Technical and Evaluation Committees, and correspondence with A.I.D. and vendors should be signed by the responsible AME authorities, and only these documents should support the contract decisions. (Recommendation No. 9)
- Update list of vendors as follows: (Recommendation No. 10)
 - . Prepare prequalification questionnaires and advertise their availability in the Commerce Business Daily and local newspapers.
 - . Evaluate the answer from the vendors to questionnaires.
 - . Prepare a document of the acceptable vendors; this document should be signed by the management of AME and by USAID.
 - . The addition of any supplier to the list should be based on an evaluation of the prequalification questionnaire filled out by the requesting vendor and approved in writing by AME and USAID.
 - . The IFB should be provided to prequalified vendors only.

b) Recommendations of DEVRES, INC. Report on the
Evaluation of Commodity Administration
System

- Institute procedures for the follow up of damages and shortages claims as AME does not have such procedures right now. (Recommendation No. 3)
- Establish procedures for identifying and returning incorrect parts as such procedures do not currently exist for returning incorrectly ordered spare parts. (Recommendation No. 4)
- Include funding source information in inventory records of the commodities acquired under Project No. 519-0279 since current inventory records for spare parts do not include this information. (Recommendation No. 5)

- Dispose of unserviceable and surplus equipment and spares. (Recommendation No. 8)
- Provide maintenance manuals, currently not available for much of the existing equipment. (Recommendation No. 9)

MANAGEMENT COMMENTS

The draft of this report was discussed with representatives from AME and USAID/El Salvador, who, in general, agreed with the report. Their comments have been considered in the preparation of this report.

The entire text of AME's Management Comments is included as Annex I to this report.

Arthur Andersen & Co

ARTHUR ANDERSEN & Co.

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

REPORT ON MANAGEMENT CAPABILITY

INDEPENDENT AUDITOR'S REPORT

We have performed an evaluation of AME's management capability for the administration of activities assigned to it under the PUBLIC SERVICES IMPROVEMENT PROJECT, USAID/EL SALVADOR PROJECT No. 519-0320. Our evaluation included those areas we considered relevant to the criteria established by USAID/EL SALVADOR as set forth in the statement of work for this survey.

Except as discussed in the next paragraph, we conducted our survey in accordance with generally accepted auditing standards and the Government Auditing Standards issued by the Comptroller General of the United States (1988 revision).

We did not have an external quality control review by an unaffiliated audit organization as required by paragraph 46 of chapter 3 of Government Auditing Standards since no such quality review program is offered by professional organizations in Guatemala. We believe that the effect of this departure from the financial audit requirements of Government Auditing Standards is not material because we participate in the ARTHUR ANDERSEN & Co. worldwide internal quality control program which requires the ARTHUR ANDERSEN-GUATEMALA office to be subjected, every three years, to a quality control review by partners and managers from other ARTHUR ANDERSEN & Co. offices.

Based on our evaluation and understanding of the criteria included in the statement of work referred to in the preceding paragraph, we believe that AME has sufficient capability to manage the PUBLIC SERVICES IMPROVEMENT PROJECT, USAID/EL SALVADOR PROJECT No. 519-0320, except for what are described under findings No. 1 to 3 in the following pages.

This report is intended for the use of the ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME) and the U.S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter public record.

Arthur Andersen & Co.

June 23, 1992

11

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

REPORT ON MANAGEMENT CAPABILITY

FINDINGS

1. Administrative deficiencies in central
maintenance and repairs shop

Condition

The central repairs and maintenance workshop has the following administrative deficiencies:

- It does not have sufficient space to attend to present and future demands, for repairs and maintenance.
- There is obsolete and unusable machinery and equipment taking up space which could be used for maintenance of equipment in use. In addition, AME's action plan for 1992 does not indicate measures to be taken to dispose of them.
- There is no physical segregation by type of repairs and maintenance: for example: shop, for heavy vehicles, for light vehicles, electricity, welding, lubrication and greasing, and others.

Criteria

AME's central workshop should have sufficient capacity to attend to present and future demands for maintenance and be structured so as to provide more efficient service. In addition, the shop should be used to attend only to usable and repairable equipment. Also, under Section II.B 1 (b) of implementation letter No. 3 of the agreement, the AME action plan should include measures to dispose of unusable equipment.

Cause

Lack of funds to expand the central workshop and reorganize it by specific areas. AME did not receive a copy of implementation letter No. 3 and was therefore unaware of the requirement. Moreover, the physical and accounting release of unusable equipment is very slow as it must first be authorized by the court of accounts.

Effect

The objectives of the project may not be attained if there is not sufficient equipment due to deferment of maintenance and repairs. In addition unusable machinery and equipment occupy space which might be better taken up by usable goods.

Recommendation

AME should apply for additional resources and allocate them to expansion of the central workshop and to create specific work areas. In addition, AME should take measures to dispose of obsolete and unusable equipment and include these units annual action plan. Also, AME should speed up application procedures before the Court of Accounts to release these goods both physically and from the accounts.

2. Lack of approval of internal work regulations

Condition

The internal work regulations applicable to the offices and departments of the Ministry of Public Works, have not been authorized by the Directorate for Planning.

Criteria

Sound administrative practices require that labor relations between employer and employee be governed by work regulations.

Cause

The Ministry of Public Works (MOP) has not taken official steps with the Directorate for Planning for the authorization of these regulations.

Effect

Employees can carry out action prejudicial to the entity and claim lack of knowledge of norms governing labor relations.

Recommendation

AME should request the Ministry of Public Works (MOP) to speed up steps for authorization of the draft regulations and put them into effect.

3. Lack of disclosure questionnaire on conflicts of interest

Condition

The principal AME officers do not periodically confirm in writing that they are not involved in situations likely to cause conflicts of interest.

Criteria

Sound administrative practices require that officers state in writing that they are not involved in situations giving rise to conflicts of interest.

Cause

Although conflict of interest policy is defined in various documents (for example, work contract and Ministry of public Works Supplies Law), there is no preprinted questionnaire to be completed periodically by the principal officers.

Effect

Employees or officers may carry out acts representing conflict of interest because they are not aware of policy or may believe that there are no prohibitions in this regard.

Recommendation

AME should require its officers to confirm in writing that they are not involved in situations likely to give rise to conflicts of interest. AME should design a printed questionnaire for the purpose and see to it that it is completed at least once a year.

ARTHUR ANDERSEN & Co.

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

REPORT ON FINANCIAL CAPABILITY

INDEPENDENT AUDITOR'S REPORT

We have performed an evaluation of AME's financial capability to manage the activities assigned to it under the PUBLIC SERVICES IMPROVEMENT PROJECT, USAID/EL SALVADOR PROJECT No. 519-0320.

Except for not conducting an external control review by an unaffiliated audit organization as described in our report on Management Capability, our evaluation was performed pursuant to USAID/EL SALVADOR's statement of work for the above mentioned project and in accordance with the United States Comptroller General's "Government Auditing Standards" (1988 Revision). Our work included, to the extent considered by us necessary to meet stated objectives, a review of both audited and unaudited financial information.

Based on our evaluation, as described above, we believe that AME has the financial capability required to execute the PUBLIC SERVICES IMPROVEMENT PROJECT, USAID/EL SALVADOR PROJECT No. 519-0320, especially since it will receive imported commodities for the project's needs, as provided for by the terms of the grant agreement.

This report is intended solely for the use of the ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME) and the US Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter of public record.

Arthur Andersen & Co.

June 23, 1992

15

ARTHUR ANDERSEN & Co.

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

REPORT ON INTERNAL CONTROL STRUCTURE

INDEPENDENT AUDITOR'S REPORT

We have performed an evaluation of AME's management capability for the administration of the activities assigned to it under the PUBLIC SERVICES IMPROVEMENT PROJECT, USAID/EL SALVADOR PROJECT No. 519-0320.

As part of our evaluation, we made a study of those internal accounting control and administrative control procedures of AME that we considered relevant to the criteria established in the statement of work for the award survey requested by USAID/EL SALVADOR, for the purpose of expressing our opinion of the management capability for the administration of the project and not to provide assurance on the internal control structure.

The management of AME is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but no absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following economical cycles: financial information, purchases, treasury and conversion (assets and inventories).

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

We noted certain matters involving the internal control structure and its operations that we considered to be reportable conditions under standards established by the American Institute of Certified Public Accountants.

Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

Our study of the AME's internal control structure related to Project activities disclosed the reportable conditions, described as findings No. 1 to 3 on the following pages of this report.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe that findings No. 1 and 2 in the following pages, are material weaknesses.

This report is intended for the use of the ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME) and the U.S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter public record.

Arthur Andersen & Co

June 23, 1992

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

INTERNAL CONTROL STRUCTURE

FINDINGS

1. Lack of responsibility cards per employee

Condition

AME does not use responsibility cards per employee for the control, custody and safekeeping of goods acquired with project funds.

Criteria

As a sound internal control measure, it is necessary to have controls to make it possible to define responsibilities for the proper use and custody of goods acquired.

Cause

There is a lack of written requirements for the specific control per employee, of the commodities acquired by project funds.

Effect

It would not be possible to lay responsibility on employees having in their charge certain equipment which suffers unjustified deterioration or loss. This leads to losses for the project and project objectives are not attained.

Recommendation

AME should prepare of responsibility cards per employee for the control of goods acquired, and which should contain as a minimum:

- Equipment control code, in running order
- Place and date of delivery
- Name of employee receiving equipment
- Description of equipment delivered
- Location and/or destination of equipment
- Signature of employee to the effect that he has satisfactorily received the equipment described on the card.

18

2. Existence of obsolete materials and spares
in central warehouse

Condition

There are obsolete materials and spare parts in the central warehouse which have not been written off and which are occupying space needed for usable material.

Criteria

Adequate control practices require that obsolete materials be segregated physically from usable materials.

Cause

Obsolete inventory releases take considerable time because they must be authorized by the court of accounts.

Effect

Usable space is wasted in the warehouse and costs and additional time are incurred in keeping unnecessary records.

Recommendation

AME should designate an area for the storage of obsolete materials and spare parts which does not reduce the available space for usable material. In addition, AME should approach the Court of Accounts as soon as possible for authorization to release the obsolete materials and spares, and evaluate the possibility of selling them at auction.

3. Lack of a document for transfer of mate-
rials and spares between warehouses

Condition

AME does not have a specific document for transfer of materials and spares between warehouses, such as transferring from the central warehouse to the warehouse in Santa Ana.

Criteria

Transfers of materials and spare parts between warehouses should be controlled with a form specifically designed for this purpose.

Cause

At present AME uses the same form as for shipment of consumables for the transfer of spares from one warehouse to another.

Effect

Inventory debits could be duplicated if a commodity output is recorded in more than one warehouse.

Recommendation

AME should design and use a specific form for transfer of materials and spares between warehouses.

ARTHUR ANDERSEN & Co.

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

COMPLIANCE WITH AGREEMENT TERMS AND APPLICABLE LAWS

AND REGULATIONS

INDEPENDENT AUDITOR'S REPORT

Compliance with agreement terms and applicable laws and regulations is the responsibility of AME's management. As part of our survey of AME in connection with the PUBLIC SERVICES IMPROVEMENT PROJECT, USAID/EL SALVADOR PROJECT No. 519-0320 we performed limited tests of AME's compliance with agreement terms and certain provision of laws and regulations. However, the objective was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

Except for the issues described under findings No. 1 to No. 2 of this report, the results of our evaluation disclosed that, with respect to items tested, AME had complied, in all material aspects, with agreement terms and applicable laws and regulations. With a respect to items not tested, nothing came to our attention that caused us to believe that AME had not complied in all material respects with those provisions.

This report is intended for the use of the ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME) and the U.S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter public record.

Arthur Andersen & Co

June 23, 1992

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

COMPLIANCE WITH AGREEMENT TERMS AND APPLICABLE LAWS

AND REGULATIONS

FINDINGS

1. Lack of separate auxiliary records for goods acquired under the project and preparation of the equipment/supplies accountability statement

Condition

AME does not keep separate auxiliary records for goods (machinery, equipment, spares and supplies) acquired with project funds and neither does it prepare the equipment/supplies accountability statement.

Criteria

Under Section VI B (2) of implementation letter No. 3 of the agreement, AME should keep independent accounting records for the use of funds or goods provided under the agreement. Additionally, in the evaluation and advance reports on the project, AME should include a section on development of the project detailing the use of funds by budget line (Equipment/Supplies Accountability Statement).

Cause

AME did not receive a copy of implementation letter No. 3 and consequently was unaware of the requirement.

Effect

Goods acquired under the project can be abstracted or used without the authorization of management or used with purposes not in accordance with the project. In addition, all USAID/El Salvador information requirements are not being complied with. Moreover, AME does not know the amount used and available for each budget line item.

Recommendation

AME should: (a) implement auxiliary records for goods (machinery, equipment, materials and spares) acquired under the project. These records should show as a minimum: (1) a description of the property, (2) identification number, (3) date of acquisition, (4) cost, (5) location, and (6) use and

Handwritten initials

condition of the property; (b) AME should keep a physical inventory of the property and the results should be reconciled with the property register and; (c) AME should also prepare monthly reports on execution of the project by budget line (equipment/Supplies Accountability Statement).

2. Lack of information in project evaluation reports

Condition

Project evaluation reports prepared by AME (monthly goal attainment reports) do not include details of problems detected and possible solutions.

Criteria

Under Article 5, Section 5.1 of the Agreement, as expanded by implementation letter No. 3, monthly, half-yearly and annual reports on project progress and advance should include problems detected and possible solutions.

Cause

AME was not aware of this requirement as the previous administration did not distribute a copy of the agreement to the different departments involved.

Effect

When problems detected in the course of execution of the project are not reported, corrective measures cannot be taken in time, and project execution itself can be affected.

Recommendation

In the monthly, half-yearly and annual reports on project progress and advance, AME should include details of problems detected and possible solutions.

ARTHUR ANDERSEN & Co.

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

REPORT ON FOLLOW UP TO PREVIOUS YEAR'S CONSULTING RECOMMENDATIONS

INDEPENDENT AUDITOR'S REPORT

We have performed an evaluation of AME's management capability for the administration of activities assigned to it under the PUBLIC SERVICES IMPROVEMENT PROJECT, USAID/EL SALVADOR PROJECT No. 519-0320.

Except for not conducting an external quality control review by an unaffiliated organization as described further in our report on Management Capability, our evaluation was performed pursuant to USAID/EL SALVADOR'S statement of work for the above mentioned project and in accordance with the United States Comptroller General's "Government Auditing Standards" (1988 Revision).

As part of our evaluation, we performed the follow up to findings and recommendations included in the following documents: (1) Report on Host Country Contracting Assessment performed by Louis Berger International, Inc. in May, 1991 (Contract No. 519-0320-C-00-01103-00) and (2) Report on Evaluation of the Commodity Management System performed by DEVRES, INC. in August, 1991 (Contract No. 519-0349-C-00-1111).

Such follow up was made of findings and recommendations which could have a material effect on our evaluation, to determine if the ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME) has take adequate corrective measures.

Except for the matters indicated in findings No. 1 through No. 2 included in this section, the results of our follow up tests indicate that the ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME) has adopted adequate corrective measures regarding the matters included in the document described in the third paragraph of this report.

This report is intended for the use of the ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME) and the U.S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter of public record.

Arthur Andersen & Co.

June 23, 1992

24

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT (AME)

REPORT ON FOLLOW UP TO FINDINGS AND RECOMMENDATIONS ARISING
FROM PREVIOUS YEAR'S AUDITS

FINDING

1. Lack of Implementation of some recommendation in
the Report of Louis Berger International, Inc

AME has not implemented the following recommendations in the report of Louis Berger International, Inc., on Host Country Contracting Assessment done in May, 1991.

- Maintain updated records of inventories and other equipment acquired under the project. These records should be reconciled on a monthly basis with the general ledger and periodically with physical inventories (Recommendation No. 4) The result of our follow up indicates that AME does have up-to-date records but they are not reconciled periodically with stocks, as periodic inventory taking is not practiced.
- Require that the Evaluation Committee prepare a table to compare the technical specifications for each item required with those proposed by the vendors. In addition, assign a technical expert to verify that bids meet the technical specifications (Recommendation No. 6). In this respect, AME prepares a table for analysis of bids but this is done only to compare prices and not technical specifications.
- Request and purchase commodities according to the annual plan and set limits for warehouse stock. The warehouse should report on a monthly basis which commodities are below the minimum (Recommendation No. 8). AME has a purchasing plan but it is not being used for its purpose as the AME income and expenditure budget limits a certain allocation of funds to the spares line. In addition, the plan was prepared on the basis of experience in consumption in previous years and not in coordination with an annual maintenance and repair plan.

As to limits in the warehouse, AME is establishing them in the normal course on the basis of the following priorities: (1) Type A spares, with high movement, (2) Type B spares, with medium movement, and (3) Type C spares, with little movement.

- The minutes from the Evaluation and Technical Committees and correspondence with A.I.D. and vendors, should be signed by the responsible AME authorities, and only these documents should support the contract decisions (Recommendation No. 9).
- Update list of vendors as follows: (Recommendation No. 10).
 - Prepare prequalification questionnaires and advertise their availability in the Commerce Business Daily and local newspapers.
 - Evaluate the answer from the vendors to questionnaires.
 - Prepare a document of the acceptable vendors; this document should be signed by the management of AME and by USAID.
 - The addition of any supplier to the list should be based on an evaluation of the prequalification questionnaire filled out by the requesting vendor and approved in writing by AME and USAID.
 - The IFB should be provided to prequalified vendors only.

Recommendation

AME should implement the recommendations of the Louis Berger report on Host Country Contracting Assessment to strengthen controls for project purposes.

2. Lack of implementation of some recommendations in the report of DEVRES, Inc.

Condition

AME has not implemented the following recommendations in the report of DEVRES, Inc. on Evaluation of the Commodity Management System, performed in August 1991:

- Institute procedures for the follow up of damages and shortages claims (Recommendation No. 3)
- Establish procedures to identify and return incorrect parts (Recommendation No. 4).
- Include funding source information in inventory records of the commodities acquired under Project No. 519-0279.
- Dispose of unserviceable and surplus equipment and spares (Recommendation No. 8).

- Provide maintenance manuals, currently not available for much of the existing equipment (Recommendation No. 9).

Recommendation

AME should implement the recommendations of Devres, Inc. derived from evaluation of the commodities management system to strengthen controls for project purposes.

AWARD SURVEY OF USAID/EL SALVADOR'S

PUBLIC SERVICES IMPROVEMENT PROJECT 519-0320

MANAGED BY THE ADMINISTRATION FOR MACHINERY AND EQUIPMENT -AME-

LIST OF REPORT RECOMMENDATIONS

Management Capability

1. AME should apply for additional resources and allocate them to expansion of the central workshop and to create specific work areas. In addition, AME should take measures to dispose of obsolete and unusable equipment and include these units annual action plan. Also, AME should speed up application procedures before the Court of Accounts to release these goods both physically and from the accounts.
2. AME should request the Ministry of Public Works (MOP) to speed up steps for authorization of the draft regulations and put them into effect.
3. AME should require its officers to confirm in writing that they are not involved in situations likely to give rise to conflicts of interest. AME should design a printed questionnaire for the purpose and see to it that it is completed at least once a year.

Internal control structure

1. AME should prepare of responsibility cards per employee for the control of goods acquired, and which should contain as a minimum:
 - Equipment control code, in running order
 - Place and date of delivery
 - Name of employee receiving equipment
 - Description of equipment delivered
 - Location and/or destination of equipment
 - Signature of employee to the effect that he has satisfactorily received the equipment described on the card.
2. AME should designate an area for the storage of obsolete materials and spare parts which does not reduce the available space for usable material. In addition, AME should approach the Court of Accounts

28

as soon as possible for authorization to release the obsolete materials and spares, and evaluate the possibility of selling them at auction.

3. AME should design and use a specific form for transfer of materials and spares between warehouses.

Compliance with agreement terms and applicable laws and regulations

1. AME should: (a) implement auxiliary records for goods (machinery, equipment, materials and spares) acquired under the project. These records should show as a minimum: (1) a description of the property, (2) identification number, (3) date of acquisition, (4) cost, (5) location, and (6) use and condition of the property; (b) AME should keep a physical inventory of the property and the results should be reconciled with the property register and; (c) AME should also prepare monthly reports on execution of the project by budget line (equipment/Supplies Accountability Statement).
2. In the monthly, half-yearly and annual reports on project progress and advance, AME should include details of problems detected and possible solutions.

Follow up to prior year consulting recommendations

1. AME should implement the recommendations of the Louis Berger report on host country contracting assessment to strengthen controls for project purposes.
2. AME should implement the recommendations of Devres, Inc. derived from evaluation of the commodities management system to strengthen controls for project purposes.

MINISTERIO DE OBRAS PUBLICAS
ADMINISTRACION DE MAQUINARIA Y EQUIPO
SAN SALVADOR, EL SALVADOR, C. A.

REF. GG-AMM-0429/92

San Salvador, 25 de septiembre de 1992

Señores
Arthur Andersen & Co.
Ciudad.

Atn. Lic. José Alfredo Aguirre
Corresponsal en El Salvador

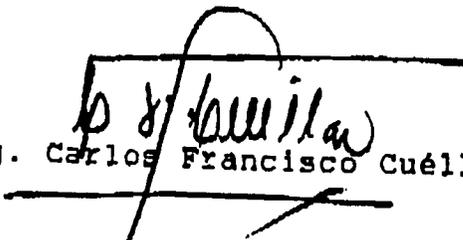
Estimados Señores:

En respuesta a su nota Ref. 133-AU-92, adjunto a esta nota sirvanse encontrar nuestros comentarios al Informe sobre la evaluación de la capacidad de AME para administrar las actividades asignadas bajo el Proyecto de Mejoramiento de Servicios Públicos USAID/El Salvador, Proyecto NQ 519-0320.

En espera de que los comentarios de esta Administración expresados anteriormente sean tomados en cuenta para la emisión del informe final, ya que de esa forma las observaciones allí presentadas estarán reflejadas de una manera más objetiva.

Atentamente,




Ing. Carlos Francisco Cuéllar

COMENTARIOS DE LA ADMINISTRACION AL INFORME DE AUDITORIA AL PROYECTO DE MEJORAMIENTO DE SERVICIOS PUBLICOS USAID/EL SALVADOR, PROYECTO NQ 519-0320.

1. Redefinir la causa y recomendación del hallazgo NQ 3 del reporte sobre la capacidad administrativa, debido a que el hecho de que SETEFE no haya autorizado el desembolso total del monto asignado para la construcción del plantel de San Miguel, no es la razón por la cual no se habían iniciado las gestiones para su construcción, sino que se debe a la clasificación en la que actualmente se encuentra AME, podrá iniciarse el proceso hasta que se conozca el resultado de la auditoría de Arias, Arias y Cía., sobre el área de inventarios.

2. En la página 3 del informe de auditoría, indican que no existen facilidades convenientes para un taller en la región oriental (San Miguel). Consideramos que este planteamiento debería ser más explicatorio, debido a que ya se efectuaron estudios y análisis técnicos sobre las condiciones existentes para la construcción de dicho plantel en la zona oriental; el cual demostró que si existen las condiciones adecuadas para llevar a cabo la infraestructura que albergará los talleres de AME en esa zona.

En base a los anterior, consideramos que sería conveniente replantear lo contenido en la parte citada del informe.

3. En el numeral 4 de la estructura de control interno, se indica que falta una estrategia de PED definida a mediano y largo plazo; no obstante lo anterior, la Unidad de PED cuenta con estrategias definidas relacionadas con el trabajo que aquí se desarrolla, así como la ejecución de evaluaciones periódicas que sobre las Pc's asignadas en los diferentes departamentos se llevan a cabo.

Al comienzo de este período fiscal, la unidad de PED presentó a la Gerencia General un plan que contenía una serie de estrategias y proyecciones que a corto y mediano plazo se tenían que implementar, siempre que se contara con los recursos para hacerlo.

A continuación presentamos un resumen del contenido del informe de fecha 21 de enero de 1992, que fue remitido a la Gerencia General y sobre la consecución del cual se está trabajando en el presente año:

- i) El equipo de cómputo asignado a los diferentes departamentos y unidades de AME, a excepción de las WYSE, será integrado en una red que permitirá la comunicación entre los diferentes departamentos y a la vez independencia entre los mismos.
- ii) Durante la etapa de transición se tendrán los dos sistemas, XENIX y NETWARE funcionando.
- iii) El traslado de aplicaciones y de bases de datos será hecho en forma gradual y ordenada, basándose en que los programas satisfagan las necesidades de los usuarios y que a la vez, permitan un trabajo interactivo total dentro del mismo; de esta forma se evitará el acceso a las bases.
- iv) Los programas que carezcan de lo indicado en el literal anterior serán modificados bajo la supervisión de un equipo de trabajo y según las especificaciones por escrito por parte de todos los que estén relacionados a ese proceso o programa.
- v) Se tendrán programas estructurados y globales donde cada usuario verá lo que necesita e ingresará los datos que le correspondan.
- vi) La estructura de la red será orientada a representar la estructura de AME; es decir, los directorios reflejarán los diferentes departamentos de la Institución, cada cual con sus respectivos usuarios y derechos; esto ayudará a la administración del sistema y al manejo de la información, ya que la orientación antes mencionada también se refiere a la captura de datos y a la ejecución de procesos.
- vii) Los datos serán ingresados a la red por el departamento que los genera y éstos estarán disponibles para consultas por otros departamentos involucrados.

32

- viii) Los datos serán ejecutados por el departamento que corresponda, esto garantizará que haya integridad y veracidad en la información y evitará duplicidad y errores en los datos ingresados.

- ix) El paso anterior puede tomar un tiempo de seis a doce meses después de la instalación de la red hasta tener una operación óptima del sistema, dependiendo de la cantidad de aplicaciones a desarrollar, el personal disponible, etc.

Handwritten mark

REPORT DISTRIBUTION

U.S. Ambassador El Salvador	1
D/USAID/El Salvador	5
AA/LAC	2
LAC/CEN	1
XA/PR	1
LEG	1
GC	1
AA/OPS	1
AA/FA	1
FA/FM	1
POL/CDIE/DI	1
FA/MC	1
IG	1
AIG/A	1
AIG/I&S	1
D/AIG/A	1
IG/A/PPO	2
IG/LC	1
IG/RM/GS	5
IG/A/FA	1
IG/A/PSA	1
RIG/A/EUR/W	1
RIG/A/Cairo	1
RIG/A/Dakar	1
RIG/A/Nairobi	1
RIG/A/Singapore	1
RIG/A/Vienna	1