

**Regional Inspector General for Audit  
Singapore**

---

**AUDIT OF USAID/SRI LANKA'S MANAGEMENT  
OF A.I.D.-FUNDED CONSTRUCTION**

---

**Audit Report No. 5-383-93-7  
January 29, 1993**



INSPECTION  
GENERAL



U.S. AGENCY FOR  
INTERNATIONAL  
DEVELOPMENT

January 29, 1993

**MEMORANDUM**

TO: Richard M. Brown, Mission Director, USAID/Sri Lanka

FROM:   
James B. Durnil, RIG/A/Singapore

SUBJECT: Audit of USAID/Sri Lanka's Management of A.I.D.-Funded Construction (Audit Report No. 5-383-93-7)

Enclosed are five copies of the subject audit report. Our audit work and written representations made by USAID/Sri Lanka confirmed that controls over A.I.D.-funded construction were adequate in most areas. For example, the Mission sufficiently defined construction activities to demonstrate eligibility for use of Fixed Amount Reimbursement financing; reviewed and approved cost estimates to establish the level of A.I.D. financing; assessed the host government agencies' personnel, financial position, and budgetary procedures; and communicated the Fixed Amount Reimbursement terms and conditions to the host government. Furthermore, the Mission's monitoring significantly conformed to A.I.D. requirements. Also, the Mission properly paid, controlled, and accounted for construction funds.

USAID/Sri Lanka's controls, however, could be strengthened by ensuring that A.I.D.-financed construction is used as intended, and United States participation is publicized at construction sites.

We made two recommendations to improve controls over construction. Your comments to these recommendations and the draft report were fully considered in finalizing this report. Based on these comments, both recommendations are resolved and will be closed upon completion of planned actions. Your comments are summarized after each finding and are presented in their entirety in Appendix II.

Please provide us information within 30 days indicating any actions planned or taken to implement the recommendations. I appreciate the cooperation and courtesies extended to my staff during the audit.

Attachments: a/s

# EXECUTIVE SUMMARY

---

## **Background**

USAID/Sri Lanka finances construction activities throughout the country. As of March 31, 1992, the Mission was responsible for administering 27 projects, 7 of which contained a construction element. Mission records showed \$19.9 million obligated and \$8.5 million expended for construction, representing approximately 20 percent and 12 percent, respectively, of total project funds. To finance the construction activities, the Mission uses the Fixed Amount Reimbursement method (page 1).

---

## **Audit Objectives**

The Office of the Regional Inspector General for Audit/Singapore audited USAID/Sri Lanka's management of A.I.D.-funded construction to determine whether the Mission followed A.I.D. procedures in (1) planning for Fixed Amount Reimbursement construction activities, (2) monitoring construction activities, and (3) paying for construction activities and controlling and accounting for construction services funds. The audit was made from March 2, 1992 to July 10, 1992 in accordance with generally accepted government auditing standards (page 2 and Appendix I).

---

## **Summary of Audit**

USAID/Sri Lanka generally followed A.I.D. procedures in properly planning for Fixed Amount Reimbursement construction activities, monitoring construction activities, paying for construction activities, and controlling and accounting for construction services funds. The Mission, however, did not ensure that buildings costing A.I.D. at least \$1.1 million were used as intended, or that publicity requirements were met at A.I.D.-funded construction sites (pages 4, 6, and 17).

---

## **Audit Findings**

### **Planning for Fixed Amount Reimbursement Construction**

USAID/Sri Lanka properly followed A.I.D. procedures in planning for Fixed Amount Reimbursement construction activities. In accordance with A.I.D. procedures, the Mission: (1) sufficiently defined construction activities to demonstrate eligibility for use of Fixed Amount Reimbursement financing; (2) reviewed and approved cost estimates to establish the level of A.I.D. financing; (3) assessed the host government agencies' personnel, financial position, and budgetary procedures; and (4) clearly communicated the Fixed Amount Reimbursement terms and conditions to the host government (page 4).

### **Monitoring Construction Activities**

USAID/Sri Lanka properly followed A.I.D. procedures in monitoring construction activities, except for ensuring that all completed buildings were used as intended, and that United States participation was publicized at all construction sites. In accordance with A.I.D. procedures, the Mission: (1) established monitoring systems; (2) held frequent meetings with government officials, contractors, and other participants; (3) made timely site visits to construction sites; (4) implemented a new Project Implementation Reporting system in 1991; (5) made final inspections of the completed construction works before processing the implementing agencies' Requests for Reimbursement; and (6) completed most evaluations as scheduled. However, as summarized below, the Mission did not always ensure that A.I.D.-funded buildings were used after completion of construction or that United States participation was publicized at construction sites (page 6).

### **A.I.D.-Financed Buildings Were Unused**

USAID/Sri Lanka did not ensure that the Sri Lankan Government used the A.I.D.-financed buildings constructed under one of three projects tested. Although the Mission knew that the host government was not providing the staff necessary to use the buildings, the Mission continued to expend funds for construction. The Mission continued construction because it expected the Government to provide the staff necessary to use

the buildings. By project completion, A.I.D. had expended up to \$1.1 million for buildings which remained unstaffed and unused (page 7).

### **United States Participation Was Not Publicized at Construction Sites**

Contrary to A.I.D. procedures, USAID/Sri Lanka did not ensure that United States participation was publicized at A.I.D.-financed construction sites. Mission management did not instruct Project Officers to verify the existence of public signs during site inspections and, therefore, site inspection reports did not alert management to the absence of such signs. As a result, the United States did not receive full recognition for at least \$4.4 million—and possibly as much as \$8 million—of development assistance funds spent on construction activities in Sri Lanka (page 12).

### **Paying, Controlling, and Accounting for Construction Funds**

USAID/Sri Lanka properly followed A.I.D. procedures in paying for construction activities and controlling and accounting for construction services funds. The Mission: (1) established a system of internal controls to account for and pay for construction activities; (2) followed A.I.D.'s administrative and certification processes; (3) verified vouchers against the underlying commitments as required; (4) scheduled vouchers for payment prior to submission for processing to the Disbursing Office; (5) established procedures to receive and track vouchers as stipulated by the Prompt Payment Act; and (6) monitored the financial pipeline to reduce unliquidated balances by \$11.5 million (page 17).

---

## **Summary of Recommendations**

This report contains two recommendations to correct problem areas, including recommendations to:

- Obtain a refund from the Sri Lankan Government for the cost of all buildings not used effectively under one project, unless staff is provided as agreed to use the buildings (page 7); and
- Ensure that United States participation is publicized at A.I.D.-financed construction sites (page 13).

---

## **Management Comments and Our Evaluation**

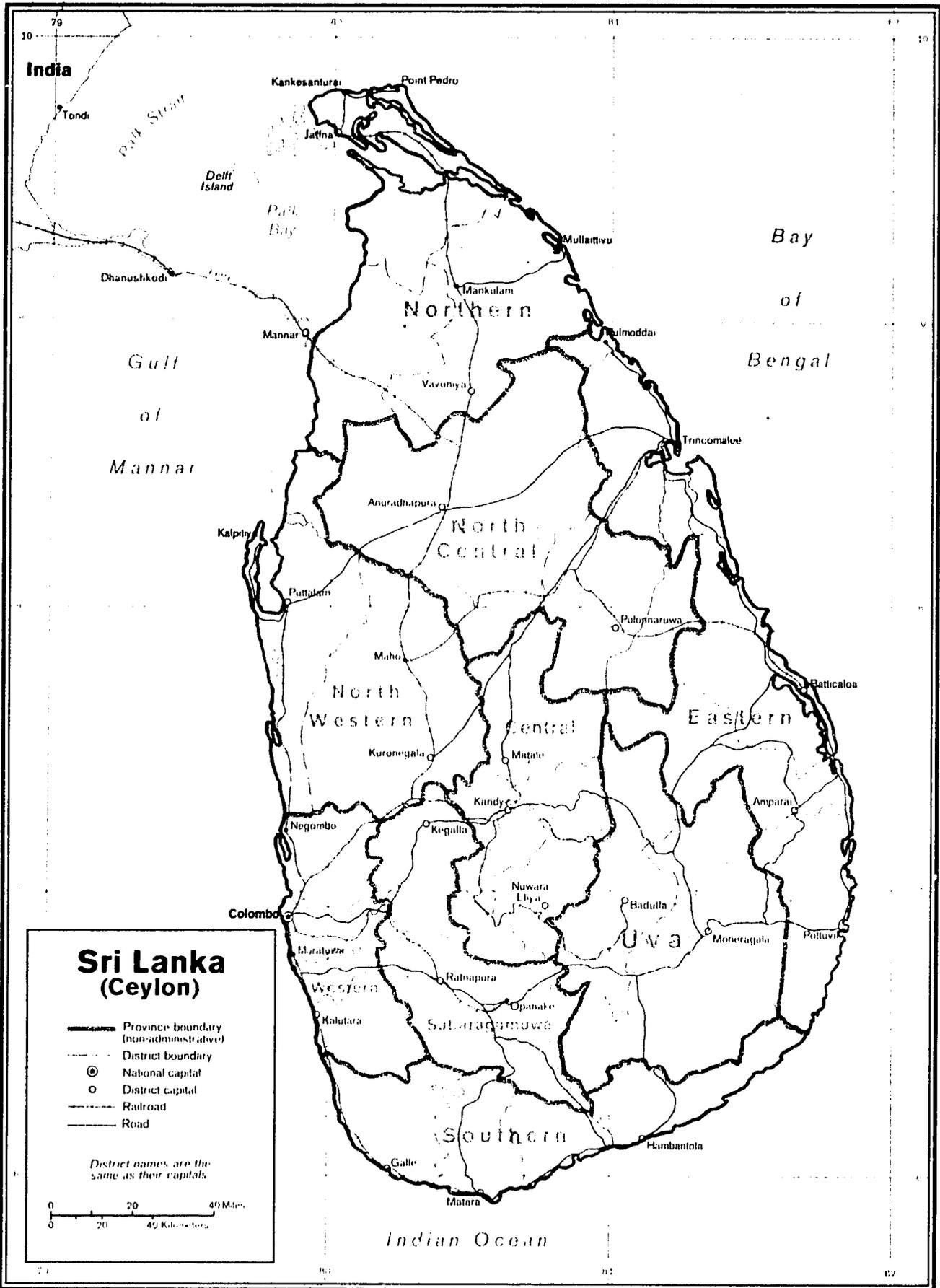
In responding to a draft of this report, USAID/Sri Lanka agreed with the audit findings and recommendations, and noted that the audit was useful in confirming the effectiveness of the Mission's management of construction. The Mission also provided some additional comments to place the audit findings in better perspective. The Mission has already initiated corrective action in response to the two recommendations. Accordingly, both recommendations are resolved and will be closed upon completion of planned actions.

USAID/Sri Lanka's comments were fully considered in finalizing this report and, where appropriate, we have revised the report. Mission comments are evaluated at the end of each finding and are presented in their entirety as Appendix II.

*Office of the Inspector General*

Office of the Inspector General  
January 29, 1993

---



## **Table of Contents**

---

	<u>Page</u>
<b>EXECUTIVE SUMMARY</b>	i
<b>INTRODUCTION</b>	1
Background	1
Audit Objectives	2
<b>REPORT OF AUDIT FINDINGS</b>	4
Did USAID/Sri Lanka follow A.I.D. procedures in planning for Fixed Amount Reimbursement construction activities?	4
Did USAID/Sri Lanka follow A.I.D. procedures in monitoring construction activities?	6
A.I.D.-Financed Buildings Were Unused	7
United States Participation Was Not Publicized at Construction Sites	12
Did USAID/Sri Lanka follow A.I.D. policies and procedures in paying for construction activities, and controlling and accounting for construction services funds?	17
<b>REPORT ON INTERNAL CONTROLS</b>	19
<b>REPORT ON COMPLIANCE</b>	22
<b>EXHIBIT</b>	<u>Exhibit</u>
USAID/Sri Lanka Construction Projects	I
<b>APPENDICES</b>	<u>Appendix</u>
Scope and Methodology	I
USAID/Sri Lanka Comments	II
Report Distribution	III

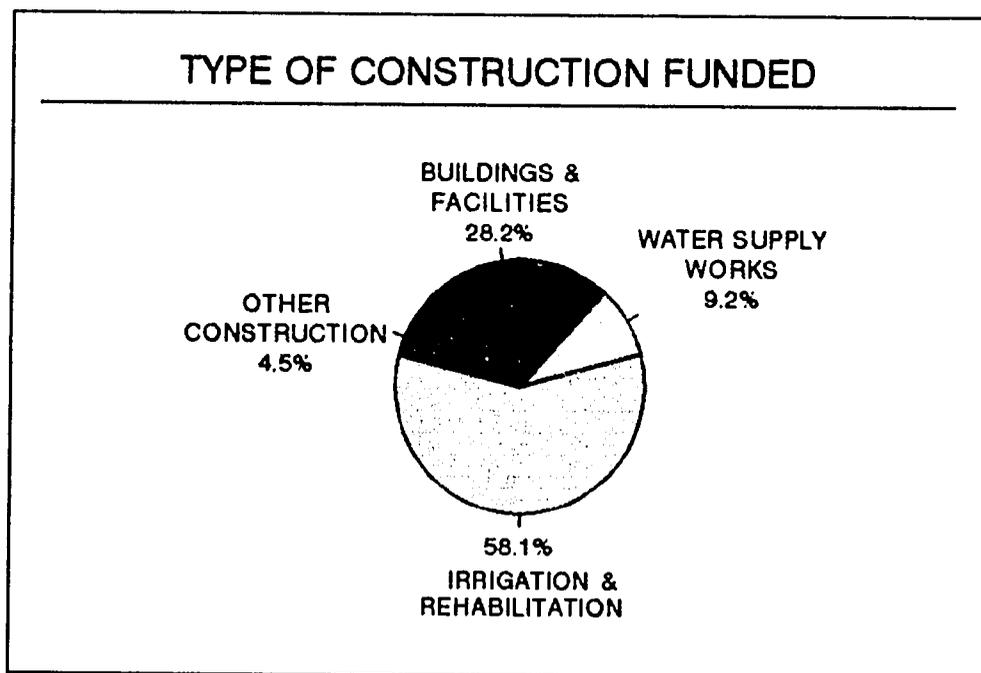
---

# INTRODUCTION

## Background

USAID/Sri Lanka finances construction activities throughout the country, much of which is directed at Sri Lanka's Accelerated Mahaweli Program: a large irrigation program started in the late 1970's and designed to use the water resources of the Mahaweli river through a series of dams. The resultant irrigation and power generation sustains large populations in the north-central and eastern parts of Sri Lanka.

As of March 31, 1992, USAID/Sri Lanka was responsible for administering 27 projects, 7 of which contained a construction element. The types of construction funded by A.I.D. consist of (1) office buildings and facilities, (2) water supply works, (3) rehabilitation of irrigation systems, and (4) other projects such as the construction of roads. The following chart illustrates the allocation of expended funds to the construction activities.



For these construction activities, Mission records showed \$19.9 million obligated and \$8.5 million expended as of March 31, 1992, representing about 20 percent and 12 percent, respectively, of total project funds.

To finance the construction activities, USAID/Sri Lanka uses the Fixed Amount Reimbursement method. This method of financing involves determining in advance the total cost of the construction activity based upon cost estimates reviewed and approved by A.I.D. The Mission is responsible for monitoring construction progress and making periodic inspections—the most important being the final inspection. A.I.D. funds are disbursed, i.e. the Sri Lankan Government is reimbursed, generally upon final inspection and acceptance by A.I.D. that the construction has been completed in accordance with pre-agreed specifications. However, when warranted, advance payment provisions may be authorized.

Ethnic/social conflicts have interrupted the progress of construction activities within Sri Lanka. Prolonged civil conflicts and the resulting security problems have both directly and indirectly (through inflation, labor/material shortages, etc.) impaired the progress of many construction activities. Due to the conflicts, USAID/Sri Lanka has completed only 2 of 7 construction projects and has suspended 1 indefinitely. Exhibit I identifies these projects and the respective project periods.

The conflicts have occasionally also restrained USAID/Sri Lanka's ability to monitor effectively construction activity on almost all projects. On several occasions, the Mission could neither make site visits nor evaluate projects as scheduled because of travel restrictions.

USAID/Sri Lanka plans to phase out construction and direct assistance to other types of activities. Mission officials said that the Sri Lankan Government is fully capable of carrying out construction activities on its own, and that the Mission's administration and oversight of construction activities requires too much staff time. Thus, A.I.D. funds could be used more effectively in other areas of development.

---

## **Audit Objectives**

The Office of the Regional Inspector General for Audit/Singapore audited USAID/Sri Lanka's management of A.I.D.-funded construction to answer the following audit objectives:

- **Did USAID/Sri Lanka follow A.I.D. procedures in planning for Fixed Amount Reimbursement construction activities?**
- **Did USAID/Sri Lanka follow A.I.D. procedures in monitoring construction activities?**
- **Did USAID/Sri Lanka follow A.I.D. policies and procedures in paying for construction activities, and controlling and accounting for construction services funds?**

In answering these audit objectives, we tested whether USAID/Sri Lanka followed applicable internal controls and complied with certain legal requirements. We designed tests to provide reasonable assurance that the answers to the above audit objectives are valid. We also included steps to detect abuse or illegal acts which could affect the audit objectives. USAID/Sri Lanka's management provided written representations which we considered essential to confirming our conclusions on the audit objectives and to assessing internal controls and compliance. These written representations have been included as part of the Mission comments attached to this report as Appendix II.

For each problem area, we did additional work to:

- Identify the cause and effect of the problem; and
- Make recommendations to correct the problem and the cause.

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

---

# REPORT OF AUDIT FINDINGS

---

## **Did USAID/Sri Lanka Follow A.I.D. Procedures in Planning for Fixed Amount Reimbursement Construction Activities?**

USAID/Sri Lanka properly followed A.I.D. procedures in planning for Fixed Amount Reimbursement construction activities.

In accordance with A.I.D. Handbook 1, Supplement B, and Handbook 3, Appendix 3J, USAID/Sri Lanka sufficiently defined construction activities for all seven projects to demonstrate eligibility for financing with the Fixed Amount Reimbursement method. The Mission selected this method because the construction activities were low cost, short term, and divisible into self-sustaining segments small enough to enable the host government to complete prior to receiving reimbursement from A.I.D.

USAID/Sri Lanka reviewed and approved cost estimates and determined the amount of A.I.D.'s contributions as required by A.I.D. Handbooks 1 and 3. Cost estimates for all seven projects were prepared by the Sri Lankan Government and submitted to A.I.D. for review and approval. The Mission then approved the estimates and prepared Project Implementation Letters to identify the binding fixed costs under this method of financing.

USAID/Sri Lanka also assessed the host government agencies' personnel policies, financial position, and budgetary procedures for all seven projects as required by A.I.D. Handbooks 1 and 3. These assessments included: (1) in-depth analyses of the agencies done during each project design, (2) financial reviews of the agencies' accounting and budgetary procedures carried out by the Mission Controller's office, and (3) external reviews of all implementing agencies carried out by a management consulting firm in late 1989.

All seven external reviews were done in accordance with new A.I.D. guidance to update assessments of host government capabilities every three years. The consulting firm assessed various agencies' voucher examination and procurement processes as well as the agencies' abilities to provide audit coverage. Separate reports were compiled for each project providing USAID/Sri Lanka with useful information about each agencies' procedures. Although the reports lacked conclusions about the agencies' capabilities to carry out the required procurement procedures, the Controller planned to correct this deficiency during reviews scheduled for fiscal year 1993.

Once USAID/Sri Lanka chose to use the Fixed Amount Reimbursement method of financing, the Mission—in accordance with A.I.D. Handbook 1, Supplement B and Handbook 3, Appendix 3J—clearly communicated the terms and conditions of this method to the host government and apprised the government of the risks involved in applying this method. Mission officials provided this communication for all seven projects through Project Implementation Letters which informed the Sri Lankan Government of the mechanics of the Fixed Amount Reimbursement system: what actions are required, how and when these actions must be implemented, and what actions the Mission would and would not allow.

---

## **Did USAID/Sri Lanka Follow A.I.D. Procedures in Monitoring Construction Activities?**

USAID/Sri Lanka properly followed A.I.D. procedures in monitoring construction, except for ensuring that buildings were used effectively, and United States participation was publicized at construction sites.

USAID/Sri Lanka established monitoring systems in line with A.I.D. procedures. The Mission used monitoring plans, project agreements, Project Implementation Letters, and progress reports as references and information sources in monitoring all seven projects, as stipulated in A.I.D. Handbook 3, Chapter 11, Section 11C. Also, for all seven projects, Project Papers, Project Implementation Letters, project agreements, and contracts established reporting requirements as required by Section E of Chapter 11. This documentation specified the nature and timing of reports. Of 17 host government and contractor progress reports examined for 3 projects, all reports met the requirements. Furthermore, the Mission held frequent meetings with government officials, contractors, and other participants as called for by Section 11E, Part C of Handbook 3. When safe to do so, Project Officers made site visits to each construction site every one to two months, although the frequency varied during different stages of completion—increasing as construction activity progressed. Of 6 site visit reports for 3 projects reviewed at random, all 6 contained the information suggested in Appendix 11C of Handbook 3.

USAID/Sri Lanka also implemented a new Project Implementation Reporting system in 1991 to better ensure compliance with Chapter 11, Section F of A.I.D. Handbook 3. Officials of the Mission's Projects Office compiled quarterly reports using performance information provided by Project Officers and financial information provided by the Controller. Of 19 quarterly project implementation reports examined for 3 projects, all reports met the requirements. The format of all 19 reports complied with guidance issued by the Asia Bureau and Chapter 11 of Handbook 3. Mission officials discussed the information contained in these reports at quarterly project review meetings, and the information was also used by senior Mission officials during similar meetings held on an ad hoc basis when project activities warranted the attention of management.

USAID/Sri Lanka officials made final inspections of the completed construction works for all seven projects before processing the implementing agencies' reimbursement requests. According to Mission officials, when they found certain elements or components of the construction to be unsatisfactory or incomplete, reimbursement requests

were refused. If a contractor had not completed work in accordance with specifications, the implementing agency followed up until the work was completed satisfactorily, and Mission officials then made follow-up inspections in accordance with A.I.D. Handbook 3, Appendix 3J. Field trips to 11 construction sites involving 3 projects showed that Mission records were accurate in identifying the status of construction activity.

USAID/Sri Lanka completed 8 evaluations (both Mid-Term and Final) for the 7 projects as scheduled in Project Papers; another 3 evaluations were not done as scheduled, mainly because civil disturbances prevented project activities from progressing enough to warrant an evaluation. In these instances, the Mission justified and documented its decision not to make the scheduled evaluations. In compliance with the established Mission procedures, The Mission evaluated the projects .

As discussed below, however, USAID/Sri Lanka did not always ensure that buildings were used effectively upon completion, or that United States participation was publicized at construction sites.

### **A.I.D.-Financed Buildings Were Unused**

Contrary to A.I.D. procedures, USAID/Sri Lanka did not ensure that the Sri Lankan Government used most of the A.I.D.-financed buildings constructed under one of three projects tested. Although the Mission knew that the host government was not providing the staff necessary to use the buildings, funds continued to be expended for construction. The Mission continued construction because it expected the Government to eventually provide the staff necessary to use the buildings. By project completion, A.I.D. had expended up to \$1.1 million for buildings which remained unstaffed and unused.

#### **Recommendation No. 1: We recommend that USAID/Sri Lanka:**

- 1.1 Determine how many of the 52 A.I.D.-financed buildings have not been used effectively as required by the project agreement for the Mahaweli Environment Project;**
- 1.2 Obtain a refund from the Sri Lankan Government for the cost of all building not used effectively unless the Sri Lankan Government provides the agreed-upon staff and uses the buildings within a specified time; and**

**1.3 Make a determination on whether to report on the Mission's failure to ensure the proper use of A.I.D.-financed construction as an internal control weakness in the next report required under the Federal Manager's Financial Integrity Act.**

Section 101 of the Foreign Assistance Act of 1961 requires that United States development resources be used effectively. In recognition of this section, A.I.D. Handbook 3, Appendix 6A, stipulates that project agreements must include a clause requiring the effective use of goods or services financed by U.S. project assistance funds.

In accordance with this requirement, all project agreements included a clause such as the one included in the Water Supply and Sanitation Project agreement:

*"If the failure of the Cooperating Country to comply with any of its obligations under this Agreement has the result that goods or services financed under the Assistance are not used effectively in accordance with this Agreement, A.I.D. may require the Cooperating Country to refund all or any part of the amount of the disbursements under this Agreement for such goods or services in U.S. dollars to A.I.D. within sixty days after receipt of a request therefor."*

For two of the three projects reviewed, USAID/Sri Lanka ensured compliance with this requirement. For the third project, however, the Mission did not ensure that the Sri Lankan Government used effectively at least 20 of the A.I.D.-financed buildings. This project—the Mahaweli Environment Project—included the construction of 60 buildings for the Department of Wildlife Conservation's programs. When we visited 4 project sites, 52 of the 60 buildings had been constructed and should have been used as planned.

Of the 52 buildings, we inspected 25 which had been completed for an average of eight months, but only 5 were occupied and fully used. Fourteen buildings showed no indication of having been used at all (did not contain furnishings and were unoccupied). Six were partially used (were either sparsely furnished or had very few or no occupants). The photos on the following pages show some of the buildings not used.



*Unused Storage Facility/Garage Located in Ambagaswewa, Sri Lanka*



*Unoccupied Ranger's Residence Located in Ambagaswewa, Sri Lanka*



*Unoccupied "Circuit" Bungalow Located in Angamedilla, Sri Lanka*

The buildings were not used because no staff was available. The Director of the Department of Wildlife Conservation said that the project had completed about 98 percent of the buildings but had only hired about 25 percent of the intended staff because of difficulties in recruiting qualified personnel. During the field trips to the project sites, government officials said that they were awaiting either the hiring of new employees or the transfer of present employees to the location. The officials expected some buildings to be occupied very soon, yet they could not say for sure when or if the buildings would be used.

This staffing problem occurred even though the host government had assured A.I.D., in satisfaction of a condition precedent to the disbursement of A.I.D. funds, that the necessary staff would be provided. USAID/Sri Lanka monitored the Sri Lankan Government's compliance with project agreement terms and, in 1982, obtained assurances from the Sri Lankan Government that the necessary staff would be hired over the life of the project. These assurances were provided in satisfaction of a condition precedent necessary for the release of project funds. However, as the construction proceeded, the promised staffing was not forthcoming. This was well known by Mission officials who repeatedly requested the Sri Lankan Government to provide the staff as agreed. However, when staff was still not provided, the Mission proceeded with the construction of nearly all the buildings as planned—even though the originally established "need" was now questionable.

USAID/Sri Lanka officials said that they continued the construction activities because they believed that the staffing problem would eventually be resolved and that all staff would be forthcoming. The Mission pointed out that there has been a moratorium on the creation of new permanent posts since 1986 and that the International Monetary Fund has been pressuring Sri Lanka to cut back on staffing. Nevertheless, the Mission believed that the Sri Lankan Government would still make staff available for this project.

We do not believe that USAID/Sri Lanka has obtained sufficient assurance that the necessary staffing will be provided. Notwithstanding the Mission's efforts, the staffing problem has persisted throughout the life of the project — 10 years— and now, the buildings have been completed, the project is over, and the staff has still not been provided. If the Sri Lankan Government would not honor its commitments to use the buildings during 10 years of project implementation when A.I.D. could have responded with the termination of financing, the Mission has little basis to expect the government to honor the commitments after project completion when A.I.D. has less leverage available.

To resolve this issue, USAID/Sri Lanka should determine how many buildings are not being used effectively, and then inform the Sri Lankan Government of the Mission's intent to claim a refund for the cost of the buildings, unless the required staffing is provided and the buildings are used. For the 20 buildings which we observed were not used effectively, A.I.D. expended \$.6 million but only received value for \$.1 million. Projecting these amounts to the total \$1.3 million spent on all construction for this project, \$1.1 million were used only partially or not at all. Pursuant to the project agreement, A.I.D. has three years after project completion to demand a refund of funds not used as intended.

Also, USAID/Indonesia should determine whether to report on the Mission's failure to ensure the proper use of A.I.D.-financed construction as an internal control weakness in the next report required under the Federal Manager's Financial Integrity Act.

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

USAID/Sri Lanka pointed out that the Mahaweli Environment Project was a major success partially due to the constructed facilities, without which, the Government would have lacked the infrastructure to undertake its field programs and safeguard the protected habitat established by the project. This success was achieved in spite of significant delays from

security problems. Therefore, the Mission believed that it was proper to continue project funding despite the absence of full staffing. The Mission also said that, based on substantial progress over the last six months, the Sri Lankan Government was fully committed to use all the buildings. Also, the Mission's support of a follow-on project provided the necessary leverage to ensure that previous A.I.D.-financed resources are used.

USAID/Sri Lanka agreed with the recommendation and initiated corrective action. The Mission has made unannounced visits to all 52 buildings financed under the project and reported that 40 are now occupied and used as intended. The Mission plans to: (1) obtain a written, four-month timetable and strategy for staffing the remaining 12 buildings from the Government of Sri Lanka; (2) conduct unannounced inspections over the next four months to confirm that the buildings are properly used; and (3) make a final unannounced inspection at the end of this four-month period to confirm the status of all buildings. For any building not used as intended at the end of this four-month period, the Mission will issue a bill of collection to the Government of Sri Lanka. Finally, the Mission determined that the delay in using the buildings was not sufficiently significant for reporting under the Federal Manager's Financial Integrity Act. The Mission requested that recommendation 1.1 and 1.2 be closed upon receipt of evidence that corrective actions have been completed, and that recommendation 1.3 be closed upon issuance of this report.

While the Mission does have some leverage to ensure the full use of previously A.I.D. financed resources, we note that the project agreement only provides the Mission three years to claim a refund if the buildings are not fully used. Recommendation Nos. 1.1 and 1.2 are resolved and will be closed upon receipt of documentary evidence that the entire 52 A.I.D.-financed buildings are used as intended or a bill for collection has been issued. Based on the Mission's determination and request for closure, Recommendation No. 1.3 is closed upon report issuance.

### **United States Participation Was Not Publicized At Construction Sites**

USAID/Sri Lanka did not always ensure that A.I.D. requirements were met for publicizing United States participation at construction sites. Mission management did not instruct Project Officers to verify the existence of public signs during site inspections and, therefore, site inspection reports did not alert management to the absence of signs. As a result, the United States did not receive full recognition for at least \$4.4 million—and possibly as much as \$8 million—in development assistance funds.

**Recommendation No. 2: We recommend that USAID/Sri Lanka:**

- 2.1 Ensure that the Sri Lanka Government posts signs or plaques at all A.I.D.-financed construction sites publicizing United States participation in the project;**
- 2.2 Require site visit reports to identify whether or not construction sites publicize United States participation as required by A.I.D Handbook 1, Supplement B, Chapter 22; and**
- 2.3 Make a determination on whether to report on the Mission's failure to monitor the posting of signs or plaques at A.I.D.-financed construction sites as an internal control weakness in the next report required under the Federal Manager's Financial Integrity Act.**

A.I.D. Handbook 1, Supplement B, Chapter 22 incorporates Section 641 of the Foreign Assistance Act which requires programs under this Act to be identified appropriately overseas as "American Aid". This same Chapter establishes specific publicity requirements by stipulating that:

*"Project construction sites and other project locations must display signs suitably marked and indicating participation by the United States in the project. These signs should be erected at an early date in the construction or implementation phase and be replaced by permanent signs, plates, or plaques, suitably marked, at the end of this phase."*

Section B.8 of the model project agreement in A.I.D. Handbook 3, Chapter 6 stipulates that the borrower or grantee must give appropriate publicity to the loan or grant and to the United States' contribution to the project as a whole, and mark goods financed by A.I.D. as specified in Project Implementation Letters.

Finally, A.I.D. Handbook 3, Appendix 11C provides guidelines for reporting on the results of site visits. One of the suggested elements to be covered is the Status of Construction and Installation which instructs reporting officers to note the existence of signs on or near the construction/installation which identify A.I.D. participation.

For the projects reviewed, the required public signs had been placed at only 1 of 11 sites visited (8 facility sites and 3 irrigation schemes). The 8 facility sites consisted of both completed buildings and on-going construction activity, while the 3 irrigation schemes consisted of more than 17 miles of rehabilitated and upgraded irrigation systems.

Only the training complex at one of the facility sites displayed the required signs. The Project Officer said that the signs were posted at this site during its opening ceremony held in February 1992, yet USAID/Sri Lanka did not request that the Sri Lankan Government post similar signs at all other construction sites to comply with the project agreements. The sign posted at the training complex is shown below:

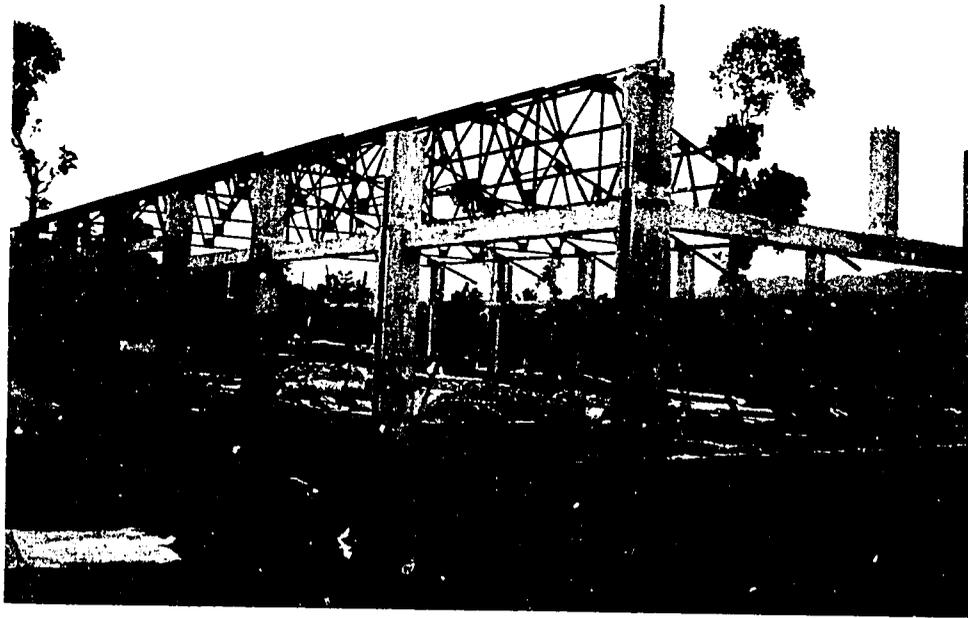


*Sign showing A.I.D. participation in a construction project.*

USAID/Sri Lanka did not instruct Project Officers to verify during site inspections the placement of publicity signs. Mission officials have recently begun to use a standardized Site Inspection Report format, but this report does not include the suggested checklist item in A.I.D. Handbook 3 requiring the Reporting Officer to note the existence of signs on or near the construction site.

As an example of the importance of public signs for A.I.D.-funded construction, one construction site visited (Water Supply and Sanitation

Project) was initiated with A.I.D. funding, but construction was suspended due to civil conflict. The Sri Lankan Government plans to resume construction without A.I.D. assistance. Signs publicizing United States funding of the construction were never posted at the site, and it is highly unlikely that the Sri Lankan Government will later install such signs. The people of Sri Lanka will therefore likely assume that the Government funded the entire project.



*Since no sign had been posted at this site, the Sri Lankan people will not be aware that this Water Supply and Sanitation Project was partially funded by the United States.*

The importance of publicizing United States participation at A.I.D.-funded construction sites can be demonstrated at another site where we noted a sign publicizing Japanese funding adjacent to an A.I.D.-funded site. However, there was no sign publicizing United States participation. Therefore, while the Japanese have been recognized for their economic assistance, the people of Sri Lanka are unlikely to be aware of the assistance from the United States.

One of the primary reasons for providing development assistance through bilateral projects is to promote goodwill between nations. U.S. law and A.I.D. policy requires that signs publicizing United States participation be posted at all construction sites to ensure that the intended goodwill is communicated to the people of the recipient country. For the three projects visited, an estimated \$4.4 million of U.S. government funds were

spent on construction activities, yet little evidence existed to identify who funded these activities. If this condition is present in the projects not tested, as much as \$8 million in U.S. assistance is not fully publicized.

To resolve this problem, USAID/Sri Lanka should ensure that the Sri Lankan Government posts signs publicizing participation by the United States at all A.I.D.-funded construction sites, and require Project Officers to verify and report on the existence of these signs when making site visit inspections. Also, the Mission should determine whether to report on the Mission's failure to monitor the posting of signs or plaques at A.I.D.-financed construction sites as an internal control weakness in the next report required under the Federal Manager's Financial Integrity Act.

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

USAID/Sri Lanka said that it has always been Mission policy to fully publicize A.I.D.-financed activities through signboards, plaques, official openings, newspapers, and electronic media. The Mission, however, agreed with the audit recommendation and has initiated corrective action.

USAID/Sri Lanka has installed plaques on 32 buildings of two of the projects audited and said that all sites with more than 3 buildings will have the required public signs by December 31, 1992. The Mission will also make unannounced site inspections to verify that all buildings have the required signs in place. Finally, the Mission will issue instructions to Project Officers requiring site visit reports to identify whether or not construction sites are publicized, and, if not, to take corrective action. With respect to reporting under the Federal Manager's Financial Integrity Act, the Mission plans to make a determination on the significance of the internal control weaknesses. The Mission requested that recommendation 2.1 and 2.2 be considered closed upon submission of reports which provide evidence that the required plaques/signboards have been installed. The Mission also requested that recommendation 2.3 be closed.

Recommendation No. 2.1 is resolved and will be closed upon receipt of documentary evidence that the required plaques or signboards have been installed. Recommendation No. 2.2 is resolved and will be closed upon receipt of a copy of Mission procedures which require site visit reports to identify the existence of plaques or signs which satisfy A.I.D. publicity requirements. Recommendation No. 2.3 is resolved and will be closed upon receipt of the Mission's determination on the significance of the internal control weaknesses.

---

## **Did USAID/Sri Lanka Follow A.I.D. Policies and Procedures in Paying for Construction Activities, and Controlling and Accounting for Construction Services Funds?**

USAID/Sri Lanka properly followed A.I.D. policies and procedures in paying for construction, and controlling and accounting for construction funds. The Mission established a system of internal controls which includes Mission Orders, a computerized database with built-in controls (the Mission Accounting and Control System), the segregation of duties within the Controller's Office, and supervisory reviews and approvals to ensure proper payment for construction-related activities.

In accordance with the Controller's Handbook, Chapter 5, and A.I.D. Handbook 19, Chapter 3, USAID/Sri Lanka followed A.I.D. certification processes for the 24 vouchers tested from a universe of 154 vouchers as of March 31, 1992. Examiners ensured that the vouchers were approved administratively and certified for payment before being released for further processing. As required by A.I.D. Handbook 19, Chapter 3, Project Officers approved the vouchers with an addendum—the "Checklist for Administrative Approval"—which gave the Authorized Certifying Officer a more thorough knowledge of the vulnerability of each payment.

USAID/Sri Lanka Voucher Examiners verified vouchers against the underlying commitments as required by the Controller's Handbook, Chapter 5. All 24 vouchers tested were in compliance with these requirements. The examiners verified each voucher to ensure that funds available were evidenced by the underlying commitment documents, i.e. Project Implementation Letters and contracts, before allowing payment to be processed. Also, examiners verified payment claims against the applicable terms and conditions of the project agreements, Project Implementation Letters, and contract agreements for eligibility and validity. The examiners ascertained the eligibility of claims by ensuring that the supporting documentation required by project agreements and Project Implementation Letters was submitted together with the vouchers as required by the Controller's Handbook, Chapter 5. Twenty-two out of 24 vouchers were supported by the required documentation.

In compliance with the Controller's Handbook, Chapter 5, USAID/Sri Lanka scheduled vouchers for payment prior to submission for processing to the Disbursing Office. As required by A.I.D. Handbook 19, Chapter 3, the Authorized Certifying Officer certified the schedules.

To comply with the Prompt Payment Act, USAID/Sri Lanka established procedures to receive and track vouchers. These procedures were implemented using the computerized Mission Accounting and Control System. However, a recent Mission review for the fiscal year ending September 30, 1991 found that the Mission had not complied fully with the Prompt Payment Act. The review was made as part of the Office of Management and Budget's annual request for assurance that Missions have fulfilled the requirements of the Prompt Payment Act. As a result of this review, the Mission is revising its policies and procedures to conform to the computerized Automated Voucher Tracking System implemented in February, 1991.

USAID/Sri Lanka monitored its financial pipeline to ensure that unneeded funds were not held in reserve. Unliquidated balances were limited to only those funds which were expected to be committed in the near future, as required by Handbook 19, Chapter 2. For 5 of the 7 projects tested, the pipeline was reduced by approximately 51 percent over the last 2 years from \$22.6 million at March 31, 1990 to \$11.1 million at March 31, 1992. Obligations were also reduced from \$25.5 million to \$17.7 million over the same period—a 31 percent reduction.

The USAID/Sri Lanka Controller made certifications on year-end "U-101"<sup>1</sup> reports in accordance with A.I.D. Handbook 19, Chapter 2. All year-end "U-101" reports as of September 30, 1991 showed that the Mission had complied with Handbook requirements by ensuring that all reports were certified by the Mission Controller. Also, 25 commitments (\$10.2 million) and 6 de-commitments (\$2.3 million)—selected from a universe of 160 and 106, respectively—were valid and supported by Project Implementation Letters. These transactions conformed to a provision under Section 1311 of the Supplemental Appropriations Act, 1955 [31 U.S.C. 1501] which stipulates that obligations should be recorded only when supported by documentary evidence.

As discussed above, USAID/Sri Lanka followed A.I.D. procedures to control and account for funds; however, some minor errors were noted during testing which we communicated to the Mission separately.

---

<sup>1</sup> "Summary of Budget Allowance Ledger Transactions and Reconciliation With Disbursing Officer's Accounts"

# REPORT ON INTERNAL CONTROLS

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

We made the audit in accordance with generally accepted government auditing standards, which requires us to:

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

Our assessment of internal controls, which included obtaining a representation letter from USAID/Sri Lanka's management confirming in writing information which we considered essential to our assessment, was limited to controls applicable to the audit objectives and not to provide assurance on the overall internal control structure of A.I.D. or the Mission.

For the purposes of this report, we have classified the significant internal control policies and procedures applicable to each audit objective by categories. For each category, we gained an understanding of the design of relevant policies and procedures and determined whether these policies and procedures have been placed in operation—and we assessed control risk. We have reported these categories as well as any significant weaknesses under the applicable section heading for each audit objective.

## **General Background on Internal Controls**

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

The objectives of internal controls for United States Government foreign assistance 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 are 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.

### **Conclusion for Audit Objective One**

The first audit objective was to determine whether USAID/Sri Lanka followed A.I.D. procedures in planning for Fixed Amount Reimbursement construction activities. In planning and making the audit, we considered the applicable internal control policies and procedures cited in A.I.D. Handbooks 1 and 3. For the purpose of this report, we have classified those policies and procedures into the following categories:

- The process for assessing the capabilities of host government agencies prior to selecting the use of Fixed Amount Reimbursement financing;
- The process for communicating Fixed Amount Reimbursement terms and conditions to the host government; and
- The process for reviewing and approving cost estimates submitted by the host government.

Our tests showed that A.I.D. controls were consistently applied.

### **Conclusion for Audit Objective Two**

The second audit objective was to determine whether USAID/Sri Lanka followed A.I.D. procedures in monitoring construction activities. In planning and making the audit, we considered the applicable internal control policies and procedures cited in A.I.D. Handbook 3. For the purpose of this report, we have classified those policies and procedures into the following categories:

- The process for making and documenting site visits;

- The process for preparing Project Implementation Reports;
- The process for monitoring construction progress;
- The process for overseeing the host government agencies' monitoring of contract implementation; and
- The process for evaluating projects.

Our tests showed that USAID/Sri Lanka consistently applied the A.I.D. procedures except for ensuring that A.I.D.-finance construction was used as intended and for ensuring compliance with requirements for publicizing United States participation of construction sites.

### **Conclusion for Audit Objective Three**

The third audit objective was to determine whether USAID/Sri Lanka followed A.I.D. policies and procedures to pay for construction activities, and control and account for construction services funds. In planning and making the audit, we considered the applicable internal control policies and procedures cited in A.I.D. Handbook 19 and Chapter 5 of the Mission Controller's Handbook. For the purposes of this report, we have classified those policies and procedures into the following categories:

- The process for examining, administratively approving and certifying vouchers for payment;
- The process for tracking vouchers to ensure timely payment; and
- The process for committing funds.

Our tests showed that the Mission consistently applied A.I.D. procedures.

### **Reporting Under Federal Managers' Financial Integrity Act**

USAID/Sri Lanka did not report on any of the internal control weaknesses identified in this report. Recommendations to correct the internal control weaknesses are contained in the findings section of this report.

# REPORT ON COMPLIANCE

## **Scope of Our Compliance Assessment**

We made the audit in accordance with generally accepted government auditing standards which require us to assess compliance with applicable laws and regulations when necessary to satisfy the audit objectives.

We tested USAID/Sri Lanka's compliance with: (1) A.I.D. Handbook 1, Supplement B provisions relating to the Fixed Amount Reimbursement method of financing; (2) provisions of A.I.D. Handbook 1, Supplement B and Section 641 of the Foreign Assistance Act relating to the identification of A.I.D. programs as American aid; (3) Section 1311 of the Supplemental Appropriations Act, 1955 [31 U.S.C. 1501] governing the recording of obligations; and (4) Section 611 (e) of the Foreign Assistance Act, as they could affect our audit objectives. As part of our assessment, we obtained a representation letter from USAID/Sri Lanka's management, confirming in writing information considered essential to our compliance assessment. However, the audit objectives were not to provide a conclusion on overall compliance with laws and regulations.

## **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 entity conduct. Not following internal control policies and procedures in the A.I.D. Handbooks generally does not fit into this definition of noncompliance, and is included in our report on internal controls. Abuse is distinguished from noncompliance, in that abusive conditions may not directly violate laws or regulations. Abusive activities may be within the letter of laws and regulations but violate either their spirit or the more general standards of impartial and ethical behavior.

Compliance with: (1) A.I.D. Handbook 1, Supplement B provisions relating to the Fixed Amount Reimbursement method of financing; (2) provisions of A.I.D. Handbook 1, Supplement B and Section 641 of the Foreign Assistance Act relating to the identification of A.I.D. programs as American aid; (3) Section 1311 of the Supplemental Appropriations Act, 1955 [31 U.S.C. 1501] governing the recording of obligations; and (4) Section 611 (e) of the Foreign Assistance Act, as applicable to A.I.D.-financed construction activities in Sri Lanka, is the overall responsibility of USAID/Sri Lanka management.

### **Conclusions on Compliance**

The results of our tests of compliance disclosed the following significant instance of noncompliance:

- USAID/Sri Lanka did not ensure that construction sites contained signs publicizing the American aid (page 12).

Except as described, the results of our tests of compliance indicate that USAID/Sri Lanka complied in all significant respects with: (1) A.I.D. Handbook 1, Supplement B provisions relating to the Fixed Amount Reimbursement method of financing; (2) provisions of A.I.D. Handbook 1, Supplement B and Section 641 of the Foreign Assistance Act relating to the identification of A.I.D. programs as American aid; (3) Section 1311 of the Supplemental Appropriations Act, 1955 [31 U.S.C. 1501] governing the recording of obligations; and (4) Section 611 (e) of the Foreign Assistance Act.

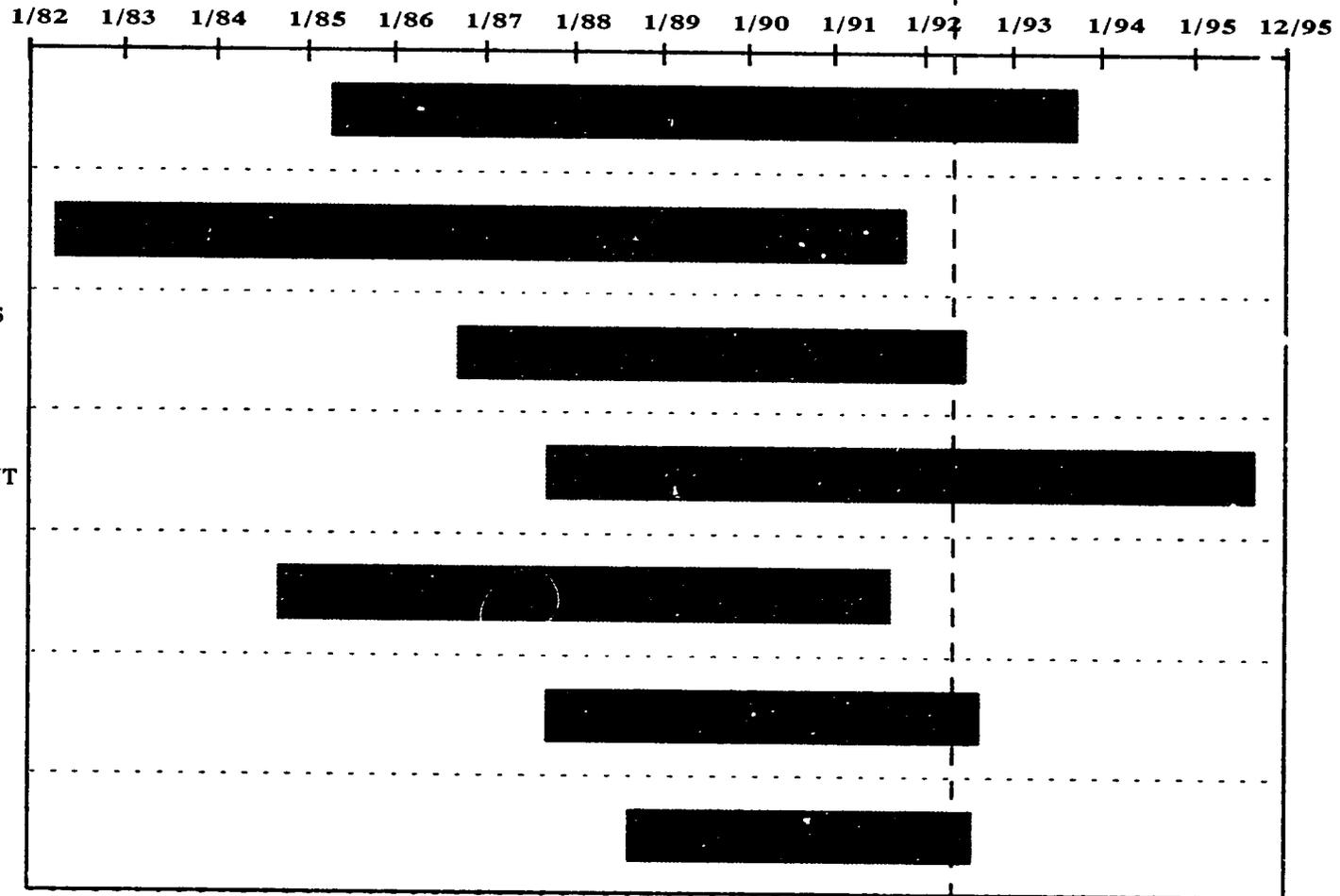
---

# USAID/Sri Lanka Construction Projects

## Schedule of Project Duration

Audit date  
March 31, 1992

**PROJECT**



\*\* Project suspended due to civil conflict.

■ Duration of Project

EXHIBIT I

42 -

## SCOPE AND METHODOLOGY

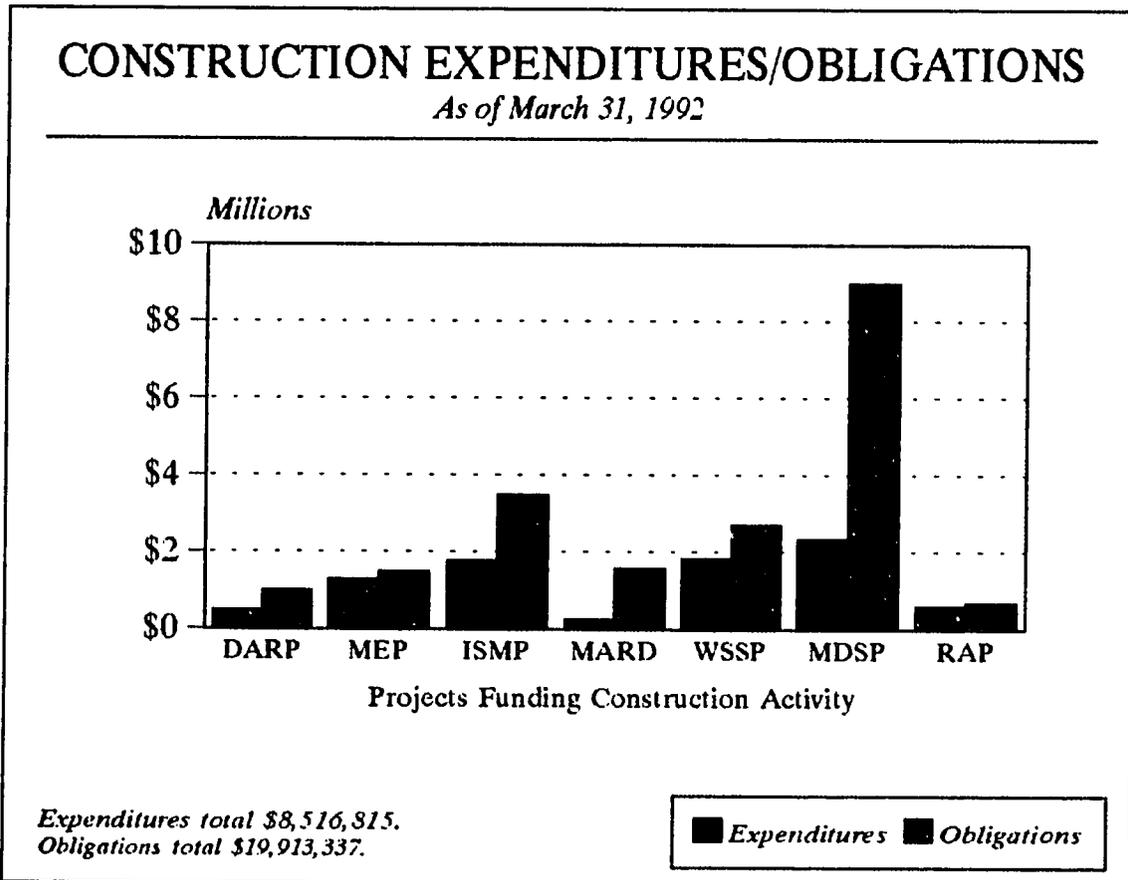
---

### **Scope**

We audited USAID/Sri Lanka's management of A.I.D.-funded construction activities in accordance with generally accepted government auditing standards. The audit was made between March 2, 1992 and July 10, 1992, and covered the systems and procedures relating to construction activities financed by A.I.D. as of March 31, 1992. We did our field work in the Colombo offices of the Mission and the Sri Lankan Government's Department of Wildlife Conservation, and three Government field offices of: (1) the National Water Supply and Drainage Board, (2) the Deputy Director of Irrigation, and (3) the Department of Wildlife Conservation. In addition, we made field trips to 8 project sites located in the regions of Kandy, Polonnaruwa, and Anuradhapura, and 3 irrigation schemes located in the region of Polonnaruwa. We interviewed Mission and host country officials and reviewed applicable Mission records.

The scope of the audit included all A.I.D.-funded bilateral projects in USAID/Sri Lanka's portfolio which contain a component for construction activity. We included in our audit universe all projects active as of March 31, 1992. Based on the fact that the Fixed Amount Reimbursement method of financing is used and that the Sri Lankan Government is therefore responsible for the procurement of all construction contracts, a review of contract procurement was not relevant to our audit. We audited the applicable construction-related systems for planning, monitoring and accounting. The audit objectives did not cover planning procedures for construction activities paid through direct reimbursement since these activities represent only a small proportion of the construction program. We reviewed USAID/Sri Lanka's procedures for planning construction activities which were financed entirely by the Fixed Amount Reimbursement method. As of March 31, 1992, A.I.D. had expended \$8,516,815 for construction activities as illustrated in the following chart:

1  
12



*DARP: Diversified Agricultural Research Project; MEP: Mahaweli Environment Project; ISMP: Irrigation Systems Management Project; MARD: Mahaweli Agriculture & Rural Development Project; WSSP: Water Supply & Sanitation Project; MDSP: Mahaweli Downstream Supply Project; RAP: Rehabilitation Assistance Project*

In addition to the methodology described in the following section for each audit objective, we obtained a representation letter from USAID/Sri Lanka's management confirming in writing, information that we considered essential for answering our audit objectives and for assessing internal controls and compliance. At the request of the USAID/Sri Lanka Director, these representations are included as part of the Mission comments attached to this report as Appendix II.

## **Methodology**

The methodology for each audit objective follows.

### **Audit Objective One**

The first objective was to determine whether USAID/Sri Lanka followed applicable procedures in planning for Fixed Amount Reimbursement construction activities. To accomplish this objective, we applied A.I.D. Handbook 1, Supplement B, Chapter 20, and A.I.D. Handbook 3, Appendix 3J (Use of Fixed Amount Reimbursement Method for Local Cost Financing), and guidance provided by the Asia Bureau in 1990. To answer this objective, we reviewed all seven projects under audit: (1) Diversified Agricultural Research Project, (2) Mahaweli Environment Project, (3) Irrigation Systems Management Project, (4) Mahaweli Agriculture and Rural Development Project, (5) Water Supply and Sanitation Project, (6) Mahaweli Downstream Supply Project, and (7) Rehabilitation Assistance Project.

To determine if USAID/Sri Lanka ensured that the Sri Lankan Government agencies were capable of fulfilling contracting responsibilities required under the Fixed Amount Reimbursement method, we reviewed all the host government capability assessments completed to date and held discussions with personnel of the Controller's Office. The reviews included a Project Design Report and a Financial and Managerial Assessment carried out at the project design stage of one project (these were the only reports which could be located for assessments carried out at the project design stage), seven assessments—one for each project—prepared by a management consulting firm in late 1989, and all the financial reviews done by financial analysts in the Controller's office.

We reviewed the Project Papers for each of the seven projects to verify the inclusion of: (1) an Administrative Analysis, (2) approved cost estimates for the construction components, and (3) USAID/Sri Lanka Director's Certification that the host government has the financial capability and human resources to use effectively the projects (Section 611 (e) of the Foreign Assistance Act of 1961).

We examined applicable Project Implementation Letters defining the Fixed Amount Reimbursement terms and conditions for all seven projects. We reviewed the Letters to verify the inclusion of: (1) a definition of the mechanics of using Fixed Amount Reimbursement as described in A.I.D. Handbook 3, Appendix 3J; (2) an established level of A.I.D. financing to the project; (3) a statement of approval of the construction design plans, specifications, and cost estimates; and (4) a statement of the risks involved in using the Fixed Amount Reimbursement method of financing.

We reviewed USAID/Sri Lanka's Internal Control Assessments for fiscal years 1989, 1990, and 1991 and tested the validity of the Mission's assertions about the host government agency's contract and contract management capabilities.

A comparative analysis of the host government capability assessments and subsequent project evaluations was done to determine if the evaluations identified weaknesses in the host government agencies' ability to carry out contracting activities. For weaknesses identified, we reviewed the assessments to determine if such weaknesses were included in those documents. If such weaknesses were identified, we then determined what actions USAID/Sri Lanka took to overcome the weaknesses.

### **Audit Objective Two**

The second objective was to determine whether USAID/Sri Lanka followed applicable procedures for monitoring construction activities. To accomplish this objective, we applied A.I.D. Handbook 3, Chapter 11 and Appendix 3J. We interviewed Mission Officials and reviewed project files for 3 of the 7 projects under audit. These three projects are: (1) Water Supply and Sanitation Project, (2) Mahaweli Environment Project, and (3) Irrigation System Management Project.

To determine compliance with Section 11-C, which requires the monitoring of construction activities, we interviewed Mission officials and examined 98 documents for evidence of monitoring. To determine compliance with Section 11E, we interviewed Mission, host government and contractor officials and randomly selected the minutes of nine meetings held between 1989 and 1992.

28

We reviewed Project Papers, Project Implementation Letters, project agreements, and contracts for the three projects to determine if these documents identified reporting criteria as required by Section 11E. We randomly selected 17 host government and contractor progress reports and reviews between 1989 and 1992 to determine if the reporting requirements were adhered to.

We interviewed Mission officials and examined Mission guidance on site visits to determine adherence to Section 11E and Appendix 3J. We randomly selected six site visit reports from 1988 to 1991 to determine compliance with Appendix 11E and 11C.

We discussed USAID/Sri Lanka's Project Implementation Reporting system with Mission Officials and reviewed four reports randomly selected from 1991 and 1992 to verify compliance with Chapter 11, Section F of Handbook 3.

We also made field trips to 8 facilities sites and 3 irrigation schemes under 3 projects. We chose these three projects for site visits because they represented the largest percentages of construction expenditures, and construction activity was located in areas considered reasonably safe for travel. The specific sites contained a variety of building types and both completed and uncompleted construction.

All 8 evaluation reports were obtained and reviewed for the 7 projects to determine if these evaluations were done as scheduled in Project Papers and USAID/Sri Lanka annual Evaluation Plans. In the three instances where evaluations were not done as scheduled, we verified that justification existed in Mission files. We discussed with the Evaluation Officer the results of the evaluations, and the Mission's follow-up and reporting system for implementing recommendations made in the evaluations.

For the sites we visited, we examined four final inspection reports to determine if they were in compliance with Handbook 3. These reports were randomly chosen from inspection reports on the 11 sites that we visited.

**Audit Objective Three**

The third objective was to determine whether USAID/Sri Lanka followed A.I.D. policies and procedures to pay for construction activities, and control and account for construction services funds. To accomplish this objective, we applied A.I.D. Handbook 19 and the Mission Controller's Handbook. We interviewed Mission staff to gain an understanding of the Mission's accounting system and procedures for following A.I.D. policies and procedures.

To test this system for conformance with A.I.D. procedures, we selected 24 vouchers from a universe of 154 vouchers (Form SF 1034) representing \$3,969,750 of \$5,600,920 expended for construction. We made tests to verify that each voucher was examined, administratively approved, and certified in accordance with agency procedures. We also confirmed that the Controller certified the year-end "U-101" reports as required by A.I.D. Handbook 19, Chapter 2.

Finally, we tested 25 commitments (\$10.2 million) and 6 de-commitments (\$2.3 million)—selected from a universe of 160 and 106, respectively—to determine whether they were valid and supported by the required Project Implementation Letters which documented the amounts and reasons for the underlying commitments. We also determined whether these transactions conformed to a provision under Section 1311 of the Supplemental Appropriations Act, 1955 [31 U.S.C. 1501] which stipulates that obligations should be recorded only when supported by documentary evidence.

---



UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT  
MISSION TO SRI LANKA  
COLOMBO (ID)  
Washington D.C. 20521-6100

December 14, 1992

James Durnil  
RIG/A/S  
#17-03 Peninsula Plaza  
111, North Bridge Road  
Singapore 0617

Response to Draft Audit Report of USAID/Sri Lanka's  
Management of Construction

Dear Jim:

I refer to your letter dated November 20, 1992, enclosing a copy of the subject draft audit report. I thank you for the assistance and cooperation of your staff in completing the audit of USAID/Sri Lanka's Management of AID-funded Construction in Sri Lanka.

We are pleased that the audit team found that USAID/Sri Lanka's management of project-funded construction activities fully complied with AID procedures for planning for Fixed Amount Reimbursement construction activities and also for paying for construction activities and controlling accounting for construction service funds.

Furthermore, with the exception of only two deficiencies noted in the report, the audit helped to confirm the effectiveness of the Mission's management and monitoring of construction activities. In light of the disparate, rural and in many cases remote, locations of USAID construction activities, we are pleased with the positive findings of this audit. The Mission, particularly the project officers and the Mission engineers, have worked hard to ensure A.I.D. rules and regulations are followed and documented.

I have accepted RIG/Singapore's two audit recommendations, and the Mission is already taking actions (described below) aimed at closing both recommendations as soon as possible. However, I believe it is useful to more fully describe the context within which these recommendations were made.

The draft audit's finding that "USAID did not ensure that the Government of Sri Lanka (GSL) used the financed buildings" referred specifically to the Mahaweli Environment Project (MEP). As noted by the auditors, USAID/Sri Lanka had been actively engaged with the GSL to staff these facilities. It was our management decision to proceed with construction on the basis of

3/1

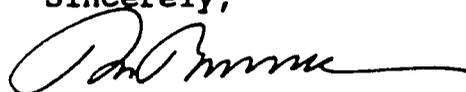
overall MEP investment in national parks. This decision also continued our leverage (in addition to our ongoing NAREP Project) to staff the parks. Based upon the progress we have been able to make, which is described below, we still think this premise was sound.

I would also like to make a comment with respect to the draft audit finding that "U.S. Assistance was not fully publicized." I would like to clearly state that it has always been the policy of Mission management to fully publicize AID-financed activities through signboards, plaques, official openings, newspapers, and electronic media. USAID/Sri Lanka's success in publicizing U.S. projects has been quite significant and in particular, our newspaper coverage has been remarkable. Over the last twelve months, we have also given special attention to ensuring that all AID-financed commodities are fully marked. The marking of all construction sites will fully meet our Mission standards by the end of January 1993.

With respect to the audit, I have also attached my representation letter, as requested by you.

I look forward to receiving your final audit report. I trust that the information contained in this letter and attachment will assist you in finalizing your report.

Sincerely,



Richard M. Brown  
Director

Enc: As stated.

## MISSION RESPONSE TO SPECIFIC RECOMMENDATIONS

### Audit Finding 1: A.I.D.-Financed Buildings Were Unused

The Mahaweli Environment Project (MEP), which provided the GSL with the resources to mitigate the negative environmental impact of a \$2 billion resettlement and water development program, was a major success. With MEP project assistance, the GSL established, demarcated, and developed 6 parks covering 220,000 hectares which now provide protection for the country's numerous and diverse endangered flora and fauna. The AID-financed construction of wildlife management facilities and staff housing was an essential element to maintain and further build on the MEP investments. Without these facilities in place, the GSL would have lacked the physical basis to undertake its field programs and safeguard the protected habitat established by the project. For this reason, USAID placed a premium on completion of construction by the end of the project.

As documented in the project files, the original construction schedule of MEP was significantly delayed. In part, this was due to security problems which broke out in Sri Lanka in late 1989. Another reason was that the Department of Wildlife Conservation (DWLC) only assumed full control over the project in 1988. This organization, which was a major factor in the institutional success of the project, committed itself to construction of the buildings under MEP. But due to normal challenges confronting a new institution and to the remote locations of the facilities, a major portion (41 of 52) of the buildings were actually only completed during the last couple of months of the project. This puts some perspective on the relatively short time (in relation to the overall life of project) that the buildings have been available for staffing. Although the staffing delays experienced under MEP have been longer than we had wished, USAID has never felt any long-term risk that the buildings would remain unutilized. Over the life of the project, the DWLC (with substantial USAID support) was able to increase its staff by 135 positions despite general reductions of staff throughout the GSL and tight IMF restrictions on new positions. Our current issues concern staff re-deployment to the project sites and, in some cases upgrading of skills that can be provided through short courses.

As documented in attachments hereto, substantial progress has been made in the last six months. The DWLC is fully committed to the utilization of all MEP buildings, and it considers the USAID-funded facilities essential to the success of its training and park management programs. USAID is now supporting many of these programs under its \$12 million Natural Resources and Environmental Policy (NAREP) project. USAID therefore has an ongoing interest and substantial leverage with respect to the organizational capabilities of the DWLC, including staff development, and the full utilization of existing resources to achieve the DWLC's objectives. We monitor the MEP construction

33

as part of our NAREP project activities, and we are confident that we will be able to follow up on the actions proposed below, in response to the draft audit recommendations.

**Recommendation 1.1: Determine how many of the 55 A.I.D.-financed buildings have not been used effectively as required by the project agreement for the Mahaweli Environment Project.**

**Recommendation 1.2: Obtain a refund from the Sri Lankan Government for the cost of all buildings not used effectively unless the Sri Lankan Government provides the agreed-upon staff and uses the buildings within a specified time.**

**Recommendation 1.3: Make a determination on whether to report on the Mission's failure to ensure the proper use of A.I.D. financed construction as an internal control weakness in the next report required under the Federal Manager's Financial Integrity Act.**

The USAID project manager made unannounced site inspections of all MEP-financed buildings during October 26 - 28. His findings are presented in his site inspection report (Annex A to this memorandum).

The results of this inspection are:

- \* A.I.D. financed 52, not 55, buildings under MEP. Funding for the other three buildings was de-earmarked and de-committed because of problems with their completion, due to proximity to sensitive security areas.
  
- \* Of the remaining 52 buildings, 40 are currently deemed properly occupied and utilized by Department of Wildlife Conservation (DWLC) staff. The DWLC has made good progress in utilizing these buildings over the past six months. For example, the DWLC has begun a series of park ranger/game guard training programs at the Giritale Training Center. One of these programs was inaugurated on November 28th and attended by the USAID project manager.

DWLC's planned training programs for the year 1993 are attached to this memorandum as Annex B. Photos of the inauguration ceremony and of some of the buildings which are now being used at the Giritale Training Center are enclosed.

Another reason for the progress made by the DWLC in utilizing these buildings has been the reassignment of staff. For example, the DWLC's Range Office, which previously had functioned out of borrowed buildings at

Sigiriya, was moved to Ambagaswewa in June 1992, while other office staff was transferred from Sigiriya to Polettewa and Angamedilla.

- \* 6 of the 52 buildings are occupied by DWLC staff who are involved in park management and development, but whose skills need some upgrading. USAID is negotiating with the DWLC to upgrade these staff positions through a combination of training and redeployment of staff. The DWLC has agreed to submit a timetable to USAID by December 31, 1992, for the upgrading of this staff. After this staff upgrading takes place, these buildings will be deemed fully utilized.
- \* 6 of the 52 buildings are deemed unutilized. Of these, 3 buildings cannot be occupied at this time, because of security reasons that were not apparent at the time of their construction in 1988.

The DWLC has agreed to include their staffing plan for the remaining 3 buildings in the same timetable by December 31, 1992.

USAID recommends the following actions to bring this recommendation to a successful closure:

1. By December 31, 1992, the DWLC will submit a written, four-month timetable and strategy to USAID for the staffing of the remaining 12 buildings.
2. During the following four months, USAID will conduct unannounced inspections of MEP buildings to confirm that they are being properly utilized and to report on progress for those 12 buildings that are not fully utilized as of the date of this response.
3. At the end of this four-month period, USAID will do an unannounced final inspection to confirm the status of all MEP buildings.

4. For any MEP building that is un(der)utilized at the end of this four-month period, for other than security reasons, USAID will issue a bill of collection for the USAID contribution to the construction cost of that building.
5. For any MEP building unutilized because of security reasons after a six-month period, USAID will either: A) Issue a bill of collection for those buildings; or B) Extend the period to staff those buildings if the security situation remains unsettled but appears to be improving.

Based on the actions taken/planned provided, we request that recommendation 1.1 and 1.2 be resolved and considered closed once evidence is provided of the actions taken which are outlined above.

With regard to recommendation 1.3, USAID has been monitoring the effective use of facilities constructed under the Mahaweli Environment Project. However, due to the reasons given above, there were time lags between construction and full utilization. USAID does not consider these delays as a failure on the part of USAID management system, and as such does not consider it significant to be reported as an Internal Control Weakness in the next report required under the Federal Manager's Financial Integrity Act. Therefore, USAID requests that recommendation No. 1.3 be resolved and closed with the issuance of this report.

Audit Finding 2: U.S. Assistance Was Not Fully Publicized

**Recommendation 2.1: Ensure that the Sri Lankan Government posts signs or plaques at all A.I.D.-financed construction sites identifying United States participation in the project.**

**Recommendation 2.2: Require site visit reports to identify whether or not construction sites are publicized as required by A.I.D. Handbook 1, Supplement B, Chapter 22.**

**Recommendation 2.3: Make a determination on whether to report on the Mission's failure to monitor the posting of signs or plaques at A.I.D. financed construction sites as an internal control weakness in the next report required under the Federal Manager's Financial Integrity Act.**

Mahaweli Environment Project

As part of the USAID project manager's unannounced site inspection referred to above, his report documents the following finding:

- \* 24 buildings have already been marked with the AID plaque,

including all 15 at the Giritale Training Center. Many of the photos taken at the course inauguration show buildings properly marked with plaques.

The USAID project manager has received a verbal assurance from the DWLC that all MEP buildings will be marked with the A.I.D. plaque by December 20, 1992. Also, all sites with more than 3 buildings will be indicated with a signboard showing that the buildings were constructed with the assistance of A.I.D.

#### Water Supply & Sanitation Project

The National Water Supply & Drainage Board (NWSDB) has installed the AID plaque signboards on eight buildings funded under the USAID project. Annex C to this memorandum is a letter from NWSDB which states that they have completed installing these plaque and signboards on AID-funded buildings. Annex C 1 shows the status of installation of these plaques at the various locations. Installing plaques in the remaining 3 buildings will be completed by December 31, 1992. The AID project manager will carry out an unannounced inspection in January 1993, to verify that all AID funded buildings have the required AID emblem in place.

USAID recommends the following actions to bring this recommendation to a successful closure:

- A. During the four-month timetable for the DWLC to comply with its commitment to fully utilize MEP buildings, the USAID project manager will confirm the installation of plaques and signboards during one of his unannounced inspection visits.
- B. The USAID project manager will carry out unannounced inspections to confirm the installation of plaques/signboards on all AID-funded buildings.
- C. USAID/Sri Lanka will issue instructions to project managers requiring site visit reports to identify whether or not construction sites are publicized, and, if not, to take corrective action.

Based upon this response, we request that recommendation 2.1 and 2.2 be resolved and considered closed upon submission of evidence from the project officers that the required plaques/signboards have been installed.

With regard to recommendation 2.3, at the time of the next report required under the Federal Manager's Financial Integrity Act, USAID will make a determination whether to report on the USAID's failure to monitor posting of signs or plaques at AID financed construction sites as a material internal control weakness. Based on this we request that recommendation 2.3 be resolved and closed.

Based on all the preceding comments, we suggest that the wording (".. and did not enforce a condition precedent dealing with the staffing issue") in the last paragraph on page (ii) of the Executive Summary be changed, as USAID/Sri Lanka was enforcing the condition precedent (as noted above 135 new positions were created) by continuing a dialogue with the GSL on this staffing issue.

As discussed with RIG/Singapore on November 19, 1992, USAID/Sri Lanka further sub-divided the Fixed Amount Reimbursement System for the Mahaweli Downstream Support Project in September 1992. This action taken on the recommendation of consultants who were helping to verify GSL reimbursement claims further refined the FAR system we were using, and did not alter USAID's original cost estimates. As agreed per telecon with RIG/Singapore, this does not alter any of the findings of the audit.



UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT

MISSION TO SRI LANKA.

P.O. Box 106, Colombo, Sri Lanka.

Telephone: 574333, Fax No: 574264

APPENDIX II

Page 9 of 10

January 19, 1993

Mr. James Durnil  
Regional Inspector General/Audit  
Singapore

Re: **Audit of USAID Sri Lanka's Management of AID-Funded Construction**

Dear Jim:

You have asked for a Representation Letter in connection with your audit of USAID/Sri Lanka's Management of AID Funded Construction. Your staff has informed us that the audit covered the Mission's management of construction activities in seven projects that were active as of March 31, 1992 and was intended to answer the following audit objectives:

(A) Did USAID/Sri Lanka follow AID procedures in planning Fixed Amount Reimbursement construction activities?

(B) Did USAID/Sri Lanka follow AID procedures in monitoring construction activities?

(C) Did USAID/Sri Lanka follow AID policies and procedures in 1) paying for construction activities, and 2) controlling and accounting for construction services funds?

For the activities under audit during the audit period, USAID/Sri Lanka is responsible for the internal control system, for compliance with applicable U.S. laws, regulations, and for compliance by the host government with Fixed Amount Reimbursement Agreements for the fairness and accuracy of the Mission's accounting and management information.

I asked appropriate members of my staff, particularly those in the Controller's office and projects office, and others, to make available to you all records in our possession for the purpose of the audit. The seven projects your staff identified as the base for the audit are numbered 383-0058, 0075, 0080, 0086, 0088, 0103, and 0107.

231

Based on representations made to me by my staff and their written concurrence with the representations made in this letter, and in reliance on your office which has not informed me of any difficulty in obtaining records or information, or of any difficulty in obtaining the full cooperation of the various offices and staff involved, I confirm, as a layman and not as a lawyer, the following representations with respect to the subject matter of the audit and the audit objectives:

(1) To the best of my knowledge and belief, USAID/Sri Lanka has made available to your staff all mission records relating to the audit objectives;

(2) To the best of my knowledge and belief, the records relating to the audit objectives are accurate and complete and constitute a fair representation of the status of the matter under audit.

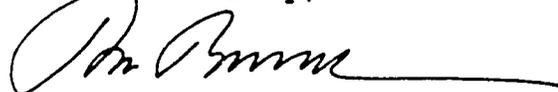
(3) To the best of my knowledge and belief, USAID/Sri Lanka is not aware of any material instances where financial or management information on matters directly relating to this audit has not been properly and accurately recorded and reported, other than in any findings that may be in the audit report.

(4) To the best of my knowledge and belief, USAID/Sri Lanka has disclosed any known material irregularities related to the subject matter of the audit that we consider substantive involving Mission employees with internal control responsibilities for the matter under audit.

(5) To the best of my knowledge and belief, as a layman and not as a lawyer, USAID/Sri Lanka has reported all known instances which, in the Mission's judgment, would evidence material noncompliance with AID policies, and Fixed Amount Reimbursement Agreements procedures or violations of U.S. laws and regulations.

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

Yours sincerely,



Richard M. Brown  
Director

## APPENDIX III

### REPORT DISTRIBUTION

	<u>No. of Copies</u>
U.S. Ambassador to Sri Lanka	1
Mission Director, USAID/Sri Lanka	5
Assistant Administrator for Asia (AA/Asia Bureau)	1
Sri Lanka Desk Officer	1
Asia/FPM	1
Office of Press Relations (XA/PR)	1
Bureau for Legislative Affairs (LEG)	1
Office of the General Counsel (GC)	1
Associate Administrator for Operations (AA/OPS)	1
Associate Administrator for Finance and Administration (AA/FA)	1
Office of Financial Management (FA/FM)	1
POL/CDIE/DI, Acquisitions	1
FA/MCS	2
FA/FM/FPS	2
Inspector General (IG)	1
Assistant Inspector General/Audit (AIG/A)	1
Deputy Inspector General/Audit (D/AIG/A)	1
IG/A/PPO	3
IG/LC	1
IG/RM	12
Assistant Inspector General for Investigations/Singapore Field Office (IG/I/SFO)	1
Regional Inspector General for Investigations/Singapore (RIG/I/S)	1
RIG/A/Cairo	1
RIG/A/Dakar	1
RAO/Manila	1
RIG/A/Nairobi	1
RIG/A/Tegucigalpa	1
RIG/A/Vienna	1
RIG/A/Europe	1
IG/A/FA	1
IG/A/PSA	1

41-