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Regional Inspector General for Audit  
Cairo, Egypt

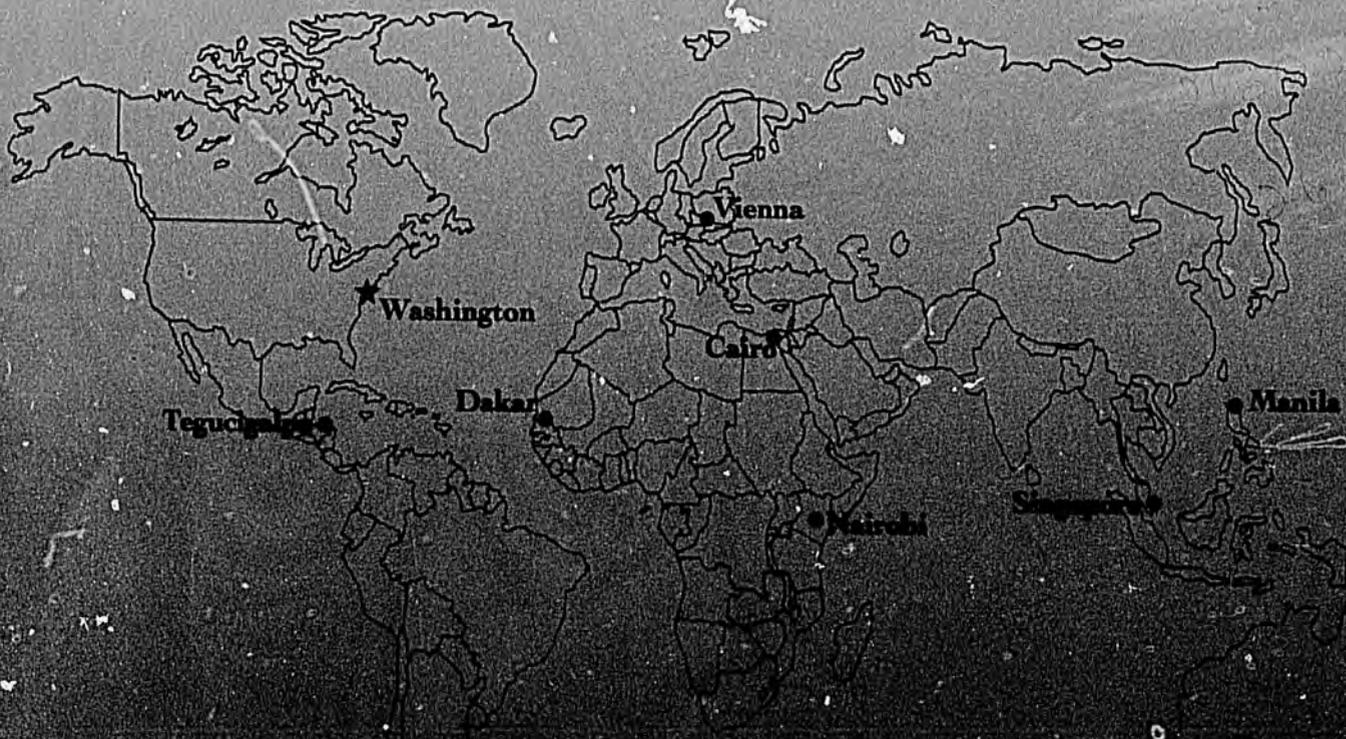
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**Audit of Commodity Assistance Furnished under  
USAID/Egypt Agriculture Projects**

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**Report No. 6-263-93-08  
May 13, 1993**



U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT



**UNITED STATES OF AMERICA  
AGENCY FOR INTERNATIONAL DEVELOPMENT  
OFFICE OF THE REGIONAL INSPECTOR GENERAL/AUDIT**

May 13, 1993

**MEMORANDUM FOR D/USAID/Egypt, Henry H. Bassford**

**FROM :** RIG/A/Cairo, *Philippe L. Darcy*

**SUBJECT:** Audit of Commodity Assistance Furnished under USAID/Egypt Agriculture Projects

Enclosed are ten copies of the subject audit report. We received the Mission's comments on a draft of the report and your written representation regarding the audited activities and have included them in Appendix II to the report. Representations were limited with regard to an essential confirmation and, in accordance with A.I.D./Washington guidance, mission staff directly responsible for the audited activities did not provide written representations to you or us regarding these activities. Thus, our answers to the audit objectives are qualified.

The report contains one recommendation. The recommendation has been resolved and will be closed upon receipt of an acceptable signed contract and scope of work for end-use checks of project commodities monitored through the Directorate of Agriculture Resources.

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

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# EXECUTIVE SUMMARY

## Background

A.I.D. finances the purchase of commodities (materials, articles, supplies, goods and/or equipment) to help achieve the goals and objectives of projects and programs in developing countries. As of September 30, 1992, USAID/Egypt had procured about \$52 million of commodities to expand the irrigation networks, improve water management and crop production and provide research equipment and facilities for the Egyptian people.

To protect this investment in commodities, USAID/Egypt must ensure that the need for the commodities is established, commodities are received, commodity inventory records are maintained, and commodities are properly used to further project objectives. If the Mission does not ensure these actions are taken, the probability increases that the commodities will be stolen, lost, damaged, unused or remain idle for long periods of time.

The Office of the Inspector General, Cairo, Egypt conducted the audit answer the following questions:

1. Did USAID/Egypt develop and review the Irrigation and Production Credit projects commodity needs as required by A.I.D.'s policies and procedures?
2. Did USAID/Egypt monitor the Irrigation and Production Credit projects to ensure that A.I.D.-financed commodities met A.I.D.'s source/origin requirements and were received and used in accordance with A.I.D.'s policies and procedures?

The Director USAID/Egypt provided us with written representations covering Mission responsibilities, full and accurate disclosure of financial and management information, compliance with contractual agreements and other matters (The complete representation is contained in Appendix II of this report). The Director limited his representations to those which should be contained in the records under audit with regards to instances of irregularities, noncompliance and or violations of laws and regulations. Also, in accordance with A.I.D./W guidance, the Mission policy is that only the Director, not the officials directly responsible for the activities under audit, will provide written representations. (See Appendix I Scope and Methodology.) As a result of these limitations, our answers to the audit objectives are qualified.

## **Audit Findings**

We found that USAID/Egypt had established the needs for commodities. These needs were reflected in the procurement plans used to procure commodities, and the plans were amended as the needs changed. (See page 4.)

The Mission made sure that commodities purchased met the source/origin requirements. When commodities which did not meet the requirements had to be purchased, waivers were obtained. In addition, the Mission had effectively monitored the receipt of commodities. However, the Mission did not effectively review commodities to ensure they were properly used to further project objectives, i.e., the Mission did not conduct end-use reviews of commodities. This situation occurred because:

- Mission project officers believed the monitoring being done was adequate;
- Mission project officers thought the host country already had or would assume the responsibility for the reviews; and
- the Mission's proposed plan to strengthen controls over commodities, including end-use reviews, had not been implemented.

Our tests showed that, had end-use reviews been conducted, they would have disclosed: (1) commodities of significant value were missing from the equipment and vehicle monitoring reports, (2) adequate records were not being kept to determine whether vehicles were used for project purposes, (3) costly equipment had not been used for one to two years, and (4) commodities were not at the locations shown in the monitoring office reports. Lack of end-use reviews increases the risk that the \$52 million of commodities purchased by A.I.D. were not used effectively. (See pages 8 - 14.)

To correct the end-use review problem, we recommended that the Mission establish and implement a strategy for conducting periodic end-use reviews. (See page 6.)

*Office of the Inspector General*  
Office of the Inspector General  
May 13, 1993

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# INTRODUCTION

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## Background

A.I.D. finances the purchase of commodities, which are defined in its Handbook 15, (Chapter 12, Regulation 1,) as any material, article, supply, goods, or equipment. Project commodities typically include vehicles, computers, laboratory equipment and many other types of mechanical and technical equipment and supplies purchased to achieve the goals and objectives of its projects and programs. For Egypt, A.I.D. plans to spend approximately \$164 million for commodities for three agricultural projects intended to expand the irrigation network, improve water management and crop production and provide research equipment and facilities—the Irrigation Management Systems Project (herein after referred to as the Irrigation project), the Agricultural Production and Credit Project (herein after referred to as the Production Credit project), and the National Agricultural Research Project (herein after referred to as the Research project). USAID/Egypt's Offices of Irrigation and Land Development, Agricultural Credit and Economics, and Agriculture are responsible for overseeing these projects.

Because A.I.D.-financed commodities are vital to project success, USAID/Egypt should have effective systems to monitor the planning, procurement, receipt and use of those commodities. Among other things, the system to monitor the use of commodities should include independent testing of selected items to ensure that the items are being properly used to achieve project objectives.

The Irrigation project is made up of ten independent but related components which are to assist the Egyptian Government in improving the operating efficiency of the irrigation system in Egypt and to strengthen the Ministry's ( Ministry of Public Works and Water Resources) operational, maintenance and planning capabilities. The Mission treats each component as a project with its own project officer and Egyptian government implementing entity. These components are the equivalent of large A.I.D. projects with obligations ranging from \$6 million to \$76 million.

The Production Credit project seeks to increase Egypt's agricultural productivity through deregulation of crop prices, improved farming technology and funds made available through bank loans for farmers to purchase seed, fertilizer and other farming needs. The greater portion of the funds provided have been cash transfer to support the bank loan program.

As of September 30, 1992, amounts obligated for the three projects and budgeted for commodities were as follows.

<b>Project Name</b>	<b>Obligations (Millions)</b>	<b>Budgeted for Commodities (Millions)</b>	<b>Start Date</b>	<b>End Date</b>
Irrigation Project	\$313	\$95.7	1981	1995
Production Credit Project	\$233	\$5.7	1986	1995
Research Project	\$229	\$62.6	1985	1994
Totals	\$775	\$164.0		

We did not include the Research project in this audit because no significant procurements were made since we audited this project in 1989.

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## **Audit Objectives**

The Office of the Regional Inspector General for Audit/Cairo conducted an audit of commodity assistance furnished under USAID/Egypt's agricultural projects to answer the following objectives:

1. Did USAID/Egypt develop and review the Irrigation and Production Credit projects' commodity needs as required by A.I.D.'s policies and procedures?
2. Did USAID/Egypt monitor the Irrigation and Production Credit projects to ensure that A.I.D.-financed commodities met A.I.D.'s source/origin requirements and were received and used in accordance with A.I.D.'s policies and procedures?

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

# **REPORT OF AUDIT FINDINGS**

USAID/Egypt's Director provided us a written representation that USAID/Egypt is responsible for the internal control system, the fairness and accuracy of the accounting and management information and other matters relating to the audited activities. However, the Director limited his representations to state that the records under audit should contain any instances of irregularities, noncompliance or violations. He did not provide representations as to whether he was aware of any such instances of noncompliance or violations. Also, in accordance with A.I.D./W 1992 guidance, the Mission policy is that only the Director, not the officials directly responsible for the activities under audit, will provide written representations. Because of these limitations, our answers to the audit objectives are qualified to the extent of any effect on the audit findings. (The complete representation is contained in Appendix II to this report.)

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**Did USAID/Egypt develop and review the Irrigation and Production Credit projects' commodity needs as required by A.I.D.'s policies and procedures?**

We found that USAID/Egypt documented project procurement needs in the Irrigation and Production Credit<sup>1</sup> project papers in accordance with A.I.D.'s policies and procedures. The plans were sufficient to establish a budget for planned commodity purchases, but the plans did not have much supporting documentation. However, the project papers provided that A.I.D.-funded technical assistance contractors would later develop detailed procurement plans after assessing project needs. We found that the contractors assessed these needs and developed procurement plans which the Mission approved. The procurements then followed the plans.

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<sup>1</sup> As noted earlier, the Research project was not included in this audit because no significant procurements were made since we audited this project in 1989.

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**Did USAID/Egypt monitor the Irrigation and Production Credit projects to ensure that A.I.D.-financed commodities met A.I.D.'s source/origin requirements and were received and used in accordance with A.I.D.'s policies and procedures?**

USAID/Egypt monitored the Irrigation and Production Credit projects to ensure that A.I.D.-financed commodities met source/origin requirements and were received in accordance with A.I.D. policies and procedures. Regarding whether USAID/Egypt ensured commodities were used as required, although the Mission to some extent monitored the use of commodities by project officers' site visits, progress reports and utilization records, the Mission did not conduct the end-use reviews as required in Mission Order 5-3—reviews we believe are vital to ensuring commodities are used in accordance with A.I.D.'s policies and procedures.

Because of procurement violations by the technical assistance contractor of one of the Irrigation project components, which the Mission identified before we started the audit, we excluded this component from our tests of A.I.D.'s source/origin requirements. However, our tests of project files disclosed that the Mission incorporated A.I.D.'s source/origin requirements in project papers, grant agreements and host country contracts. When justified, waivers were issued. Our tests of commodities received for the two projects,<sup>2</sup> found that the commodities met the source/origin requirements established in the host country contracts.

With regard to receiving commodities, our review of 29 procurement transactions found that the Mission had established adequate monitoring procedures to ensure that such commodities were checked at the port for compliance with contract specifications, quantities, loss and damage. Furthermore, our tests of 249 items (of 1,578 listed in the monitoring report) showed that on arrival at the project site, host country project personnel and technical assistance contractors inspected the commodities to make sure they met contract requirements.

USAID/Egypt project officers told us that they monitored commodities through site visits, review of progress reports, host country personnel and technical assistance contractors. However, we found limited evidence on file to show the extent that commodities were monitored. For example, four of the six project officers did not document site visits. Nevertheless, our interviews with the officers and our work at project sites disclosed that, to varying degrees, they:

- assessed the progress of the project,
- reviewed the receipt and use of commodities,

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<sup>2</sup> The two projects consist of the Production Credit project and five components of the Irrigation project. The Mission treats each component of the Irrigation project as a separate project with its own project officer.

- met with host country and contractor personnel,
- identified and solved problems, and
- ensured problems were successfully resolved during subsequent visits.

However, project officers' monitoring activities did not include the performance of end-use reviews as suggested in Handbook 15 and required by USAID/Egypt Mission Order 5-3.

**Project Officers Did Not Conduct End-Use Reviews of Commodities**

A.I.D. Handbook 15 and Mission Order 5-3 state that project officers have ultimate responsibility for ensuring that A.I.D.-funded commodities are used effectively for project purposes. As part of this responsibility, project officers are to periodically conduct end-use reviews to assess the accuracy and completeness of host country files and accounting records and to test a sample of commodities for proper use. Although the Irrigation and Production Credit projects began in 1981 and 1986, respectively, the project officers had not conducted end-use reviews of project commodities.

These reviews were not conducted in part because Mission project officers believed that routine project monitoring activities included substantial monitoring of end-use, and because they believed that the host country project monitoring office was or would be conducting end-use reviews. Also, certain Mission actions to strengthen controls over project commodities, including end-use reviews, had not yet been implemented. Without end-use reviews, we do not believe the Mission has adequate controls to ensure that commodities procured for the Irrigation and Production Credit projects will be used as required. At the time of this audit, these procurements totalled about \$52 million.

**Recommendation No. 1: We recommend that USAID/Egypt establish and implement a plan to conduct periodic end-use reviews for commodities procured under agriculture projects. This plan should include guidance on how to conduct an acceptable end-use review, a sampling method, and the frequency of such reviews.**

**A.I.D. Handbook 15 and Mission Order 5-3 state that project officers have ultimate responsibility for ensuring that A.I.D.-funded commodities are effectively used for project purposes. Handbook 15, (Chapter 10.D.4) and Mission Order 5-3 advise project officers to periodically assess the accuracy and completeness of host country files and accounting records and to test a sample of commodities to determine if they are being used properly. In assessing host country files and accounting records, the Handbook suggests that the officers:**

- (1) review the Loan/Grant Agreement, Implementation Letters, and prior end-use and audit reports for general background information and to determine whether there are restrictions/conditions regarding usage of the commodities, and whether there are problem areas requiring follow-up; and

- (2) review and compare files and accounting ledgers to determine Host Country Government responsibilities, dollar value, shipping and billing instructions, completeness of shipping documents, accuracy of ledger, and commodity arrivals to date.

Based on the results of such assessments, project officers should determine how many commodities to test. If the records are significantly inaccurate and incomplete, project officers may need to test the entire commodity inventory. The test results are reported to the Mission Deputy Director. The advantage of end-use reviews is that they provide an independent means, outside day to day activities, to verify that project commodities are being used as planned.

**Since the projects began, the Mission has conducted no end-use reviews as defined in the A.I.D. Handbook and stipulated in Mission Order 5-3.** For the Irrigation project this means that since 1981, this guidance for monitoring end-use has not been used to check commodities financed at a cost of \$49 million. For the Production Credit project, which began in 1986, this guidance has also not been used for checking \$3 million of commodities procured since that time.

The project officers agreed that they did not conduct end-use reviews as outlined in the A.I.D. Handbook and Mission guidance provided in Mission Order 5-3. However, they said that during normal project monitoring activities they check on use of the commodities and, in fact, report on the commodities to the Director of USAID/Egypt quarterly. To determine whether the officers' quarterly reports contained information on use of commodities, we analyzed the reports issued between December 1990 and September 1992. We found that the Irrigation project reports addressed the progress of the project, the studies and evaluations being conducted, and the training undertaken and completed but did not comment on the use of commodities. Similarly, the Production Credit project reports addressed the progress of the project, the evaluations conducted, the training undertaken and completed and the delivery and installation of project computers, but did not comment on the use of commodities.

To assess what end-use reviews would have disclosed, had they been conducted, we visited several sites of the Irrigation project which represented \$49 million of the \$52 million procured for the Irrigation and Production Credit projects. We did not test the \$3 million of commodities procured under the Production Credit project because of (1) the small amount of procurements compared to the Irrigation project, and (2) the widely scattered locations where the commodities were being kept. We did note however, that records of site visits, contractor activities and receiving reports were more complete for this project than for the Irrigation project.

To verify that equipment at the Irrigation project sites was being used for project purposes and to test the validity of inventory records, we requested the Mission's inventory of the Irrigation project commodities (See Scope and Methodology section, Appendix I). The Mission provided two reports generated by the host country project monitoring office. One report covered equipment; the other vehicles. The reports (inventory) showed (1) the commodity name, (2)

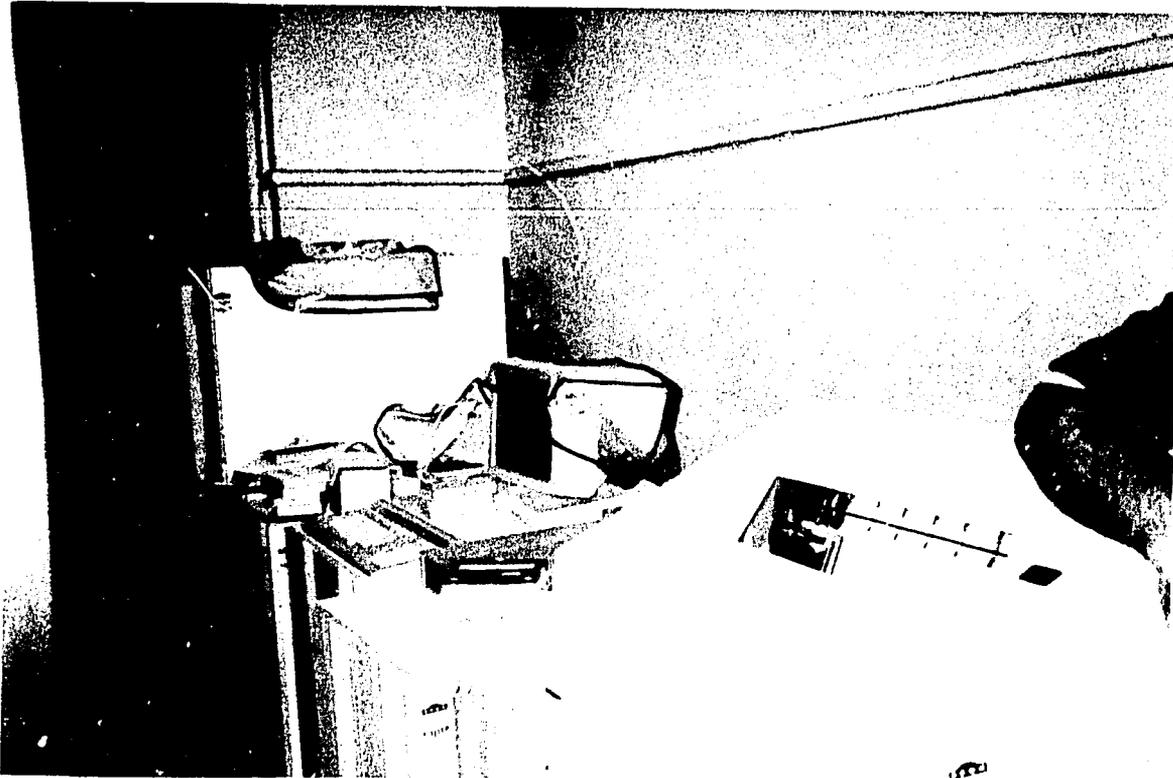
quantity, (3) manufacturer, (4) serial number, (5) year purchased, (6) status,—i.e., active, under repair, or maintenance—and (7) location.

Our tests of 249 items (of 1,578 listed in the monitoring report) showed that, had end-use reviews been conducted, they would have disclosed that: (1) commodities of significant value were missing from the reports, (2) adequate records were not being kept to determine whether vehicles were used for project purposes, (3) costly equipment had not been used for one to two years, and (4) commodities were not at the locations shown in the monitoring office reports. Disclosing such problems is critical if project officers are to take timely corrective action. Examples of these problems follow.

(1) Commodities of Significant Value Were Missing From the Monitoring Reports - In 1989, the Water Research Center (Center) component procured a computer network (Tower System) to provide a communications link with its institutes. This system, valued at about \$1 million, was operational and included a main frame computer, terminals, printers and transmitting towers. However, during our visit to the Center's main office, to verify that commodities purchased were installed and being used, we examined some of the components of the Tower System but did not find the system listed in the monitoring reports. Also, our comparison of the technical assistance contractor records and the monitoring reports disclosed that 90 other items totalling \$376,600 procured for various of the Center's 11 Research Institutes were missing from the reports. These items included 14 printers costing \$8,059, 11 water current meters costing \$31,435, seven inflatable boats and three motors costing \$28,692, and a microprocessor control gas chromatograph costing \$43,822.

In addition, two pickup trucks worth \$35,000 procured for the Main Systems Management component and three pickup trucks worth about \$60,000 procured for the Preventive Maintenance component were missing from the monitoring office vehicle report.

Mission personnel agreed that items of significant value were not included in the reports. They said it was likely that items in addition to those uncovered during the audit could be missing from the reports. The items are missing because commodity procurements were carried out by several technical assistance contractors prior to 1989 which complicated the task of keeping accurate equipment and vehicle listings. When new contracts were signed in 1989, the new contractors evidently did not pick up all items in their lists. Thus, monitoring office reports may not match the commodities on hand. Obviously, if the Mission does not have an accurate list of commodities on hand, it cannot be sure that all commodities are properly used and controlled.



**Main frame computer of the Water Research Center Tower System. Cairo Governorate - September 1992.**

(2) Adequate Records Were Not Being Kept to Determine Whether Vehicles were Used for Project Purposes - A logbook should account for every vehicle and record each trip, date, destination, distance traveled, time, purpose, passengers, etc. The logbook serves as a control to distinguish project from nonproject use. We inspected 72 of the 428 vehicles procured for the Irrigation project. We found that project staff did not maintain logbooks for 27 vehicles. We reviewed 45 vehicles' logbooks, these daily use records did not include adequate information on: (1) date, (2) vehicle destination, (3) distance traveled, (4) start and stop time, (5) trip purpose, (6) passengers, and (7) signature of user.

Individual trips were not recorded as separate line item entries in the logbook. Rather, multiple trips were recorded as one item each day. For example, if a vehicle was used for home to office commuting in the morning and evening and made multiple trips for project purposes during the day, the logbook showed only one trip. The driver would record the beginning and ending mileage, start time, ending time, one destination, purpose and passenger(s). In some cases, the vehicle user did not sign the log sheet. In other cases, the log sheet was not signed until the end of the month.

Our discussions with host country project officers and contractors revealed that several vehicles were driven primarily for personal use, such as home to office commuting for local employees.

Two 1991 Ford Taurus Station Wagons costing \$33,072 were purchased for the Survey & Mapping Project. According to the Administrative Director, both vehicles were assigned to one person, the GOE project Director. One was used for home to office commuting and was parked during the day at the Director's office. Although the other vehicle is available for use by the project, it is held primarily as a "backup" for the Director. However, because of its high operating cost, this vehicle is used infrequently. During August 1992, it appears that because the Director was away travelling these vehicles were not used.



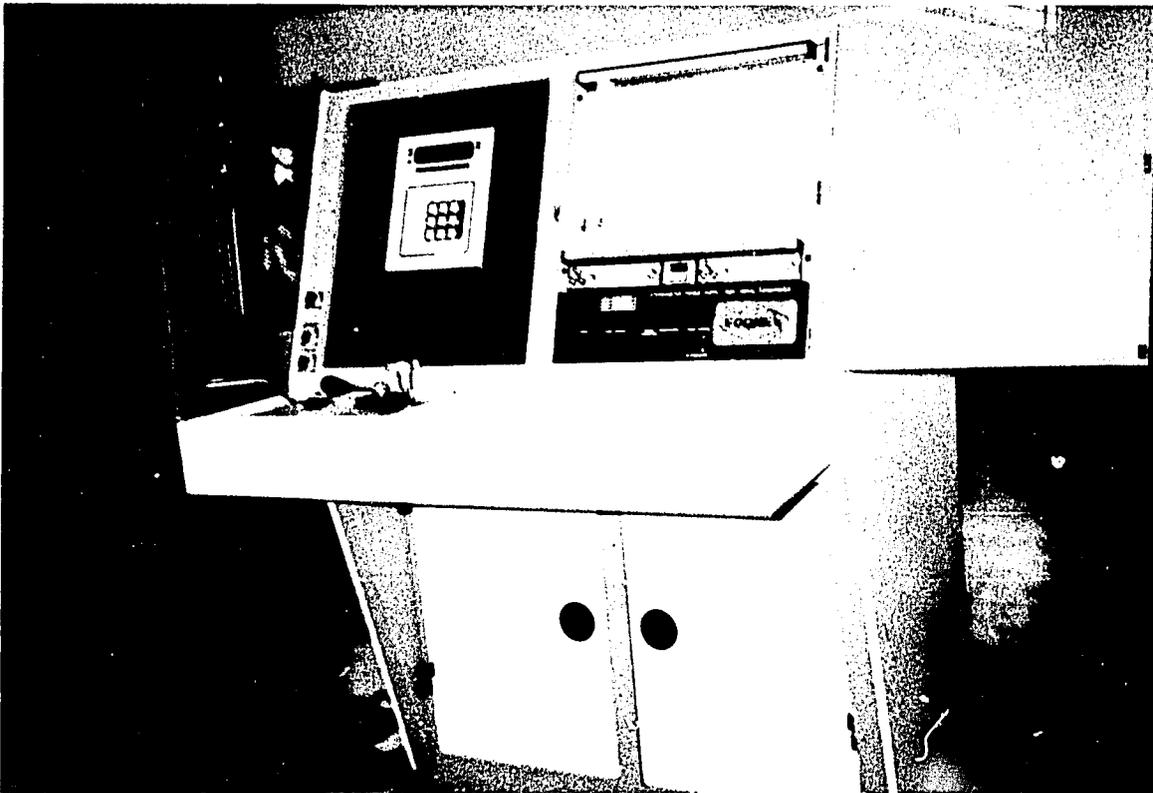
**One 1991 Ford Taurus Station Wagon assigned to GOE project director. Giza Governorate - February 1993.**

Use of project vehicles for local employees' home to office commuting is authorized by Project Implementation Letter No. 28 for the Irrigation project. However, Mission policy limits

nonproject use of project vehicles to 25 percent of each vehicle's total use. Since Mission policy states that vehicle needs cannot be based on personal use, if vehicles are used primarily for personal use it is reasonable to conclude that these vehicles are excess to legitimate project needs.

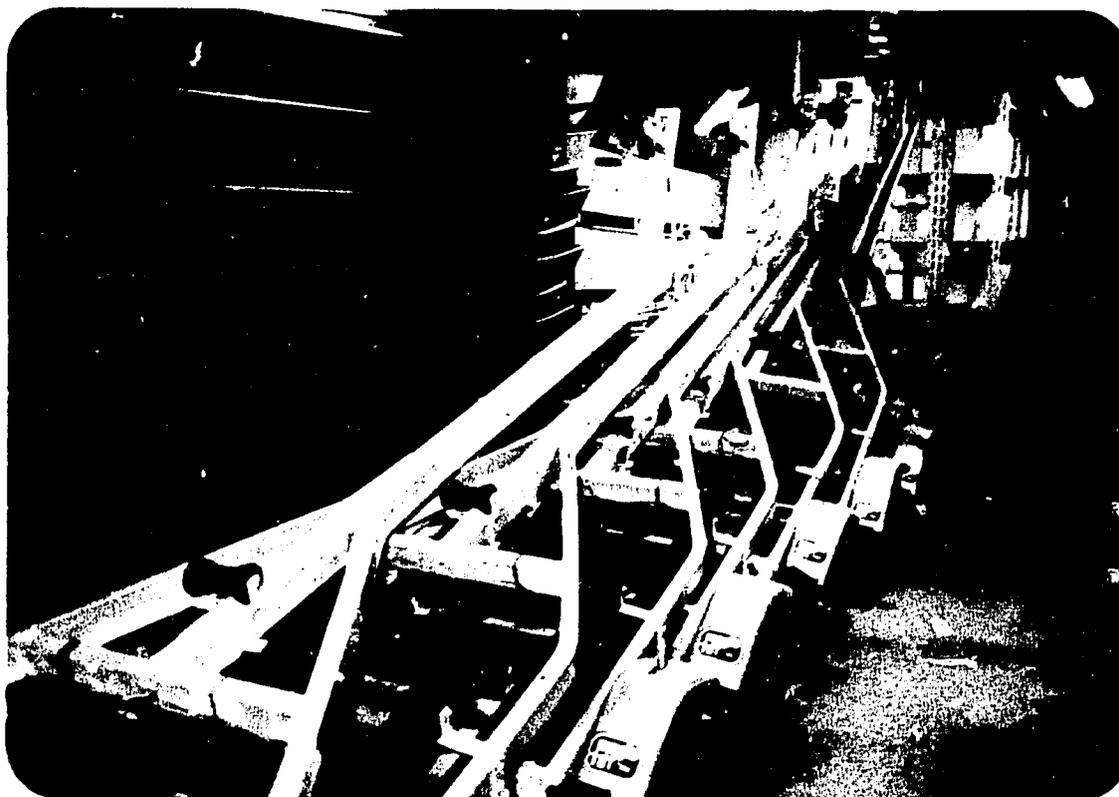
(3) Costly Equipment Had Not Been Used for One to Two Years - If project equipment is idle for long period of times, intended project benefits are not being realized. We found equipment that had been idle or had been kept in storage for one to two years. For example, the Irrigation project procured three pieces of equipment about two years ago: (1) a Universal testing machine and associated equipment for \$92,638, (2) a 20-ton Cone penetrometer for \$32,900, and (3) a temperature and humidity chamber for \$12,400. We located the equipment and found that none of it had been used since its procurement because:

- project personnel had to be trained how to use the equipment,
- project personnel were afraid to use it because of its high value, or
- the equipment was being saved for future use.



**Universal testing machine purchased in 1990 for the Soil Mechanics Research Institute of the Water Research Center. Qalubiya Governorate - September 1992.**

At another location, the Main Systems Management component received 45 boats (including trailers, motors and spare parts) costing \$215,983 in January 1992. Eleven of the boats had never been used and were being stored—seven at Delta Barrage, two at Damanhour and two at Minia. Project personnel told us that the boats were being "saved" to replace other boats, should the need arise to replace them. We do not believe that buying eleven boats as back-up spare equipment is a justifiable A.I.D. investment—especially since the project procurement plan provided for the purchase of only five spare boats to be used while other boats were undergoing maintenance and repair. Also, the procurement plan provided for only 25 trailers (including 5 spares) although 45 were procured.



**Seven boats and trailers stored at the Main Systems Management component warehouse at Delta Barrage. Qalubiya Governorate - September 1992.**

In addition, we found 246 motorcycles and spare parts (\$537,000) procured by the Irrigation Improvement Project component which were still in storage after 10 months because licensing procedures had not been completed.



**Twenty of 246 motorcycles received at Damanhour by the Irrigation Improvement Project component in February 1992. The 246 motorcycles were stored at various sites, all awaiting licensing. Beheira Governorate - September 1992.**

(4) Commodities Were Not at the Locations Shown in the Monitoring Reports - The Water Research Center component's main office and 10 of its 11 research institutes were originally located in the Cairo/Giza area. Later, the 10 research institutes were moved to the Delta Barrage, Qalubiya Governorate. At that time, most of the commodities were reported at the new location. However, the reports continued to show that the 99 research institute vehicles (costing about \$1.6 million) were located in Cairo although 75 of the vehicles had been relocated to Alexandria and Delta Barrage. Mission officials indicated that although the records may not have shown the right locations, Mission project officers knew that the vehicles were located at Alexandria and Delta Barrage.

One of the reasons for the lack of end-use reviews was that Mission personnel believed that routine project monitoring activities constituted end-use reviews. Accordingly, project officer site visits and the daily duties performed by host country and technical assistance contractor personnel were incorrectly believed to fulfill the end-use review requirements specified in Mission Order 5-3. Inspecting commodities when received and observing commodity use during the course of performing other duties were also incorrectly believed to fulfill end-use review

requirements. While such procedures are important, they do not constitute commodity end-use reviews as described in Mission Order guidance.

Mission Order 5-3 stipulates that an end-use review will consist of (1) reviewing project records and, (2) selecting a sample of project commodities to test whether they are being used in accordance with project requirements. What is vital about end-use reviews is that they are systematic *independent tests* to verify that commodities purchased by USAID are being used as required and to inform project officers of potential problems.

Lack of end-use reviews was also due to the project officers' not understanding who was to conduct the reviews. The project officers told us they believed the host country project Monitoring Office was responsible for conducting the reviews. They assumed that, as long as the Monitoring Office had overall project monitoring responsibility and acted as the liaison between the Irrigation project components and the GOE, end-use reviews were part of that office's responsibility. However, the Monitoring Office believed its function was to account for project commodities rather than to conduct end-use reviews.

Another reason for not conducting end-use reviews was that the Mission had not yet implemented satisfactory internal controls for project commodities. In its 1989, 1990 and 1991 Federal Managers' Financial Integrity Act Reports on Internal Controls, the Mission cited as a major internal control weakness host country entities', contractors' and nonprofit organizations' inability to maintain satisfactory and complete records on the arrival, use, storage and disposition of non-vehicular commodities financed by A.I.D. To correct this weakness, the Mission indicated it would strengthen the guidance given to grantees and contractors on how to control the arrival, use, storage and disposition of commodities. The Mission also indicated it was considering delegating end-use reviews to a new contractor hired directly by USAID/Egypt to conduct the reviews for the Agricultural Directorate.

Mission officials informed us, in January 1993, that the Agricultural Directorate had submitted a Project Implementation Order for Technical Services totalling about \$157,186 (LE525,000/LE3.34 = \$157,185.63) to the Mission Contracting Office to procure the services of a firm to develop a system to statistically sample commodity end-use with a high level of confidence. Although initiated in June 1992, the system is not expected to be fully implemented until April or May 1993. We agree that, once implemented, this new system should provide better control over verifying commodities' end-use, and we support the Mission's actions.

Commodities are a high risk area because they are subject to theft, misuse, loss, and unauthorized disposal. It is imperative, therefore, that they be closely monitored. We do not believe that the host government's day-to-day monitoring or project officers' site visits take the place of or serve the purpose of independent end-use reviews. Periodic end-use reviews should be performed, summarized and reported to the Mission Deputy Director. Before they can be performed, the Mission must determine how much of the \$52 million of commodities procured

on these projects are at risk of not being used properly and what size of a sample should be subject to end-use reviews. This would provide the Mission with better assurance that commodities are used as intended.

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## MANAGEMENT COMMENTS AND OUR EVALUATION

The Mission generally agreed with our report and recommendation and its response to the draft report is included in its entirety in Appendix II to this report. The Mission has also requested that its letter of audit representations be included as part of its comments. (See Appendix II.) The Mission's response and our evaluation are discussed below.

Recommendation No. 1 - The Mission agreed with the recommendation and the importance of end-use reviews as an internal control to ensure commodities are benefitting the projects. As part of an effort to strengthen controls in this area, the Mission in 1992 decided to contract for end-use reviews for its Directorate for Human Resources and Development Cooperation. Toward the end of the audit, the Mission authorized the Directorate for Agricultural Resources to also proceed with a contract. Based on the Mission's actions, this recommendation is now considered resolved. It can be closed when RIG/A receives a copy of the signed contract and scope of work.

The Mission states that the audit report identifies the same internal control weakness with respect to end-use checks noted in the Mission's 1991 Internal Control Assessment and therefore validates the Mission's findings. We agree with the Mission but found that this weakness had been reported as early as 1989 but no substantive action was taken until 1992, when end-use review services were procured for the Directorate of Human Resources and Development Cooperation. As noted in this audit report, it was not until the end of the audit that the Mission began to negotiate a contract for end-use reviews for the Directorate of Agricultural Resources. As the report points out, no end-use reviews had ever been conducted for the two projects audited.

In its response, the Mission points out that with project officers' field visits, contractors and host country personnel day-to-day activities and reports, it had in place a system adequate to limit the risk that project commodities would not be used properly or adequately accounted for. The Mission recognized that there were limited records on file of these activities. On pages 5 and 13, the audit report discusses the role of site visits, etc. in ensuring that project commodities are adequately monitored and recognize the Mission's activities in these areas. However, the report cautions the Mission that these activities, many of which are part of the daily routine of project monitoring, do not provide the same control that *independent* and *systematic* end-use

reviews provide—as stipulated in Mission Order No. 5-3. Essentially, end-use reviews tell management that these daily monitoring activities are effective.

The Mission stated that the report did not make a distinction between the Irrigation and Production Credit projects or the type of controls in place in each project. The audit report was changed to better reflect the difference in the type and complexity of the two projects. (See pages 1, 2 and 7.)

The Mission claims that a significant amount of commodities for the Irrigation project are in place and need little end-use review and therefore the report is not fair in pointing out that \$52 million of commodities procured on the projects are at risk because end-use reviews were not conducted. We agree that whether commodities are fixed in place would have an impact on the extent of risk and that this factor should be considered in deciding on the scope of end-use reviews to be conducted. However, the purpose of end-use reviews are to assess such risk and determine which commodities should be subject to review. The fact that commodities are in place and, therefore, the risk of theft or loss is reduced does not ensure that they are used properly or accounted for. Therefore, end-use review of the use of equipment would still be needed as well as ensuring that commodity records are accurate.

The Mission stated that it was aware of or resolving many of the problems stated as examples in our report. During the audit we found no clear evidence that the project officers were aware, or if aware, that they were taking substantive action to resolve the problems. We consider unacceptable the fact that some 246 motorcycles had been stored in warehouses unused for over about one year awaiting licensing, or that boats and trailers were procured in excess of requirements and stored in warehouses for more than one year. In addition, for the Ford Taurus station wagons, the GOE director still controlled the two vehicles when audit fieldwork ended. Had end-use reviews been conducted, we believe that problems such as these would have been elevated and may have resulted in stronger action on the part of Mission top management.

End-use reviews serve a function in the internal control system that is not compensated by normal and daily monitoring activities. These independent reviews of commodities are designed to identify problems and elevate them to the attention of Mission management. Project personnel, including contractors, can easily overlook problems of commodity utilization or not take action because they are too close to the problem. End-use reviews are designed to focus on whether project records adequately account for commodities and whether the commodities are used as intended. Because the results of end-use reviews can be quickly elevated to mission top management, they provide a better chance that total mission management expertise will be brought to bear to solve problems. We strongly believe that, in recognizing the lack of end-use reviews as an internal control weakness, and in choosing to contract for such reviews, USAID/Egypt wanted to ensure that it had an *independent* control to elevate problems to top management to ensure that prompt and effective actions were taken.

Therefore, we fully support the Mission's action in this critical area and believe that the Directorate of Agricultural Resources steps to contract for end-use reviews will significantly strengthen its system of internal controls.

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## SCOPE AND METHODOLOGY

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### Scope

We audited the commodity assistance furnished under USAID/Egypt's agriculture projects in accordance with generally accepted government auditing standards, except as discussed below with regard to the extent of representations made by Mission officials.

Government auditing standards require auditors to obtain representation letters when deemed useful. The Office of the Inspector General deems them necessary to support potentially positive findings. We requested USAID/Egypt's management to furnish us written representations regarding this audit assignment. Based on discussions with cognizant Mission officials, the Director of USAID/Egypt provided us a written representation stating that USAID/Egypt is responsible for the internal control system and the fairness and accuracy of the accounting and management information relating to the audited activities and that, to the best of his knowledge and belief, USAID/Egypt had provided us all the financial and management information relating to the audit objectives, USAID/Egypt is unaware of any material instances where information provided had not been properly and accurately recorded and reported, and USAID/Egypt has complied with contractual agreements that could materially affect Mission accountability. (The complete representation is contained in Appendix II to this report.)

Although the Director provided us these essential written representations, he did not provide acceptable representations as to whether he is aware of any instances of irregularities, noncompliance with A.I.D. policies and procedures or violations or possible violations of laws and regulations for the activities under audit. Instead, the Director limited his representation to the statement that, to the best of his knowledge and belief, the records under audit should contain any instances of irregularities, noncompliance or violations. Also, in accordance with A.I.D./Washington guidance of May 13, 1992, the Mission policy is that only the Director will sign a letter of representation. Therefore, other USAID/Egypt officials directly responsible for the audited activities—in this case the Associate Director for the Office of Agriculture—did not provide written representations to the Director confirming essential information. Therefore, our answers to the audit objectives are qualified to the extent of the effect of not having such representations.

We reviewed commodities procured under two of USAID/Egypt's three Agriculture projects: Irrigation Management Systems (the Irrigation project) and Agriculture Production Credit Project (the Production Credit project). The third project—National Agricultural Research Project (the Research project)—was excluded from our review because no significant commodity procurements have occurred since our last report on the project in December 1989 (Audit No. 6-263-90-01).

We conducted the audit from March 19, 1992 through November 12, 1992 and covered actual commodity expenditures of about \$52 million and planned expenditures of \$101.4 million. As of September 30, 1992, commodity expenditures under the Production Credit project amounted to \$2.9 million (of \$5.7 million planned procurement). At the audit exit conference, on January 13, 1993, the Mission told us that the commodities procured under the Irrigation projects cost \$49.2 million (of \$95.7 planned). However, we were unable to corroborate this amount because the Mission Accounting and Control System does not provide detailed line item budget information for each Irrigation project component. The audit covered the systems and procedures relating to project inputs financed by A.I.D. from 1981 and 1986—the Irrigation and Production Credit projects' inception dates—through September 30, 1992.

Our review of the Production Credit project's commodities costing \$2.9 million (of \$283 million obligated) was limited to the review of files maintained by the Mission and the technical assistance contractor. We verified the dollars expended from the procurement and receiving documents, as well as the Mission's records. We did not conduct field visits to verify that the commodities were received and installed because of the limited dollars spent and the numerous locations involved.

However, our review of the Irrigation project's reports on commodities use—i.e., the host country monitoring office reports—found that they did not include dollar values. Thus, we were not able to reconcile commodities received with dollars expended. As noted above, Mission accounting records did not identify the dollar value expended for commodities for each project component. Therefore, we were unable to determine if the commodities listed in the monitoring office reports fully accounted for A.I.D.'s expenditures.

As of September 30, 1992, the funds obligated for the five Irrigation project components we judgmentally selected as a sample totaled \$190 million of the \$313 million total project obligations. Commodity allocations for the five components totalling \$87.7 million represented 91.6 percent of the total (\$95.7 million) project commodity budget.

We conducted our work in the offices of USAID/Egypt, the technical assistance contractors, the Ministry of Public Works and Water Resources, and at governorate warehouse facilities and selected sites of five of the ten project components: Preventive Maintenance, Irrigation Improvement Project, Survey and Mapping, Water Research Center and Main Systems

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Management. The offices and sites were located in Cairo, Alexandria, Damanhour, Tanta, Kafr El Zayat, Giza, Minia, and Delta Barrage.

We interviewed Mission officials and project staff who explained the procedures used. We reviewed Mission files and records, those policies and procedures necessary to answer the audit objectives, and progress reports prepared by the host country monitoring office and the technical assistance contractors to assess whether the reports' information on commodity procurements was sufficient for monitoring purposes. We conducted further tests to verify if the Mission (1) maintained adequate records to ensure that source/origin requirements were met for all procurement transactions, and (2) checked to ensure that ordered goods were in fact received.

We tested a sample of 29 commodity procurement transactions and reviewed pertinent procurement and shipping documents on file at the Mission and at the offices of technical assistance contractors responsible for the transactions. We determined if appropriate waivers had been obtained in cases where sampled commodities were found to have been procured from countries other than those specified by the authorized geographic code.

We inspected 249 of the 1,578 items listed in the project monitoring equipment report for project components. For vehicles, we inspected 72 of the 428 vehicles listed in the report. Because we could not rely on the Monitoring Office reports, we visited locations where more than one project had ongoing activities. At each location and project component, we judgmentally selected commodities to inspect based on a review of procurement plans, supplier invoices, receiving reports, storekeeper records, and technical assistance contractors' inventories. During this review, we noted any discrepancies in the documents and inspected selected commodities to compare their serial numbers, manufacturer, or size with those listed in the Monitoring Office reports.

In performing our audit, we considered the findings contained in the Office of Inspector General Audits of USAID/Egypt's Irrigation Management Systems (report No. 6-263-89-7, dated September 2, 1989) and of USAID/Egypt's National Agricultural Research Project (report No. 6-263-90-01, dated December 27, 1989).

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CAIRO, EGYPT

RECEIVED  
5 MAY 1993

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MEMORANDUM

TO: Philippe L. Darcy, RIG/A/C  
FROM: Henry H. Bassford, DIR  
SUBJECT: Audit of Commodity Assistance Furnished Under  
USAID/Egypt Agriculture Projects

SUMMARY:

In 1991, the Mission conducted an Internal Control Assessment (ICA) pursuant to the Federal Managers Financial Integrity Act. The audit report in essence identifies the same internal control weakness with respect to end-use checks and thereby authenticates the Mission's work. Since the assessment, the Mission has taken steps to improve end-use checking throughout the Mission. The work done by the Mission to date attempts to address the same problems identified by the recommendation made in the audit report.

Notwithstanding our concurrence with the audit recommendation, the Mission believes it has implemented procedures to reduce risk to a level significantly below that stated in the audit report. As a result of the ICA, the IMS Project staff began to consolidate the inventory and maintain summary records of project commodities under the Monitoring Office in anticipation of implementing procedures to perform end-use checks. At the time of the audit, the summary records were not complete as verification between the Monitoring Office and the 10 Component Offices had not taken place. As stated in the report, the Monitoring Office records were incomplete, however detailed inventory records are maintained at the component level.

The Mission had assessed risks and performed end-use checks through project and contractor staff at the component level, however they were neither well documented nor done in the manner suggested by the handbooks. However, the Mission's alternate internal control procedures had identified most of the instances cited in the report where project commodities were not being used for project purposes.

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In conclusion, we are not saying there are no problems. We know there are. However a more informative and balanced report might consider: the differences between the APCP and IMS projects, means other than formal end-use reviews employed to assure proper use of commodities, evaluation of the risks inherent in various types of commodities procured, and evaluation of the extent to which actions taken or planned are adequate to correct deficiencies, as more fully discussed in the body of our management comments appended to this report.

STEPS TAKEN IN RESPONSE TO 1991 INTERNAL CONTROL ASSESSMENT:

Recognizing the value of end-use reviews, and its inability to conduct them to the extent needed given its limited staff, the Mission decided in December 1991 to procure this service through contracts. The Mission began this process on a trial basis with its Human Resources Directorate in May 1992. The Mission plans to replicate this measure in other Directorates if it is successful. In anticipation of success, the Agricultural Directorate took steps to initiate a similar procurement in June 1992, but it was put on hold while the Mission reviewed the results of the HRDC trial. The Agricultural Directorate has now been authorized to proceed with the procurement, and a contract is being negotiated with the selected firm. Work is expected to begin soon.

IMS VS. APCP:

The audit report states "... we do not believe the Mission has adequate controls to ensure that commodities procured for IMS and APCP projects will be used as required." (pg. 9) In this conclusion, as elsewhere in the report no distinction is made between the controls that exist or are appropriate for these two very different projects. However, all problems noted on page 12 - 22 relate to the IMS project. To our knowledge the audit did not identify any evidence of inadequate monitoring of commodity use under the APCP project. IMS is a larger more complex project and the Mission acknowledges there are commodity monitoring and utilization problems. Controls may be less than desired, but neither are they non-existent.

Monitoring Use of APCP Commodities

Although formal end-use reviews have not been used, management believes this project has taken alternative steps to eliminate the risk of theft, misuse, loss and unauthorized disposal of AID-funded commodities. The system employs three means of

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verification which Management believes accomplishes the objectives of Handbook and Mission Order guidance on end-use reviews. The need for an independent, outside source of verification of APCP commodities is minimal because PBDAC's internal control system is excellent, and the relatively small amounts of commodities purchased under the project are manageable.

The three means of verification being used are as follows:

USAID End-Use Checks - As USAID Project Officials make field trips to the Governorates, a copy of the APCP Governorate inventory is checked against commodities in that Governorate. This usually means checking serial numbers of commodities, maintenance records, availability of spare parts, etc. Copies of these field trips can be found in AGR/ACE files.

Procurement Services Agent Review - The primary TA contractor, Chemonics, also acts as the Project Procurement Services Agent (PSA). As part of its responsibilities Chemonics keeps a complete inventory of all commodities purchased. The inventory is regularly updated and verified by the PBDAC. Chemonics makes regular visits to the Governorates to identify problem areas and confirm that equipment/commodities are operational. Chemonics also does end-use checks in coordination with PBDAC and USAID, often travelling together, to assure that records are internally consistent.

PBDAC Annual Physical Inventory - Annual physical inventories are carried out in each of the Governorates. The inventory is executed by a Committee composed of PBDAC (Commodity records staff and accountant) and PBDAC Governorate staff. These official inventories are signed by the members of the committee and officials from the Governorate PBDAC following the completion of the inventory. These inventories are kept on file at the PBDAC headquarters and are checked periodically by the USAID Project Officer.

Monitoring Use of IMS Commodities:

Management believes a description of the structure and resources of the IMS Project would contribute substantially to the reader of the audit report's understanding of the nature of commodity end-use monitoring requirements for this project. The IMS project is an umbrella project with ten components. These components are essentially projects in themselves and as large and complex as most typical A.I.D. projects. While the Monitoring Office referred to in the report is charged with

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keeping a summary inventory of all IMS commodities and is expected to carry out project-wide end-use checks, it is not charged with the primary responsibility for controlling and monitoring commodities. This function lies at the component level. Technical assistance contractors are charged with providing procurement assistance, and with helping the GOE implementing entities establish commodity inventory and tracking systems. Some of these systems are working quite well while others are not fully developed.

The Mission agrees that end-use reviews, as specifically defined in the Handbook and Mission Orders, should be utilized, and that this tool could have improved monitoring of commodities under the IMS project. However there are many alternative procedures available to Project Managers to assist in monitoring end-use of commodities. Management believes the emphasis the report places on "formal" end-use reviews in terms of their importance to adequate end-use monitoring of commodities does not give credit to the value of these alternate procedures. We recognize that the emphasis stems directly from AID's own handbooks and Mission Orders, nevertheless, unless these additional procedures are discussed in the report there is a very real danger that a reader of the report might conclude that because formal end-use reviews were not performed, end-use monitoring of IMS commodities was grossly ignored and perhaps non-existent. Other procedures utilized by Project Managers to monitor commodity end-use and the varying degrees of risk of misuse or abuse inherent to different types of commodities should be considered.

Under the IMS project the vast majority of commodities were procured with the direct involvement of the contractors that provide technical assistance and oversight for project implementation on a full-time basis. Seven of the ten IMS components have full-time technical assistance teams in place. The large majority of commodities procured or to be procured fall under these components. These contractors know what has been procured and for what purposes. They are in a position to closely observe the utilization of these commodities, and are responsible for providing training and assistance to ensure proper use. Frequent meetings between Project Managers and contractor staff along with written reports by contractors are utilized by IMS project managers to assist in monitoring end-use. Many problems or potential problems, though clearly not all, have been identified and resolved using these mechanisms. Field trips and other visits to project sites by Mission and contractor staff are also utilized to monitor commodity end-use. Unfortunately, the extent to which this process is used is not well documented.

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The report recognizes degree of risk as a factor that should be considered in determining end-use monitoring requirements. Management believes consideration of the types of commodities procured by IMS and the inherent risk involved would be appropriate in determining the adequacy of the controls and monitoring mechanisms that were in place. A significant portion of the commodities procured under the IMS project become fixed as part of a system, structure or facility. The risk for theft or misuse of such items is low. For example: The project procured a multi-million dollar MSM telemetry system with components scattered throughout the country. In a visit to the headquarters here in Cairo one can view a lighted board which tells whether or not data is being properly received from each of the remote sites. The Mission believes such a visit along with a review of the data being collected, provides a strong indication that these commodities are being utilized as intended. The system works, providing the data it is intended to provide, or it doesn't. Other examples could be cited. Management believes in these instances "formal" end-use reviews are not required to adequately monitor end-use, although Agency guidance calls for such reviews. This type of commodity represents a significant portion of the IMS commodities.

In a complex project such as IMS with large commodity procurements, it can be expected that not everything will go as planned and problems such as those cited on pages 18 - 20 will occur. The motorcycles procured for the IIP component, the boats under the MSM component, and the Tarus station wagons under the S&M component are examples of such problems. Project Officers had discovered or were aware of and working to resolve these and most of the other problems of this type cited in the audit. Nevertheless, we agree that the use of end-use reviews will serve to further improve awareness of such problems and will contribute to enhanced end-use monitoring.

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UNITED STATES AGENCY for INTERNATIONAL DEVELOPMENT

CAIRO, EGYPT

Mr. Philippe L. Darcy  
Regional Inspector General  
for Audits  
Cairo, Egypt

MAR 9 1993

RECEIVED  
9 MAR 1993

Dear Mr. Darcy:

This Representation Letter is being issued in accordance with Agency guidance in response to the audit of "Commodity Assistance Furnished Under USAID/Egypt Agriculture Projects".

Based upon discussions with Mission Staff, and taking into account identified staffing constraints and vulnerabilities as expressed in Mission ICAs, to the best of my knowledge and belief, I confirm that all appropriate financial records in the possession and under the control of USAID/Cairo relating to the function being audited have been available to you. To the best of my knowledge and belief, the records made available to you are accurate and complete, and they fairly represent the status of Commodity Assistance Furnished Under USAID/Egypt Agriculture Projects within the Mission. To the best of my knowledge and belief, in conjunction with A, B, C and D below, those records, and verbal representations of AID employees currently in the Mission, should have identified any instances of non-compliance or irregularities, or violations of laws and regulations as those terms may be defined by or perceived by the Inspector General. Specifically I represent that:

- (A) USAID/Egypt is responsible for the internal control system, for the fairness and accuracy of accounting and management information for the function under audit. USAID/Egypt to the best of my knowledge and belief exercises its best efforts to ascertain and follow applicable U.S. laws and AID regulations and AID interpretations of those laws and regulations.

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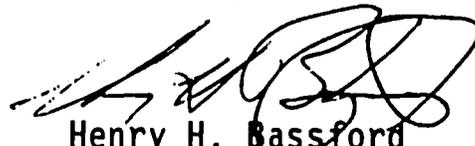
- (B) To the best of my knowledge and belief, and based on discussions and verbal representations by others in the Mission, USAID/Egypt has made available to you or otherwise provided you at your request all financial and management information related to the audit objectives.
- (C) To the best of my knowledge and belief, except for any findings or other matters included in the audit report, USAID/Egypt is unaware of any material instances associated with the function being audited where financial or management information has not been properly and accurately recorded/reported.
- (D) To the best of my knowledge and belief, USAID/Egypt has complied with all contractual agreements, to the extent there are such agreements, which could have any material effect on Commodity Assistance Furnished Under USAID/Egypt Agriculture Projects.

Upon review of your draft report and following further discussion with my staff, I know of no events subsequent to the date of your draft report, (other than those which were included in our response to that report), which to the best of my knowledge and belief would materially alter the statements in (A) thru (D) above.

All representations made herein by me are made in light of my experience since my arrival at post.

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

Sincerely yours,

  
Henry H. Bassford  
Director

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