

Regional Inspector General for Audit  
Cairo, Egypt

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Audit of USAID/Egypt's Controls Over  
Commodities Procured by Host Country  
Technical Assistance Contractors

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Report No. 6-263-93-10  
August 18, 1993

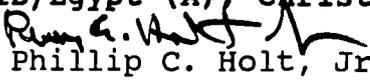


INSPECTOR  
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U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

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

August 18, 1993

**MEMORANDUM FOR Director USAID/Egypt (A), Christopher Crowley**  
**FROM :** RIG/A/C (A), Phillip C. Holt, Jr.   
**SUBJECT:** Audit of USAID/Egypt's Controls Over Commodities  
Procured by Host Country Technical Assistance  
Contractors

Enclosed are ten copies of our audit report on USAID/Egypt's Controls Over Commodities Procured by Host Country Technical Assistance Contractors, Audit Report No. 6-263-93-10. The report contains two recommendations, both of which we consider closed as a result of your actions prior to the issuance of this report.

In finalizing our report, we fully considered your comments on the draft report and have included them as Appendix II to this report. Furthermore, in accordance with your request, we have included the full text of your written representations as Appendix III to this report.

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

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## **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. Such commodities typically include vehicles, computers, laboratory equipment, as well as many other types of mechanical and technical equipment and supplies. A.I.D. often uses technical assistance contractors working for the host country to procure these goods because it reduces the resources A.I.D. has to devote to commodity procurement. Between October 1, 1990 and September 30, 1992, host country technical assistance contractors procured over \$57 million of A.I.D.-financed commodities for Egypt.

Using host country technical assistance contractors to procure commodities benefits A.I.D. because it transfers day-to-day responsibility for commodity procurement from A.I.D. to contractors. A.I.D. then monitors rather than manages the procurement process. The disadvantage of having contractors conduct procurement is that while A.I.D. is still responsible for compliance with laws, regulations, and binding policies, it is removed from—and therefore has less control over—such procurement.

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## **Audit Objectives**

Pursuant to its Fiscal Year 1993 audit plan, the Office of the Regional Inspector General for Audit/Cairo performed this audit of USAID/Egypt to answer the following audit objectives:

- Did USAID/Egypt follow A.I.D. policies and procedures and the "specific" Standards for Internal Controls in the Federal Government in ensuring all applicable commodity procurement clauses were incorporated in host country technical assistance contracts and commodity procurement documents?
- Did USAID/Egypt follow A.I.D. policies and procedures and the "specific" Standards for Internal Controls in the Federal Government in monitoring host country commodity procurements to ensure they were conducted in accordance with applicable contract clauses?

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

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## **Audit Findings**

In order to answer the second audit objective, we deemed it necessary for Mission management to provide certain written assurances regarding the audited activities. The Mission Director's written representations are included as Appendix III to this report. However, since the officials directly responsible for the programs audited did not provide written representations, we have qualified our answer to this objective.

**Did USAID/Egypt follow A.I.D. policies and procedures and the "specific" Standards for Internal Controls in the Federal Government in ensuring all applicable commodity procurement clauses were incorporated in host country technical assistance contracts and commodity procurement documents?**

We believe USAID/Egypt followed A.I.D. policies and procedures and the "specific" Standards for Internal Controls in the Federal Government (GAO Standards) in ensuring all applicable commodity procurement clauses were incorporated in host country technical assistance contracts and commodity procurement documents. However, human error sometimes resulted in the omission of necessary contract clauses.

The Mission's review and approval of both draft and final host country contracts are key A.I.D. Handbook 11, Chapter 1, controls designed to ensure that all appropriate contract clauses are included in such contracts. USAID/Egypt duly implemented these controls by reviewing and approving both draft and final host country technical assistance contracts. Such reviews were conducted by personnel from several different USAID/Egypt directorates, thereby providing an independent and objective evaluation. This review by parties outside the project office complies with the "specific" Standard for Internal Controls in the Federal Government addressing separation of duties.

**A Mandatory Commodity Clause Was Not Incorporated In All Contracts**

GAO Standards and A.I.D. Handbook 11 require that Missions establish controls to protect A.I.D. resources. Controls that allow A.I.D. to take ownership of undelivered commodities and to direct delivery of those commodities are particularly essential in host country contracts. The audit found that such a clause was not incorporated in all host country contracts—an omission which we believe increased the risk of losing over \$1.2 million of A.I.D.-financed commodities. This omission occurred because of USAID/Egypt oversight.

**Recommendation No. 1:** We recommend the Director USAID/Egypt ensure the Government of Egypt incorporates A.I.D.'s mandatory "Vesting of Title and Diversion Rights" clause when next amending host country contracts lacking this clause.

**Recommendation No. 2:** We recommend the Director USAID/Egypt incorporate A.I.D. Handbook 11, Chapter 1, clauses regarding commodity procurement into the checklist used by Mission personnel when reviewing host country procurement of professional and technical services.

GAO's Standards for Internal Controls in the Federal Government require that controls be established to protect U.S. Government resources from loss. This requirement is evident in A.I.D. Handbook 11, Chapter 1, which makes it mandatory that a contract clause permitting

A.I.D. to take title to and direct shipment of undelivered commodities be included in all host country contracts.

Our examination of all cost-plus-fixed-fee host country technical assistance contracts active at September 30, 1992, and containing funds for commodity procurement, revealed that six out of the seventeen contracts reviewed did not incorporate this mandatory clause. As a result, the Mission faced increased the risk that over \$1.2 million in A.I.D.-financed commodities could be kept or diverted by the contractor.

USAID/Egypt officials indicated that they did not know the reason for the absence of the "Vesting of Title and Diversion Rights" clause in these contracts. Since the Mission included Handbook 11's other mandatory clauses in the sampled contracts, we concluded the omission of this clause was an oversight. We believe that including mandatory clauses regarding commodity procurement in the checklist used by Mission staff when arranging for host country procurement of technical assistance will reduce the likelihood of future omissions.

**Did USAID/Egypt follow A.I.D. policies and procedures and the "specific" Standards for Internal Controls in the Federal Government in monitoring host country commodity procurements to ensure they were conducted in accordance with applicable contract clauses?**

Except for the effect of our not receiving acceptable written representations from Mission management, as discussed in Appendix I, we believe USAID/Egypt followed A.I.D. policies and procedures and the "specific" Standards for Internal Controls in the Federal Government in monitoring host country commodity procurements to ensure they were conducted in accordance with applicable contract clauses.

A.I.D. Handbook 11, Chapter 3, requires Missions to review and approve solicitations used by host country technical assistance contractors to procure commodities. Such review is a key control designed to ensure that required contractual clauses are included in commodity tenders. USAID/Egypt complied with this requirement by reviewing and approving commodity solicitations used by host country technical assistance contractors. The Mission also reviewed and approved the evaluation of proposals conducted by host country contractors and the host government. Such approval complies with the "specific" Standard for Internal Controls in the Federal Government requiring the authorization of events committing Government resources.

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

Recommendation No. 1 - Although the Mission did not believe the "Vesting of Title and Diversion Rights" clause was among A.I.D. Handbook 11, Chapter 1's mandatory clauses, it agreed with the recommended action and issued Staff Notice 93-089 instructing project offices to add the "Title" clause when next amending host country contracts omitting the provision. We

consider the recommendation closed on the basis of the Mission's action, but would like to point out that A.I.D. Handbook 11, Chapter 1, Section 4.3.24.b(1) requires inclusion of the "Title" clause in prime contracts

Recommendation No. 2 - USAID/Egypt has revised its Host Country Procurement checklist to incorporate A.I.D. Handbook 11, Chapter 1, Section 4.3.24.b(1), mandatory clauses. As a result, we consider this recommendation closed.

USAID/Egypt's response to the draft report is included in its entirety as Appendix II. The Mission has also requested that its letter of audit representations be included as part of its comments. Therefore, this letter is also included as Appendix III.

## SCOPE AND METHODOLOGY

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### Scope

We audited USAID/Egypt's control's over host country technical assistance contractors' procurement of commodities. The audit covered controls in place during the performance of field work from November 1992 through March 1993. We conducted our audit in accordance with generally accepted government auditing standards for performance audits, 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 they deem the letters useful. The Office of the Inspector General deems them necessary evidence to support potentially positive findings. We requested USAID/Egypt's management to furnish written representations regarding this audit assignment. Based on discussions with Mission officials, USAID/Egypt's Director provided us written representations that contained essential assertions regarding the audited activities. However, Mission officials directly responsible for the activities did not provide written representations as provided for in A.I.D./Washington's August 21, 1992 guidance (The complete representations are contained in Appendix II of this report.) As a result, our answer to the second audit objective is qualified to the extent of the effect of not having such representations.

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### Methodology

In answering the audit objectives, we tested whether USAID/Egypt followed applicable internal control procedures and complied with certain provisions of laws and regulations. We designed our tests to provide reasonable—but not absolute—assurance of detecting abuse or illegal acts that could significantly affect the audit objectives and reasonable—but not absolute—assurance that our answers to the audit objectives are correct. The methodology for each audit objective follows.

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### **Audit Objective One**

The first audit objective was to determine whether USAID/Egypt followed A.I.D. policies and procedures and the "specific" Standards for Internal Controls in the Federal Government in ensuring all applicable commodity procurement clauses were incorporated in host country technical assistance contracts and commodity procurement documents.

To accomplish this audit objective, we discussed current host country contracting procedures with Mission officials and prepared a flowchart identifying key internal controls. Key controls on which USAID/Egypt relied included its review and approval of draft and final host country contracts. We then reviewed formal policies and procedures that had been promulgated by USAID/Egypt. Finally, we analyzed these controls and determined whether they complied with A.I.D. Handbook 11, Chapter 1, and the "specific" Standards for Internal Controls in the Federal Government.

We tested the system for its effectiveness. This involved:

- Reviewing all cost-plus-fixed-fee host country technical assistance contracts active at September 30, 1992 and containing funds for commodity procurement to determine whether they included required commodity procurement clauses.
- Analyzing a judgmental sample of the above contracts to determine whether USAID/Egypt awarded these contracts in accordance with the requirements of A.I.D. Handbook 11 (Host Country Contracting). Our sample consisted of 10 out of a total of 17 contracts (59%) which accounted for \$51.6 million of \$66.3 million (78%) of the funds budgeted for commodity procurement.

### **Audit Objective Two**

The second objective was to determine whether USAID/Egypt followed A.I.D. policies and procedures and the "specific" Standards for Internal Controls in the Federal Government in monitoring host country commodity procurements to ensure they were conducted in accordance with applicable contract clauses. To accomplish this audit objective, we discussed current host country contracting procedures with Mission officials and prepared a flowchart identifying key internal controls. Key controls on which USAID/Egypt relied included its review and approval of Invitation for Bid documents issued by host country contractors when soliciting proposals from suppliers. Other key controls were A.I.D.'s approval of both the evaluation of supplier proposals and the resulting contract. We reviewed the structure of these controls by examining formal policies and procedures promulgated by USAID/Egypt. Finally, we analyzed these controls and determined whether they complied with A.I.D. Handbook 11, Chapter 4, and the

"specific" Standards for Internal Controls in the Federal Government.

We tested the system for its effectiveness. This involved:

- Reviewing a judgmental sample of procurements by host country technical assistance contractors to determine whether USAID/Egypt executed its review function and whether commodities were procured in accordance with contract clauses. Our sample included 49 of 716 procurements (7%) and accounted for \$36.2 million of \$57.4 million (63%) in A.I.D.-financed commodities.



UNITED STATES AGENCY for INTERNATIONAL DEVELOPMENT

CAIRO, EGYPT

**JUL 25 1993**

**MEMORANDUM**

**TO:** Phillip C. Holt, A/RIG/A/C

REGULATIVE  
25 JUL 1993

**FROM:** Douglas Clark, A/D/DIR

**SUBJECT:** Audit of USAID/Egypt's Controls Over Commodities  
Procured by Host Country Technical Assistance  
Contractors

Following is the Mission's response to the two recommendations under the subject draft audit report:

**Recommendation No. 1:**

We recommend the Director USAID/Egypt request the Government of Egypt to incorporate A.I.D.'s mandatory "Vesting of Title and Diversion Rights" clause when next amending host country contracts lacking this clause.

**Mission Response**

The Mission would like to comment on the issue of inclusion of the "Vesting of Title and Diversion Rights" clause. This clause appears as mandatory in the Commodity Procurement Chapter No. 3 of HB 11, and not in the Technical Assistance Chapter No. 1. Technical Assistance contractors are understood to be responsible for knowing the handbook and making sure that this clause is included in any commodity subcontracts they write. We can cite several instances where Technical Assistance contracts did not include the clause but commodity procurement contracts written by the contractor did. Notwithstanding this observation, we agree that recommended action, in the nature of a reminder and check list note, is a good idea. Accordingly, the Mission has drafted a Staff Notice which includes direction to Project Officers and Offices with host country contracts to comply with this requirement. Based on this action, Mission requests resolution and closure of this recommendation.

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Recommendation No. 2:

We recommend the Director USAID/Egypt include A.I.D. Handbook 11, Chapter 3 clauses regarding commodity procurement in the checklist used by Mission personnel on host country procurement of professional and technical services.

Mission Response

Attached herewith is a copy of the draft revised check list. The attached Staff Notice will be issued shortly. Based on this action, Mission requests resolution and closure of this recommendation.

Att: a/s above

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UNITED STATES AGENCY for INTERNATIONAL DEVELOPMENT

CAIRO, EGYPT

JUN 07 1993

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

RECEIVED  
8 JUN 1993

Dear Mr. Darcy:

This Representation Letter is being issued in accordance with Agency guidance in response to the audit of "Controls Over Host Country Technical Assistance Contractors' Procurement of Commodities".

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 made 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 Controls Over Host Country Technical Assistance Contractors' Procurement of Commodities within the Mission. To the best of my knowledge and belief, as a layman and not as a lawyer, in conjunction with A, B, C and D below, USAID/Egypt has reported all known instances pertaining to USAID/Egypt's Controls Over Host Country Technical Assistance Contractors' Procurement of Commodities, which, in the Mission's judgement, would evidence material irregularities or non-compliance with AID policies, or violations of U.S. laws and regulations. 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.

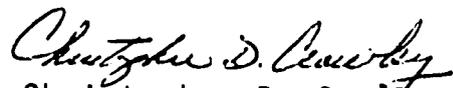
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- (B) To the best of my knowledge and belief, and based on discussions and verbal representations by others in the Mission, USAID/Egypt has made available to you or otherwise provided you at your request all financial and management information related 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 Controls Over Host Country Technical Assistance Contractors' Procurement of Commodities.

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.

Sincerely yours,

  
Christopher D. Crowley  
Acting Director

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