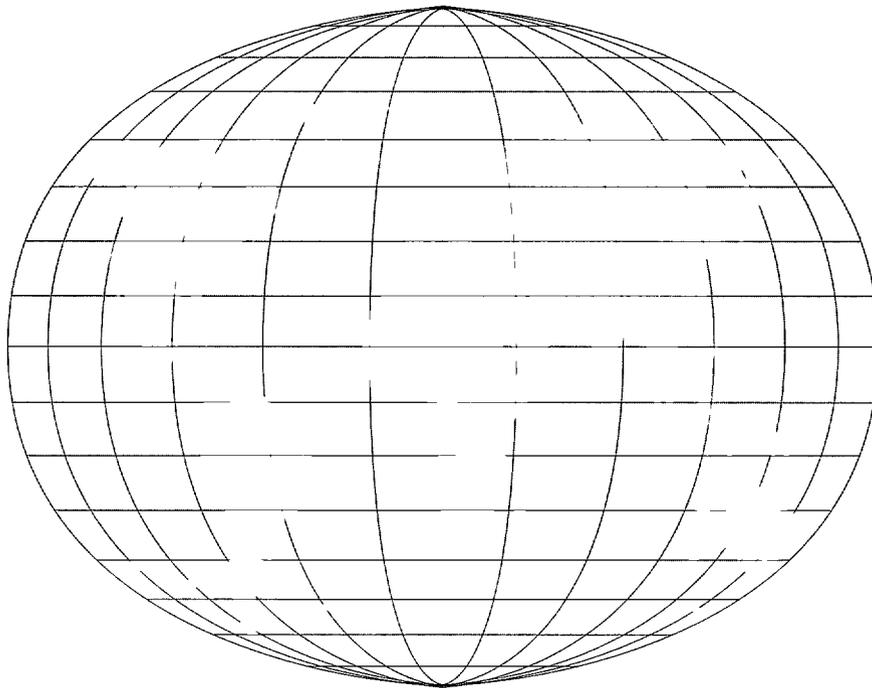


Report of Audit

Audit of USAID Resources Managed by University Research Corporation under the Primary Health Care Support Project No. 656-0226, for the Period January 10, 1994 through October 23, 1998

**Report No. 4-656-00-002-N
February 1, 2000**



**REGIONAL INSPECTOR GENERAL/PRETORIA
OFFICE OF INSPECTOR GENERAL
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT**

**Audit of USAID Resources Managed by University Research
Corporation under the Primary Health Care Support
Project No. 656-0226, for the Period January 10, 1994
through October 23, 1998**

**Report No. 4-656-00-002-N
February 1, 2000**

REGIONAL INSPECTOR GENERAL/PRETORIA



Regional Inspector General
Pretoria

February 1, 2000

MEMORANDUM FOR MISSION DIRECTOR, USAID/MOZAMBIQUE

FROM Regional Inspector General/Pretoria, Joseph Farinella

SUBJECT Agency-contracted Audit of the USAID Resources Managed by University Research Corporation under the Primary Health Care Support Project No 656-0226, for the Period January 10, 1994 through October 23, 1998, Report No 4-656-00-002-N

Attached is a report of an Agency-contracted audit of USAID's contract with the University Research Corporation (URC) under USAID/Mozambique's Primary Health Care Support Project. The audit was performed by Deloitte & Touche, Chartered Accountants, Maputo, Mozambique.

Under the Primary Health Care Support Project, USAID/Mozambique provided \$12,598,790 to URC under a cost reimbursable plus fixed fee contract to assist the Ministry of Health of the Government of Mozambique to (1) define, elaborate and implement decentralization policies and guidelines, (2) improve provincial planning priorities and resource allocation, (3) improve provincial human resources and program management, and (4) upgrade provincial or district facilities.

The Mission obligated \$11,624,993 for the contract which was signed on January 10, 1994 and expired in May 1999. This audit covered the period from January 10, 1994 to October 23, 1998. Expenditures reported by URC during the above period totaled approximately \$10,978,597.

The audit scope and objectives included

- performing a financial audit in accordance with generally accepted auditing standards and the standards of the U.S. Comptroller General's Government Auditing Standards, and expressing an opinion on URC's Fund Accountability Statement for the period January 10, 1994 to October 23, 1998,
- evaluating URC's internal controls in order to assess control risk and identify significant internal control deficiencies, and

- testing URC's compliance with applicable laws, regulations and agreements and report on any material instances of non-compliance

The audit report did not identify any questioned costs, or significant internal control weaknesses or material instances of non-compliance with applicable laws, regulations and agreements. Therefore, we are not making any recommendation and no action is required on your part.

Attachments a/s

**Audit of the USAID Resources Managed by University Research Corporation (URC)
under the Primary Health Care Support Project**

Project No 656-0226

For the period January 10, 1994 to October 23, 1998

TABLE OF CONTENTS

Section	<u>Pages</u>
A Transmittal Letter and Summary	3
B. Fund Accountability Statement	
Report of the Independent Auditors	9
Fund Accountability Statement	11
Notes to the Fund Accountability Statement	12
C Internal Control Structure	15
D Compliance with Agreement Terms and Applicable Laws and Regulations	19
E General purpose annual financial statements	

SECTION A

TRANSMITTAL LETTER AND SUMMARY

**USAID Resources Managed by University Research Corporation (URC) under the Primary
Health Care Support Project**

Project No 656-0226

Contract No 656-0226-C-00-3019-00

Appropriation No 656-0226-3-10053/20047/20157/60022



Africa RegionChartered Accountants and
Management ConsultantsAv Zedequias Manganhela 95
4º Andar Maputo 2581
Mozambique
Caixa Postal 4318
Maputo 2581
Mozambique
Tel (1) 420955/430594
Fax (1) 429163
Int Dialing Code +(258)

Maputo, 15 October 1999

Mr Martin B Karlsen
United States Agency for International Development
Caixa Postal 783
Maputo
Moçambique

Dear Sir

**Audit of the USAID Resources Managed by University Research Corporation (URC)
under the Primary Health Care Support Project****Contract No 656-0226-C-00-3019-00**

We have completed our audit of the above Project for the period 10 January 1994 to 23 October 1998 in accordance with the Contract No 656-0510-I-00-7076-00, Delivery Order No 17 As required in the section 1 6 of this Contract we report as follows

1 General description of the Project Audited

Under the Primary Health Care Support Project (project) \$12,598,790 was provided to University Research Corporation (URC) under a contract which was aimed at assisting the Ministry of Health to define, elaborate and implement decentralization policies and guidelines, improving provincial planning priorities and resources allocation, improving provincial human resources and program management, and to offer limited support to upgrade provincial or district facilities

USAID/Mozambique's contract with URC - an American contractor - Contract No 656-0226-C-00-3019-00 - was awarded on January 10, 1994 and, as amended, has total obligations of \$11,624,993 with a contract completion date of May 1999. The contract is a cost reimbursable plus fixed fee contract.

2 Objectives and scope of the financial audit

As per Delivery Order No 17 of the contract 656-0510-I-00-7076-00 between USAID/Mozambique and Deloitte & Touche the objective of this engagement was to conduct a financial audit of the USAID resources managed by the recipient for the performance of a non-Federal Audit of URC. The scope of the audit was limited to coverage of expenditures incurred from inception to October 23, 1998. Actual contract expenditures as of October 23, 1998, has been approximately \$10,978,597.

The financial audit was performed in accordance with U.S. *Government Auditing Standards* and accordingly included such tests of the accounting records as deemed necessary under the circumstances. The procedures followed can be summarized as follows:

- An entrance conference was held together with USAID officials, the URC's representative in Maputo and the auditors at USAID's Maputo premises in order to understand the audit objectives and its limitations. This conference was complemented by a meeting between the auditors and URC's representative in Maputo at their premises to allow us to get the necessary organizational and specific details to plan the financial audits,
- We obtained and reviewed the following documents:
 - i Agreement and Amendments (1 to 9) between USAID and URC,
 - ii The Contracts established between URC and subcontractors,
 - iii OMB Circular A - 122 "Cost Principles for Nonprofit Organizations"
 - iv OMB Circular A - 21 "Cost Principles for Educational Institutions"
 - v Federal Acquisitions Regulations (FAR)
 - vi USAID Acquisition Regulations (AIDAR)
 - vii Mandatory Standard Provisions
 - viii Standard Provisions Annex for Project Loan or Grant Agreements with Foreign Governments
 - ix Standard Audit Provisions for PL 480 Title II and III Agreements
 - x All the payment vouchers (1 to 59) held by USAID
- At the premises of the URC in Maputo we obtained an understanding of the internal control structure and systems (accounting system description, procurement policies and procedures, and receipt, warehousing and distribution procedures for equipment and materials) to plan the audit and to determine the nature, timing and extent of testing to be performed,
- At this phase special attention was given to some specific concerns of USAID/Mozambique regarding (a) disallowed costs in the URC's monthly vouchers, (b) URC allocation of financial resources at a provincial level (c) verification of the URC's assets register and confirmation if mechanisms are in place for the disposal of the assets in compliance with the terms of the contract,

- We tested the internal control procedures in order to confirm our understanding and to evaluate its effectiveness in preventing or detecting material misstatements in the Fund Accountability Statement and in ensuring compliance with the Agreement terms and applicable laws and regulations,
- From the voucher 59 we obtained the necessary information to prepare the Fund Accountability Statement,
- We identified the direct and indirect costs billed to and reimbursed by USAID by location where they are produced in order to determine the specific audit steps to performed in Mozambique (Maputo and Provinces) and United States

Specific audit steps in Mozambique

- We reviewed the procedures used to control the funds, including their channeling to the Provinces,
- We verified the adherence to the established procurement procedures used to purchase equipment, office supplies and contract local consultants to determine whether sound commercial practices, including competition was used, reasonable prices were obtained, and there were adequate controls on quantities and qualities received
- We verified the URC's assets register and confirmed which mechanisms are in place for the disposal of the assets in compliance with the terms of the contract and on a sample basis,
- We reviewed the transactions related to Other Direct Costs in order to determine its consistency with the objectives of the Project,
- We tested the calculations of all the costs billed on fixed rates basis

Specific audit steps in United States

- We obtained an understanding of the internal control structure and evaluated the control environment to determine the nature, timing and extent of testing to be performed as well as to determine whether the internal controls were established to ensure compliance with agreement terms and applicable laws and regulations,
- We reviewed the general ledger to determine whether costs incurred were properly recorded We reconciled direct costs billed to and reimbursed by USAID to the general ledger,
- We reviewed whether advances of funds to URC - Mozambique were justified with documentation, including reconciliation of funds advanced, disbursed and available
- We reconciled the records on general ledger to the fixed assets register located in Mozambique,
- We reviewed the direct salary charges and all the other related costs to personel, including travel, to determine whether rates were proper and charges were supported including all the tests necessary to assure an adequate billing and reimbursement from USAID,
- We reviewed the subcontracts made including the procurement procedures applied to evaluate the compliance with the agreement terms,

3 Financial audit results

The results of our procedures were satisfactory and included in this report are the various areas audited as follows

Section B - Fund accountability statement

This section includes the fund accountability statement and related notes, the unqualified report of the independent auditors. The Fund Accountability Statement has been prepared on cash receipts and disbursements basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles under the circumstances. Our opinion was in accordance with SAS No. 62 (AU623).

Section C - Internal control structure

We reviewed the internal control structure in our assessment of risk and report that there were no material weaknesses. Our review was performed in accordance with the U.S. General Accounting Office's *Standards for Internal Controls in the Federal Government (1983)*.

Section D - Compliance with agreement terms and applicable laws and regulations

The results of our tests of compliance did not disclose any material instances of non-compliance in accordance to the guidance contained in AICPA SAS No. 74 (AU801).

Section E - General-purpose annual financial statements

In this section were enclosed the audit reports of the URC as a whole for the fiscal years 1994, 1995, 1996 and 1997 issued by Rubino & McGeehin (CPA) - Bethesda.

No cost sharing contributions were required under this agreement and no prior audits were performed to this project. Consequently, we do not include any special section, report or comments on these issues.

4 URC management comments

We confirm that the contents of this report have been discussed with Jay Wechsler and no comments were considered necessary to include.

Should you require any further information please do not hesitate to contact us

Yours Faithfully



Deloitte & Touche

SECTION B

FUND ACCOUNTABILITY STATEMENT

USAID Resources Managed by University Research Corporation (URC) under the Primary
Health Care Support Project

Project No 656-0226

Contract No 656-0226-C-00-3019-00

Appropriation No 656-0226-3-10053/20047/20157/60022

For the period January 10, 1994 to October 23, 1998



Africa Region

Chartered Accountants and
Management Consultants

Av Zedequias Manganhela 95
4º Andar Maputo 2581
Mozambique
Caixa Postal 4318
Maputo 2581
Mozambique
Tel (1) 420955/430594
Fax (1) 429163
Int Dialing Code +(258)

Independent Auditor's Report

Board of Directors

URC - University Research Corporation

We have audited the Fund Accountability Statement of USAID Resources managed by University Research Corporation (URC) under the Primary Health Care Support Project under the USAID Contract No 656-0226-C-00-3019-00 for the period January 10, 1994 to October 23, 1998. The Fund Accountability Statement is the responsibility of the management of URC. Our responsibility is to express an opinion on the Fund Accountability Statement based on our audit.

Except as discussed in the following paragraphs, we concluded our audit in accordance with generally accepted auditing standards and the U.S. Government Auditing Standards issued by the Comptroller General of the United States (1994 Revision). These standards require that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statement is free of material misstatement. An audit includes examining, on the test basis, evidence supporting the amount of disclosures in the Fund Accountability Statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as an evaluation of the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 2, the financial statement was prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than the generally accepted accounting principles.

We do not have a continuing education program that fully satisfies the requirements set forth in chapter 3, paragraph 6 of the U.S. Government Auditing Standards. However, our current program provides for at least 24 hours of continuing education and training every two years. We are taking appropriate steps to implement a continuing education program that fully satisfies the requirement.

We did not have an external quality control review by an unaffiliated audit organization as required by Chapter 3, Paragraph 6 of the U.S. Government Auditing Standard, since no such program is offered to professional organizations in Mozambique. We believe that the effects of this departure from the U.S. Government Auditing Standard is not material because we

participate in the Deloitte Touche Tohmatsu world-wide internal control review program which requires our office to be subjected every three years, to an extensive quality control review by partners and managers from other affiliate offices

In our opinion, the Fund Accountability Statement referred to above presents fairly in all material respects, the revenue, costs incurred and reimbursed by A I D for the period January 10, 1994 to October 23, 19981 in accordance with the terms of the agreement in conformity with the basis of accounting described in the Note 2

The report is intended for the information of URC and the U S Agency for International Development However, upon acceptance by the A I D Regional Inspector General, this report is a matter of public record and its distribution is not limited

Maputo, 15 October 1999



Deloitte & Touche

FUND ACCOUNTABILITY STATEMENT

USAID Resources Managed by University Research Corporation (URC) under the Primary Health Care Support Project

Project No 656-0226

Contract No 656-0226-C-00-3019-00

Appropriation No 656-0226-3-10053/20047/20157/60022

For the period January 10, 1994 to October 23, 1998

	<u>Notes</u>	<u>Budget</u>	<u>Actual</u>
<u>Revenue</u>			
Total revised budget as per Modification No 8 June 27, 1997		<u>12,598,790</u>	<u>10,978,597</u>
<u>Costs Incurred</u>			
Salaries & Wages		1,625,692	1,416,847
Fringe benefits	5	345,732	311,378
Allowances		614,223	551,236
Overhead	5	296,908	268,502
Consultants		646,437	499,941
Travel/Per diem		1,554,196	1,329,755
Other direct costs	6	2,307,651	2,061,113
Equipment & Supplies		321,482	308,256
Subcontracts	7	2,774,846	2,378,574
G&A	5	<u>1,496,816</u>	<u>1,304,135</u>
Total estimated costs		11,983,983	10,429,737
Fixed fee	8	441,615	380,587
Award fee	9	173,192	173,192
Recoveries		-	(4,919)
Total Cost plus Fee		<u>12,598,790</u>	<u>10,978,597</u>

NOTES TO THE FUND ACCOUNTABILITY STATEMENT

USAID Resources Managed by University Research Corporation (URC) under the Primary Health Care Support Project

Project No 656-0226

Contract No 656-0226-C-00-3019-00

Appropriation No 656-0226-3-10053/20047/20157/60022

1 Description of the Project

Under the Primary Health Care Support Project (project) \$12,598,790 was provided to University Research Corporation (URC) under a contract which was aimed at assisting the Ministry of Health to define, elaborate and implement decentralization policies and guidelines, improving provincial planning priorities and resources allocation, improving provincial human resources and program management, and to offer limited support to upgrade provincial or district facilities

USAID/Mozambique's contract with URC - an American contractor - Contract No 656-0226-C-00-3019-00 - was awarded on January 10, 1994 and, as amended, has total obligations of \$11,624,993 with a contract completion date of May 1999. The contract is a cost reimbursable plus fixed fee contract.

2 Main Accounting Policies

Basis of accounting

The fund accountability statement has been prepared on the cash receipts and disbursements basis of accounting. Under the cash basis of accounting receipts are not recorded until received in cash and disbursements are assigned to the period in which cash payment is made.

Exchange Rate

The revenue and expenditure was accounted for in United States Dollars. Costs incurred in Meticals and in other currencies has been converted to United States Dollars at the average rate of exchange ruling during the month that the expenditure was incurred.

Equipment and Supplies

Expenditures relating to equipment and supplies are not recorded as assets in the Fund Accountability Statement.

3 Revenue

Revenue represents funds received under the USAID Contract Agreement # 656-0226-C-00-3019-00 during the period January 10, 1994 to October 23, 1998. The financial statements of USAID Resources managed by University Research Corporation (URC) under the Primary Health Care Support Project reflect an income of US\$ 10,798,597 representing amounts reimbursed by USAID as at 23 October 1998.

4 Project Expenditure

As revenue is received following submission of details of actual disbursements, project expenditure represents amounts actually disbursed.

5. Indirect costs

Provisional indirect cost rates were established under the contract and amended as per amendment no 3 dated 23 January 1995 with retroactive effect to the beginning of the contract as follows:

<u>Description</u>	<u>Rates</u>	<u>Base</u>
Fringe benefits	34%	(a)
Overhead International	15%	(b)
General and Administrative (G&A)	18%	(c)

(a) Total labor dollars,

(b) Direct labor dollars (including B&P) and applicable fringe benefits and allowances,

(c) Total costs excluding G&A costs less subcontract costs greater than USD 50,000 per year and per subcontract, not to exceed USD 400,000 per year for anyone contract.

6 Other direct costs

The disbursements made under this category can be disclosed as follows

Video/Audio Taping	27,539
Outside Labor	205,163
Conferences	14,425
Computer software	22,583
Moving & Storage	38,573
Books	1,895
Printing	2,988
Rent	185,325
Repair & Maintenance	542,523
Recruitment & Relocation	70,972
Postage & Freight	114,229
Insurance	27,843
Office supplies	518,705
Reproduction	161,788
Telephone	<u>126,562</u>
Total	<u>2,061,113</u>

7. Subcontracts

Two contracts were signed with subcontractors and the disbursements were made as follows

Development Associates, Inc	1,614,818
Austral, Consultoria e Projectos, Lda	<u>763,756</u>
	<u>2,378,574</u>

8 Fixed fee

As per contract agreement, in addition to the reimbursements of costs a fixed fee was paid. Until 85% of the total fee was paid, the fee was paid at the same ratio of invoiced costs to total estimated costs. The total contracted fixed fee was agreed as per amendment no 8, dated 27 June 1997.

9 Award fee

Upon certification by the USAID/Mozambique COTR of successful completion of the critical tasks set forth in the Section C 7 "Contractor Benchmark" of the contract agreement an award fee was to be paid amounting USD 173,192. Amendment No 5 of 1st November 1996 and Amendment No 8 dated 27 June 1997 modified the indicators of performance and achievement maintaining the award fee at the same amount as per contract agreement.

SECTION C

INTERNAL CONTROL STRUCTURE

USAID Resources Managed by University Research Corporation (URC) under the Primary
Health Care Support Project

Project No 656-0226

Contract No 656-0226-C-00-3019-00

Appropriation No 656-0226-3-10053/20047/20157/60022

**Africa Region**Chartered Accountants and
Management ConsultantsAv Zedequias Manganhela 95
4º Andar Maputo 2581
Mozambique
Caixa Postal 4318
Maputo 2581
Mozambique
Tel (1) 420955/430594
Fax (1) 429163
Int Dialing Code +(258)**Board of Directors
URC - University Research Corporation**

We have audited the Fund Accountability Statement of USAID Resources managed by University Research Corporation (URC) under the Primary Health Care Support Project under the USAID Contract No 656-0226-C-00-3019-00 for the period January 10, 1994 to October 23, 1998 and have issued a report thereon dated 15 October 1999

Except as discussed in the following paragraphs, we concluded our audit in accordance with generally accepted auditing standards and U S Government Auditing Standards issued by the Controller General of the United States (1994 Revision) These standards require that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statement is free of material misstatement An audit includes examining, on a test basis, evidence supporting the amount and disclosures in the Fund Accountability Statement An audit also includes assessing the accounting principles and significant estimates made by management, as well as evaluating the overall financial statement presentation We believe that our audit provides a reasonable basis for our opinion

We do not have a continuing education program that fully satisfies the requirements set forth in Chapter 3, Paragraph 6 of the U S Government Auditing Standards However, our current program provides for at least 24 hours continuing education and training every two years We are taking appropriate steps to implement a continuing education program that fully satisfies the requirement

We did not have an external quality control review by an unaffiliated audit organization as required by Chapter 3, Paragraph 46 of U S Government Auditing Standards, since no such program is offered to professional organizations in Mozambique We believe that the effects of this departure from U S Government Auditing Standards is not material because we participate in the Deloitte Touche Tohmatsu International world wide internal control review program which requires our office to be subjected every three years, to an extensive quality control review by partners and managers from other affiliate offices

In planning and performing our audit of the Fund Accountability Statement of USAID Resources managed by University Research Corporation (URC) under the Primary Health Care Support Project for the period January 10, 1994 to October 23, 1998, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the Fund Accountability Statement and not to provide assurance on the internal control structure

The management of URC is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of internal control structures, policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that the assets are safeguarded against loss from unauthorized use or disposition and that transactions are recorded properly to permit the preparation of the Fund Accountability Statement. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection for any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

Control Environment

- * Defined management and responsibility levels
- * Personnel procedures and staff selection policies
- * Management reporting framework

Accounting Systems

- * Project accounting
- * Salaries
- * Receipts and disbursements

Control Procedures

- * Authorization of transactions
- * Segregation of duties
- * Reconciliation of bank accounts and creditors
- * Use of prenumbered documents

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

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the fund accountability statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control structure and its operation that we consider to be material weaknesses as defined above.

The report is intended for the information of URC and the U.S. Agency for International Development. However, upon acceptance by the AID Regional Inspector General, this report is a matter of public record and its distribution is not limited.

Maputo, 15 October 1999



Deloitte & Touche

SECTION D

**COMPLIANCE WITH AGREEMENT TERMS AND APPLICABLE LAWS AND
REGULATIONS**

USAID Resources Managed by University Research Corporation (URC) under the Primary
Health Care Support Project

Project No 656-0226

Contract No 656-0226-C-00-3019-00

Appropriation No 656-0226-3-10053/20047/20157/60022

**Africa Region**Chartered Accountants and
Management ConsultantsAv Zedequias Manganhela 95
4º Andar Maputo 2581
Mozambique
Caixa Postal 4318
Maputo 2581
Mozambique
Tel (1) 420955/430594
Fax (1) 429163
Int Dialing Code +(258)**Board of Directors
URC - University Research Corporation****REPORT OF THE INDEPENDENT AUDITORS ON COMPLIANCE WITH
AGREEMENT TERMS AND APPLICABLE LAWS AND REGULATIONS**

We have audited the Fund Accountability Statement of USAID Resources Managed by University Research Corporation (URC) under the Primary Health Care Support Project under the USAID Contract No 656-0226-C-00-3019-00 for the period January 10, 1994 to October 23, 1998 and have issued a report thereon dated 15 October 1999

Except for not having a fully satisfactory continuing education program and not conducting an external quality control review by an unaffiliated audit organization (as described in our report on the Fund Accountability Statement), we conducted our audit in accordance with generally accepted auditing standards and U S Government Auditing Standards, issued by the Controller General of the United States (1994 Revision) Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statement is free of material misstatement

We do not have a continuing education program that fully satisfies the requirements set forth in Chapter 3, Paragraph 6 of the U S Government Auditing Standards However, our current program provides for at least 24 hours of continuing education and training every two years We are taking the appropriate steps to implement a continuing education program that fully satisfies the requirement

We did not have an external quality control review by an unaffiliated audit organization as required by Chapter 3, Paragraph 46 of U S Government Auditing Standards, since no such program is offered to professional organizations in Mozambique We believe that the effects of this departure from U S Government Auditing Standards is not material because we participate in the Deloitte Touche Tohmatsu world-wide internal control review program which requires our office to be subjected every three years, to an extensive quality control review by partners and manager from affiliate offices

Compliance with agreement terms and laws and regulations applicable to USAID Resources managed by University Research Corporation (URC) under the Primary Health Care Support Project is the responsibility of the management of URC. As part of obtaining reasonable assurance about whether the Fund Accountability Statement is free of material misstatement, we performed tests to ensure URC's compliance with certain provisions of agreement terms, laws and regulations. However our objective was not to provide an opinion on overall compliance with such provisions. Accordingly we do not express such an opinion.

Material instances of non compliance are failure to follow requirements or violations of agreement terms and applicable laws and regulations that cause us to conclude that the aggregation of misstatement resulting from those failures or violations is material to the fund accountability statement. The results of our tests did not disclose any instances of non-compliance.

The results of our tests, with respect to the items tested indicate that URC complied, in all material respects, with the provisions referred to in the fifth paragraph of the report. With respect to items not tested nothing came to our attention that caused us to believe that URC had not complied, in all material respects with those provisions.

This report is intended for the information of management and others within the organization, and the U S Agency of International Development. However, upon acceptance by the A I D Regional Inspector General this report is a matter of public record and its distribution is not limited.

Maputo, 15 October 1999



Deloitte & Touche

SECTION E

General Purpose annual financial statements

USAID Resources Managed by University Research Corporation (URC)

UNIVERSITY RESEARCH CO , LLC

FINANCIAL STATEMENTS

Year ended September 30, 1998

and

INDEPENDENT AUDITORS' REPORT



Rubino & McGeehin
C H A R T E R E D
Certified Public Accountants

6905 Rockledge Drive
Suite 700
Bethesda Maryland 20817 1818
301 564 3636
FAX 301 564 2994

Colorado Office
1221 Pearl Street
Boulder Colorado 80302
303 413 0215
FAX 303 413 0360

Shareholders

Mark Blucas
Craig A. Carlini
Margaret A. DeBoe
A. Michael Gellman
Robert N. Gray
William M. Kline
Matthew R. Kraft
Patrick A. McGeehin
Louis J. Rubino Jr.
James D. Warring
Wilcy R. Wright III

Independent Auditors' Report

Board of Directors
University Research Co., LLC
7200 Wisconsin Avenue
Bethesda, Maryland

We have audited the accompanying balance sheet of University Research Co., LLC as of September 30, 1998, and the related statements of operations and member's equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of University Research Co., LLC as of September 30, 1998, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

January 5, 1999

UNIVERSITY RESEARCH CO , LLC
BALANCE SHEET
SEPTEMBER 30, 1998

ASSETS

Current Assets

Cash	\$ 2,323,847
Accounts receivable	2,961,539
Due from affiliated company	188,275
Income tax receivable	108,590
Other	<u>83,391</u>

5,665,642

Fixed Assets

Furniture and equipment	275,410
Less accumulated depreciation	<u>(200,822)</u>

74,588

Other Assets

Investments	<u>141,009</u>
-------------	----------------

\$ 5,881,239

See notes to financial statements

UNIVERSITY RESEARCH CO , LLC
BALANCE SHEET
SEPTEMBER 30, 1998

LIABILITIES AND MEMBER'S EQUITY

Current Liabilities

Accounts payable	\$ 1,064,231
Billings on contracts in progress in excess of costs incurred and income recognized	1,550,000
Accrued salaries and payroll withholdings	847,781
Other accrued liabilities	236,091
Income taxes payable	<u>1,222,250</u>
	<u>4,920,353</u>

Member's Equity

Member's equity	<u>960,886</u>
-----------------	----------------

\$ 5,881,239

See notes to financial statements

UNIVERSITY RESEARCH CO , LLC
 STATEMENT OF OPERATIONS AND MEMBER'S EQUITY
 YEAR ENDED SEPTEMBER 30, 1998

<i>Income</i>	
Contracts	\$ 15,394,884
Interest and other income	18,870
	<u>15,413,754</u>
 <i>Costs and Expenses</i>	
Direct contract costs	
Salaries and other direct costs	8,064,967
Subcontract costs	4,067,117
	<u>12,132,084</u>
Indirect expenses	2,249,302
	<u>14,381,386</u>
Income before provision for income taxes	1,032,368
Provision for income taxes	1,309,056
	<u>(276,688)</u>
<i>Net Loss</i>	<u>(276,688)</u>
Equity - beginning	3,443,347
Adjustments related to reorganization as limited liability company	
Redemption of stock	(500,000)
Elimination of note receivable from member	(1,705,773)
	<u>960,886</u>
<i>Member's equity - ending</i>	<u>\$ 960,886</u>

See notes to financial statements

UNIVERSITY RESEARCH CO , LLC
STATEMENT OF CASH FLOWS
YEAR ENDED SEPTEMBER 30, 1998

<i>Cash Flows From Operating Activities</i>	
Net income	\$ (276,688)
Adjustments to reconcile net income to cash provided by operating activities	
Depreciation and amortization	38,977
Deferred tax provision	84,896
Change in assets and liabilities	
Accounts receivable, net	440,538
Due from affiliates	117,353
Income taxes receivable	(108,590)
Other current assets	271,895
Accounts payable and accrued expenses	16,807
Accrued salaries and withholdings	(12,428)
Billings on contracts in progress in excess of costs incurred and income recognized	(272,064)
Income taxes payable	1,212,750
	<u>1,790,134</u>
Net cash provided by operating activities	<u>1,513,446</u>
<i>Cash Flows From Investing Activities</i>	
Purchase of property and equipment	(61,912)
Disposition of investments	50,000
Increase in note receivable	(220,000)
Distributions from investments	12,560
	<u>(219,352)</u>
Net cash used in investing activities	<u>(219,352)</u>
<i>Cash Flows From Financing Activities</i>	
Redemption of stock	(500,000)
	<u>(500,000)</u>
<i>Net increase in cash</i>	794,094
Cash - beginning of year	<u>1,529,753</u>
<i>Cash - end of year</i>	<u><u>\$ 2,323,847</u></u>
 Supplemental disclosure of cash flow information	
Cash paid during the year	
Income taxes	\$ 120,000
Interest	\$ 2,627

See notes to financial statements

UNIVERSITY RESEARCH CO , LLC

NOTES TO FINANCIAL STATEMENTS

1 *Summary of Significant Accounting Policies*

Accounting policies which affect significant aspects of the Company's financial position and results of operations are summarized below

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Revenue Recognition

The Company derives substantially all of its revenue from consulting contracts with the US Government and its Agencies, specifically the Agency for International Development and the Department of Health and Human Services. Revenue from cost-plus-fixed-fee contracts is recorded on the basis of direct costs incurred plus indirect expenses and the allocable portion of the fixed fee. Revenue under time and materials contracts is recorded at the contracted rates as the labor hours and other direct costs are incurred. Revenue under fixed price contracts is recorded on the basis of the estimated percentage of completion of services rendered. Anticipated losses on contracts are recognized as soon as they become known. Changes in job performance, job conditions, and estimated profitability, including final contract settlements, may result in revisions to costs and income and are recognized in the period in which the revisions are determined.

Billings under cost-plus-fixed-fee contracts are based on provisional rates, which allow tentative recovery of direct and indirect expenses. When final determination and approval of the allowable rates have been made, billings are adjusted accordingly. Allowable rates have been determined and approved through September 30, 1996.

Allowance for Doubtful Accounts

The Company provides an allowance for doubtful accounts for receivables which may be uncollectible.

Property and Equipment

Property and equipment are stated at cost. Such assets purchased under federal contracts which are subject to reversion to the federal government are charged to expense as contract costs. Depreciation is computed on the straight-line and accelerated methods over the estimated useful lives of the related assets.

UNIVERSITY RESEARCH CO , LLC
NOTES TO FINANCIAL STATEMENTS

1 *Summary of Significant Accounting Policies (cont'd)*

Statement of Cash Flows

For the purposes of the presentation of the Statement of Cash Flows, the Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents

The Company maintains deposits with federally insured financial institutions. At times balances exceed federally insured limits. Management, however, does not consider this to be a significant concentration of credit risk.

2 *Accounts Receivable*

Accounts receivable consist of the following at September 30, 1998

Federal government	\$1,334,314
Federal government contractors	898,803
Commercial	774,422
Allowance for doubtful accounts	<u>(46,000)</u>
	<u>\$2,961,539</u>

3 *Due From Affiliated Companies*

The Company has made non-interest bearing advances to related companies which are under common management control.

4 *Line of Credit*

The Company has a line of credit agreement for a maximum of \$1.5 million. Borrowings under the line of credit agreement bear interest at the Wall Street Journal prime rate plus 1% with interest payable quarterly. The line of credit allows the Company to borrow against accounts receivable for working capital needs. The line of credit is secured by substantially all corporate assets and expires April 1, 1999. There was no outstanding balance as of September 30, 1998. In addition, the line of credit agreement contains minimum tangible net worth and other financial covenants for the Company.

5 *Retirement Plan*

The Company has a 401(k) retirement plan which covers substantially all employees. The Company makes contributions based upon employee compensation. Total employer contributions to the plan were \$189,000 for the year ended September 30, 1998.

UNIVERSITY RESEARCH CO , LLC

NOTES TO FINANCIAL STATEMENTS

6 *Income Taxes*

Effective August 1, 1998, the Company became a single member limited liability company (LLC) As the Company is not a taxpaying entity for federal income tax purposes, but rather, its revenue and expenses are included in the return of its member, no income tax expense is recorded in the financial statements for the period from August 1, 1998, through September 30, 1998 In addition, the deferred tax asset as of the beginning of the year has been eliminated However, income tax expense has been recorded for the period October 1, 1997 through August 1, 1998 The tax provision consists of the following

Current portion	\$1,224,160
Deferred portion	<u>84,896</u>
	<u>\$1,309,056</u>

The tax provision reflects the effect of state income taxes and the disallowance of certain deductions totaling approximately \$2,988,858 upon examination of prior years' tax returns by the Internal Revenue Service

7 *Commitments*

The Company leases office space and equipment under operating leases which expire at various dates through August, 2004 The future minimum annual rental payments for these leases as of September 30, 1998 are as follows for the years ending

September 30, 1999	\$ 461,027
September 30, 2000	511,903
September 30, 2001	509,873
September 30, 2002	509,873
September 30, 2003	509,873
September 30, 2004	<u>467,383</u>
Future minimum rental payments	<u>\$2,969,932</u>

Rent expense amounted to \$634,000 for the year ended September 30, 1998

UNIVERSITY RESEARCH CORPORATION

FINANCIAL STATEMENTS

Years ended September 30, 1997 and 1996

and

INDEPENDENT AUDITORS' REPORT



Rubino & McGeehin

C H A R T E R E D

Certified Public Accountants

6905 Rockledge Drive

Suite 700

Bethesda Maryland 20817 1818

301 564 3636

FAX 301 564 2994

sharchou r s

Independent Auditors' Report

Board of Directors
University Research Corporation
7200 Wisconsin Avenue
Bethesda, Maryland

We have audited the accompanying balance sheets of University Research Corporation as of September 30, 1997 and 1996 and the related statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of University Research Corporation as of September 30, 1997 and 1996, and the results of its operations and cash flows for the years then ended in conformity with generally accepted accounting principles.

November 21, 1997

UNIVERSITY RESEARCH CORPORATION

BALANCE SHEETS

ASSETS

	<u>September 30,</u>	
	<u>1997</u>	<u>1996</u>
<i>Current Assets</i>		
Cash	\$ 1,529,753	\$ 861,616
Note receivable, current portion	666,756	592,735
Accounts receivable	3,402,078	2,622,489
Due from affiliated company	305,628	-
Income taxes receivable	-	896,798
Deferred tax asset	-	31,315
Other	355,286	210,546
	<u>6,259,501</u>	<u>5,215,499</u>
 <i>Fixed Assets</i>		
Furniture and equipment	269,169	258,923
Less accumulated depreciation	<u>(217,517)</u>	<u>(184,803)</u>
	<u>51,652</u>	<u>74,120</u>
 <i>Other Assets</i>		
Note receivable	819,017	1,385,773
Investments	203,569	400,000
Deferred tax asset	<u>84,896</u>	<u>132,000</u>
	<u>1,107,482</u>	<u>1,917,773</u>
	<u>\$ 7,418,635</u>	<u>\$ 7,207,392</u>

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS' EQUITY

	September 30,	
	<u>1997</u>	<u>1996</u>
<i>Current Liabilities</i>		
Accounts payable	\$ 966,730	\$ 1,142,097
Billings on contracts in progress in excess of costs incurred and income recognized	1,822,064	1,463,450
Accrued salaries and payroll withholdings	860,209	713,629
Other accrued liabilities	316,785	340,319
Due to affiliated companies	-	259,609
Income taxes payable	9,500	-
	<u>3,975,288</u>	<u>3 919,104</u>
 <i>Stockholders' Equity</i>		
Common stock, no par value, 1,500 shares authorized, 1,337 shares issued and outstanding	51,072	51,072
Retained earnings	3 392,275	3 237 216
	<u>3 443,347</u>	<u>3 288 288</u>
	<u>\$ 7 418,635</u>	<u>\$ 7 207,392</u>

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

STATEMENTS OF OPERATIONS AND RETAINED EARNINGS

	Year ended September 30,	
	1997	1996
<i>Income</i>		
Contracts	\$ 14,511,384	\$ 14,452,042
Interest and other income	212,514	252,948
	<u>14,723,898</u>	<u>14,704,990</u>
 <i>Costs and Expenses</i>		
Direct contract costs		
Salaries and other direct costs	7,610,169	6,920,532
Subcontract costs	4,074,549	4,314,380
	<u>11,684,718</u>	<u>11,234,912</u>
Indirect expenses	2,786,536	3,233,678
Bad debt	-	2,338,858
	<u>14,471,254</u>	<u>16,807,448</u>
Income (loss) before provision for income taxes	252,644	(2,102,458)
Provision (benefit) for income taxes	<u>97,585</u>	<u>(803,488)</u>
<i>Net Income (Loss)</i>	155,059	(1,298,970)
Retained earnings - Beginning of year	<u>3,237,216</u>	<u>4,536,186</u>
<i>Retained earnings - End of year</i>	<u>\$ 3,392,275</u>	<u>\$ 3,237,216</u>

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

STATEMENTS OF CASH FLOWS

	Year ended September 30,	
	1997	1996
<i>Cash Flows From Operating Activities</i>		
Net income (loss)	\$ 155,059	\$ (1,298,970)
Adjustments to reconcile net income to cash provided by operating activities		
Depreciation and amortization	33,040	43,727
Deferred tax provision	78,419	(31,315)
Bad debt expense	-	2,338,858
Change in assets and liabilities		
Accounts receivable, net	(779,589)	582,122
Due to/from affiliates	(565,237)	365,905
Income taxes receivable	896,798	(896,798)
Other current assets	(144,740)	(177,314)
Accounts payable and accrued expenses	(198,901)	164,806
Accrued salaries and withholdings	146,580	(42,122)
Billings on contracts in progress in excess of costs incurred and income recognized	358,614	(106,261)
Income taxes payable	9,500	(265,375)
	(165,516)	1,976,233
Net cash (used in) provided by operating activities	(10,457)	677,263
<i>Cash Flows From Investing Activities</i>		
Purchase of property and equipment	(10,572)	(12,677)
Purchase of investments	(3,569)	(416,667)
Decrease in note receivable	492,735	1,541,499
Distributions from investments	200,000	16,667
Increase in note receivable	-	(2,338,858)
Net cash provided by (used in) investing activities	678,594	(1,210,036)
<i>Net (decrease) increase in cash</i>	668,137	(532,773)
Cash - Beginning of year	861,616	1,394,389
<i>Cash - End of year</i>	\$ 1,529,753	\$ 861,616
<i>Supplemental disclosure of cash flow information</i>		
Cash paid during the year		
Income taxes	\$ -	\$ 390,000

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

1 *Summary of Significant Accounting Policies*

Accounting policies which affect significant aspects of the Company's financial position and results of operations are summarized below

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Revenue Recognition

The Company derives substantially all of its revenue from consulting contracts with the U.S. Government and its Agencies, specifically the Agency for International Development and Health and Human Services. Revenue from cost-plus-fixed-fee contracts is recorded on the basis of direct costs incurred plus indirect expenses and the allocable portion of the fixed fee. Revenue under time and materials contracts is recorded at the contracted rates as the labor hours and other direct costs are incurred. Revenue under fixed price contracts is recorded on the basis of the estimated percentage of completion of services rendered. Anticipated losses on contracts are recognized as soon as they become known. Changes in job performance, job conditions, and estimated profitability, including final contract settlements, may result in revisions to costs and income and are recognized in the period in which the revisions are determined.

Billings under cost-plus-fixed-fee contracts are based on provisional rates which allow tentative recovery of direct and indirect expenses. When final determination and approval of the allowable rates have been made, billings are adjusted accordingly. Allowable rates have been determined and approved through September 30, 1995.

Allowance for Doubtful Accounts

The Company provides an allowance for doubtful accounts for receivables which may be uncollectible.

Property and Equipment

Property and equipment are stated at cost. Depreciation is computed on the straight-line and accelerated methods over the estimated useful lives of the related assets.

Statements of Cash Flows

For the purposes of the presentation of the Statements of Cash Flows, the Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

2. *Note Receivable*

The Company has a note receivable from an affiliated company under common management control in the original amount of \$3,975,000, dated December 17, 1993 which bears interest at 6% per annum. The note balance and accrued interest at September 30, 1997 is \$1,485,773 and \$83,244 and at September 30, 1996 is \$1,978,508 and \$157,265. Principal and interest are due December 17, 2003, however, the Company received principal and interest payments totaling \$650,000 during the year ending September 30, 1997.

3 *Accounts Receivable*

Accounts receivable consist of the following at September 30, 1997 and 1996

	<u>1997</u>	<u>1996</u>
Federal government	\$2,273,702	\$1,940,048
Federal government contractors	686,008	658,464
Commercial	488,368	114,977
Allowance for doubtful accounts	<u>(46,000)</u>	<u>(91,000)</u>
	<u>\$3,402,078</u>	<u>\$2,622,489</u>

4 *Due To/From Affiliated Companies*

The Company has made and received non-interest bearing advances to and from related companies which are under common management control.

5 *Line of Credit*

The Company has a line of credit agreement for a maximum of \$1.5 million. Borrowings under the line of credit agreement bear interest at the Wall Street Journal prime rate plus 1% with interest payable quarterly. The line of credit allows the Company to borrow against accounts receivable for working capital needs. The line of credit is secured by substantially all corporate assets and expires March 1, 1998. There was no outstanding balance as of September 30, 1997. In addition, the line of credit agreement contains minimum tangible net worth and other financial covenants for the Company.

6 *Retirement Plan*

The Company has a 401(k) retirement plan which covers substantially all employees. The Company makes contributions based upon employee compensation. Total employer contributions to the plan were \$150,000 and \$177,000 for the years ended September 30, 1997 and 1996, respectively.

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

7 *Income Taxes*

The Company utilizes the accrual accounting method for income tax purposes. The provision (benefit) for income taxes consists of the following:

	1997	1996
Current portion	\$ 19,166	\$ (772,173)
Deferred portion	78,419	(31,315)
	\$ 97,585	\$ (803,488)

The actual provision for income taxes differs from that expected using the federal statutory rate, due primarily to the effect of state income taxes.

The income tax receivable and benefit for the year ended September 30, 1996 resulted from a carryback of the net operating loss (NOL) incurred. A current deferred tax asset was recognized at September 30, 1996 for the NOL available and used for the year ended September 30, 1997. The noncurrent deferred tax asset resulted from a charitable contribution expense carryforward which expires in 1999.

The deductions resulting in the NOL benefit and deferred tax asset are subject to examination by the Internal Revenue Service. Any disallowance would adversely affect the ultimate realization of those assets.

8 *Bad Debt Expense*

The Company reflected a bad debt expense as of September 30, 1996, a loan of \$2,338,858 made to a Limited Partnership. The Company and the Limited Partnership have management relationships.

9 *Commitments*

The Company leases office space and equipment under operating leases which expire at various dates through November, 1999. The future minimum annual rental payments for these leases as of September 30, 1997 are as follows for the years ending:

September 30, 1998	457,052
September 30, 1999	418,538
September 30, 2000	2,030
Future minimum rental payments	\$ 877,620

Rent expense amounted to \$833,000 and \$757,000 for the years ended September 30, 1997 and 1996, respectively.

10 *Subsequent Event*

Subsequent to the balance sheet date, the Company acquired a minority stockholder's shares of stock for \$500,000.

UNIVERSITY RESEARCH CORPORATION

FINANCIAL STATEMENTS

Years ended September 30, 1996 and 1995

and

INDEPENDENT AUDITORS' REPORT



Rubino & McGeehin

C H A R T E R E D

Certified Public Accountants

6905 Rockledge Drive

Suite 700

Bethesda Maryland 20817 1818

301 564 3636

FAX 301 564 2994

Shareholders

Independent Auditors' Report

Board of Directors
University Research Corporation
7200 Wisconsin Avenue
Bethesda Maryland

We have audited the accompanying balance sheets of University Research Corporation as of September 30, 1996 and 1995 and the related statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of University Research Corporation as of September 30, 1996 and 1995, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

November 27, 1996

UNIVERSITY RESEARCH CORPORATION

BALANCE SHEETS

ASSETS

	September 30,	
	<u>1996</u>	<u>1995</u>
<i>Current Assets</i>		
Cash	\$ 861,616	\$ 1,394,389
Note receivable current portion	592,735	732,641
Accounts receivable	2,622,489	3,204,611
Due from affiliated company	-	106,296
Income taxes receivable	896,798	-
Deferred tax asset	31,315	-
Other	210,546	33,232
	<u>5,215,499</u>	<u>5,471,169</u>
 <i>Fixed Assets</i>		
Furniture and equipment	258,923	246,246
Less accumulated depreciation	<u>(184,803)</u>	<u>(141,076)</u>
	<u>74,120</u>	<u>105,170</u>
 <i>Other Assets</i>		
Note receivable	1,385,773	2,787,366
Investments	400,000	-
Deferred tax asset	<u>132,000</u>	<u>132,000</u>
	<u>1,917,773</u>	<u>2,919,366</u>
	<u>\$ 7,207,392</u>	<u>\$ 8,495,705</u>

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS' EQUITY

	September 30,	
	<u>1996</u>	<u>1995</u>
<i>Current Liabilities</i>		
Accounts payable	\$ 1,142,097	\$ 1,168,420
Billings on contracts in progress in excess of costs incurred and income recognized	1,463,450	1,569,711
Accrued salaries and payroll withholdings	713,629	755,751
Other accrued liabilities	340,319	149,190
Due to affiliated companies	259,609	-
Income taxes payable	-	265,375
	<u>3,919,104</u>	<u>3,908,447</u>
 <i>Stockholders' Equity</i>		
Common stock, no par value, 1,500 shares authorized, 1,337 shares issued and outstanding	51,072	51,072
Retained earnings	3,237,216	4,536,186
	<u>3,288,288</u>	<u>4,587,258</u>
	<u>\$ 7,207,392</u>	<u>\$ 8,495,705</u>

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

STATEMENTS OF OPERATIONS AND RETAINED EARNINGS

	<u>Year ended September 30,</u>	
	<u>1996</u>	<u>1995</u>
<i>Income</i>		
Contracts	\$ 14,452,042	\$ 17,371,847
Interest and other income	252,948	280,327
	<u>14,704,990</u>	<u>17,652,174</u>
<i>Costs and Expenses</i>		
Direct contract costs		
Salaries and other direct costs	6,920,532	8,674,511
Subcontract costs	4,314,380	4,404,936
	11,234,912	13,079,447
Indirect expenses	3,233,678	3,646,790
Bad debt	2,338,858	-
	<u>16,807,448</u>	<u>16,726,237</u>
Income (loss) before provision for income taxes	(2,102,458)	925,937
Provision (benefit) for income taxes	<u>(803,488)</u>	<u>364,800</u>
<i>Net Income (Loss)</i>	(1,298,970)	561,137
Retained earnings - Beginning of year	<u>4,536,186</u>	<u>3,975,049</u>
<i>Retained earnings - End of year</i>	<u>\$ 3,237,216</u>	<u>\$ 4,536,186</u>

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

STATEMENTS OF CASH FLOWS

	Year ended September 30,	
	1996	1995
<i>Cash Flows From Operating Activities</i>		
Net income (loss)	\$ (1,298,970)	\$ 561,137
Adjustments to reconcile net income to cash provided by operating activities		
Depreciation and amortization	43,727	33,730
Deferred tax provision	(31,315)	33,000
Bad debt expense	2,338,858	-
Change in assets and liabilities		
Accounts receivable net	582,122	1,068,697
Due to/from affiliates	365,905	(57,522)
Income taxes receivable	(896,798)	-
Other current assets	(177,314)	131,388
Accounts payable and accrued expenses	164,806	(885,916)
Accrued salaries and withholdings	(42,122)	(55,271)
Billings on contracts in progress in excess of costs incurred and income recognized	(106,261)	(262,853)
Income taxes payable	(265,375)	265,375
	<u>1,976,233</u>	<u>270,628</u>
Net cash provided by operating activities	<u>677,263</u>	<u>831,765</u>
<i>Cash Flows From Investing Activities</i>		
Purchase of property and equipment	(12,677)	(28,336)
Purchase of investments	(416,667)	-
Decrease in note receivable	1,541,499	452,353
Distributions from investments	16,667	-
Increase in note receivable	(2,338,858)	-
Net cash (used in) provided by investing activities	<u>(1,210,036)</u>	<u>424,017</u>
<i>Net (decrease) increase in cash</i>	(532,773)	1,255,782
Cash - Beginning of year	<u>1,394,389</u>	<u>138,607</u>
<i>Cash - End of year</i>	<u>\$ 861,616</u>	<u>\$ 1,394,389</u>
<i>Supplemental disclosure of cash flow information</i>		
Cash paid during the year		
Income taxes	<u>\$ 390,000</u>	<u>\$ -</u>

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

1 *Summary of Significant Accounting Policies*

Accounting policies which affect significant aspects of the Company's financial position and results of operations are summarized below

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Revenue Recognition

The Company derives substantially all of its revenue from consulting contracts with the U.S. Government and its Agencies, specifically the Agency for International Development and Health and Human Services. Revenue from cost-plus-fixed-fee contracts is recorded on the basis of direct costs incurred plus indirect expenses and the allocable portion of the fixed fee. Revenue under time and materials contracts is recorded at the contracted rates as the labor hours and other direct costs are incurred. Revenue under fixed price contracts is recorded on the basis of the estimated percentage of completion of services rendered. Anticipated losses on contracts are recognized as soon as they become known. Changes in job performance, job conditions, and estimated profitability, including final contract settlements, may result in revisions to costs and income and are recognized in the period in which the revisions are determined.

Billings under cost-plus-fixed-fee contracts are based on provisional rates which allow tentative recovery of direct and indirect expenses. When final determination and approval of the allowable rates have been made, billings are adjusted accordingly. Allowable rates have been determined and approved through September 30, 1993.

Allowance for Doubtful Accounts

The Company provides an allowance for doubtful accounts for receivables which may be uncollectible.

Property and Equipment

Property and equipment are stated at cost. Depreciation is computed on the straight-line and accelerated methods over the estimated useful lives of the related assets.

Statements of Cash Flows

For the purposes of the presentation of the Statements of Cash Flows, the Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

2 *Note Receivable*

The Company has a note receivable from an affiliated company under common management control in the original amount of \$3,975,000, dated December 17, 1993 which bears interest at 6% per annum. The note balance and accrued interest at September 30, 1996 is \$1,978,508 and \$157,265 and at September 30, 1995 is \$3,520,007 and \$17,359. Principal and interest are due December 17, 2003, however the Company received principal and interest payments totaling \$1,558,858 during the year ending September 30, 1996.

3 *Accounts Receivable*

Accounts receivable consist of the following at September 30, 1996 and 1995

	<u>1996</u>	<u>1995</u>
Federal government	\$1,940,048	\$2,433,264
Federal government contractors	658,464	542,781
Commercial	114,977	306,566
Allowance for doubtful accounts	<u>(91,000)</u>	<u>(78,000)</u>
	<u>\$2,622,489</u>	<u>\$3,204,611</u>

4 *Due To/From Affiliated Companies*

The Company has made and received non-interest bearing advances to and from related companies which are under common management control.

5 *Bad Debt Expense*

In July 1996 the Company loaned \$2,338,858 in the form of a convertible demand promissory note, bearing interest at the Wall Street Journal prime rate plus 1% to a Limited Partnership. The terms included the right for the Company to convert the outstanding principal balance of the note into a Limited Partnership interest. The Company and the Limited Partnership have management relationships. The principal asset of the Limited Partnership was an investment in a New York Stock Exchange company. As of September 30, 1996, the investment had insignificant value and the partnership has insufficient assets to repay the loan. Accordingly, the loan is reflected as a bad debt expense as of September 30, 1996.

6 *Line of Credit*

The Company has a line of credit agreement for a maximum of \$1.5 million. Borrowings under the line of credit agreement bear interest at the Wall Street Journal prime rate plus 1% with interest payable quarterly. The line of credit allows the Company to borrow against accounts receivable for working capital needs. The line of credit is secured by substantially all corporate assets and expires March 1, 1997. There was no outstanding balance as of September 30, 1996. In addition, the line of credit agreement contains minimum tangible net worth and other financial covenants for the Company.

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

7 *Income Taxes*

The Company utilizes the accrual accounting method for income tax purposes. The provision (benefit) for income taxes consists of the following:

	<u>1996</u>	<u>1995</u>
Current portion	\$(772,173)	\$ 331,800
Deferred portion	<u>(31,315)</u>	<u>33,000</u>
	<u>\$(803,488)</u>	<u>\$ 364,800</u>

The actual provision for income taxes differs from that expected using the federal statutory rate, due primarily to the effect of state income taxes.

The income tax receivable and benefit resulted from a carryback of the net operating loss (NOL) incurred during the year ended September 30, 1996. The unused NOL carryforward of \$76,150 is anticipated to be utilized during the year ending September 30, 1997 and accordingly, a current deferred tax asset has been recognized.

The noncurrent deferred tax asset resulted from a charitable contribution expense carryforward which expires in 1999. The unused contribution carryforward as of September 30, 1996 and 1995 was \$343,000.

The deductions resulting in the income tax receivable and deferred tax asset are subject to examination by the Internal Revenue Service. Any disallowance would adversely affect the ultimate realization of those assets.

8 *Retirement Plan*

The Company has a 401(k) retirement plan which covers substantially all employees. The Company makes contributions based upon employee compensation. Total employer contributions to the plan were \$177,000 and \$195,000 for the years ended September 30, 1996 and 1995, respectively.

9 *Commitments*

The Company leases office space and equipment under operating leases which expire at various dates through November 1999. The future minimum annual rental payments for these leases as of September 30, 1996 are as follows for the years ending:

September 30, 1997	\$ 457,052
September 30, 1998	457,052
September 30, 1999	418,538
September 30, 2000	<u>2,030</u>
Future minimum rental payments	<u>\$1,334,672</u>

Rent expense amounted to \$757,000 and \$863,000 for the years ended September 30, 1996 and 1995, respectively.

UNIVERSITY RESEARCH CORPORATION

FINANCIAL STATEMENTS

Years ended September 30, 1995 and 1994

AND

INDEPENDENT AUDITORS' REPORT



Rubino & McGeehin

C H A R T E R E D

Certified Public Accountants

2 Democracy Center
6903 Rockledge Drive
Suite 1400

Bethesda Maryland 20817 1818

301 564 3636

FAX 301 564 2994

Shareholders

Chairman

Director

Secretary

President

Member

Attorney

Accountant

Adviser

Independent Auditors' Report

Board of Directors
University Research Corporation
7200 Wisconsin Avenue
Bethesda, Maryland

We have audited the accompanying balance sheets of University Research Corporation as of September 30, 1995 and 1994 and the related statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of University Research Corporation as of September 30, 1995 and 1994, and the results of operations and cash flows for the years then ended in conformity with generally accepted accounting principles.

November 27, 1995

UNIVERSITY RESEARCH CORPORATION

BALANCE SHEETS

ASSETS

	September 30,	
	1995	1994
<i>Current Assets</i>		
Cash and equivalents	\$ 1,394,389	\$ 138,607
Note receivable, current portion (Note 2)	732,641	457,353
Accounts receivable (Note 3)	3,204,611	4,273,307
Due from affiliated company (Note 4)	106,296	48,774
Prepaid taxes	-	67,722
Other	33,232	96,898
	5,471,169	5,082,661
 <i>Fixed Assets</i>		
Furniture & equipment	246,246	247,361
Leasehold improvements	-	66,426
Less accumulated depreciation and amortization	(141,076)	(203,223)
	105,170	110,564
 <i>Other Assets</i>		
Note receivable (Note 2)	2,787,366	3,515,007
Deferred tax asset	132,000	165,000
	2,919,366	3,680,007
	\$ 8,495,705	\$ 8,873,232

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS' EQUITY

	September 30,	
	1995	1994
<i>Current Liabilities</i>		
Accounts payable	\$ 1,168,420	\$ 1,836,906
Billings on contracts in progress in excess of costs incurred and income recognized	1,569,711	1,832,564
Accrued salaries and payroll withholdings	755,751	811,021
Other accrued liabilities	149,190	366,620
Income taxes payable	265,375	-
	3,908,447	4,847,111
 <i>Commitments (Note 7)</i>		
 <i>Stockholders' Equity</i>		
Common stock, no par value, 1,500 shares authorized, 1,337 shares issued and outstanding	51,072	51,072
Retained earnings	4,536,186	3,975,049
	4,587,258	4,026,121
	\$ 8,495,705	\$ 8,873,232

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION
STATEMENTS OF OPERATIONS AND RETAINED EARNINGS

	<u>Year ended September 30,</u>	
	<u>1995</u>	<u>1994</u>
<i>Income</i>		
Contracts	\$ 17,371,847	\$ 15,826,127
Interest and other income	280,327	200,371
	<u>17,652,174</u>	<u>16,026,498</u>
 <i>Costs and Expenses</i>		
Direct contract costs		
Salaries and other direct costs	8,674,511	7,636,636
Subcontract costs	4,404,936	4,940,885
	<u>13,079,447</u>	<u>12,577,521</u>
Indirect expenses	<u>3,646,790</u>	<u>3,814,153</u>
	<u>16,726,237</u>	<u>16,391,674</u>
 Income (loss) before provision for income taxes	925,937	(365,176)
 Provision (benefit) for income taxes	<u>364,800</u>	<u>(173,600)</u>
 <i>Net Income (Loss)</i>	561,137	(191,576)
 Retained earnings - Beginning of year	<u>3,975,049</u>	<u>4,166,625</u>
 <i>Retained earnings - End of year</i>	<u>\$ 4,536,186</u>	<u>\$ 3,975,049</u>

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

STATEMENTS OF CASH FLOWS

	Year ended September 30,	
	1995	1994
<i>Cash Flows From Operating Activities:</i>		
Net income	\$ 561,137	\$ (191,576)
Adjustments to reconcile net income to cash provided by operating activities		
Depreciation and amortization	33,730	62,742
Deferred tax provision (benefit)	33,000	(165,000)
Change in assets and liabilities		
Accounts receivable, net	1,068,697	(1,515,950)
Due from affiliates	(57,522)	3,695,895
Other current assets	131,388	(86,246)
Accounts payable and accrued expenses	(885,916)	942,972
Accrued salaries and withholdings	(55,271)	(173,911)
Billings on contracts in progress in excess of costs incurred and income recognized	(262,853)	230,615
Income taxes payable	265,375	(21,878)
	270,628	2,969,239
Net cash provided by operating activities	831,765	2,777,663
<i>Cash Flows From Investing Activities:</i>		
Sale (purchase) of marketable securities	-	637,246
Purchase of property and equipment	(28,336)	(68,028)
Decrease (increase) in note receivable	452,353	(3,875,000)
Net cash provided by (used in) investing activities	424,017	(3,305,782)
<i>Net increase (decrease) in cash</i>	1,255,782	(528,119)
Cash and equivalents - Beginning of year	138,607	666,726
<i>Cash and equivalents - End of year</i>	\$ 1,394,389	\$ 138,607
Supplemental disclosure of cash flow information:		
Cash paid during the year		
Income taxes	\$ -	\$ 81,000

See notes to financial statements

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

1. *Summary of Significant Accounting Policies*

Revenue Recognition

The Company derives substantially all of its revenue from contracts with the U S Government and its Agencies Revenue from cost-plus-fixed-fee contracts is recorded on the basis of direct costs incurred plus indirect expenses and the allocable portion of the fixed fee Revenue under time and materials contracts is recorded at the contracted rates as the labor hours and other direct costs are incurred. Revenue under fixed price contracts is recorded on the basis of the estimated percentage of completion of services rendered Anticipated losses on contracts are recognized as soon as they become known.

Billings under cost-plus-fixed-fee contracts are based on provisional rates which allow tentative recovery of direct and indirect expenses When final determination and approval of the allowable rates have been made, billings are adjusted accordingly Allowable rates have been determined and approved through September 30, 1993

Allowance for Doubtful Accounts

The Company provides an allowance for doubtful accounts for receivables which may be uncollectible

Property, Equipment, and Leasehold Improvements

Property, equipment, and leasehold improvements are stated at cost Depreciation is computed on the straight-line and accelerated methods over the estimated useful lives of the related assets Leasehold improvements are amortized over the shorter of the asset life or the lease term.

Statements of Cash Flows

For the purposes of the presentation of the Statements of Cash Flows, the Company considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents

2. *Note Receivable*

The Company has a note receivable from an affiliated company in the original amount of \$3,975,000, dated December 17, 1993 The note balance at September 30, 1995 and 1994 is \$3,520,007 and \$3,972,360 and bears interest at 6% per annum. Principal and interest are due December 17, 2003, however, the Company received principal and interest payments totaling \$750,000 during the year ending September 30, 1995

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

3. *Accounts Receivable*

Accounts receivable consist of the following at September 30, 1995 and 1994

	<u>1995</u>	<u>1994</u>
Federal government	\$2,433,264	\$3,677,677
Federal government contractors	542,781	536,476
Commercial	306,566	147,154
Allowance for doubtful accounts	<u>(78,000)</u>	<u>(88,000)</u>
	<u>\$3,204,611</u>	<u>\$4,273,307</u>

4. *Due From Affiliated Company*

The Company has made non-interest bearing advances to a related company which is under common management control

5. *Income Taxes*

The Company utilizes the accrual accounting method for income tax purposes The provision for income taxes consists of the following

	<u>1995</u>	<u>1994</u>
Current portion	\$331,800	\$ (8,600)
Deferred portion	<u>33,000</u>	<u>(165,000)</u>
	<u>\$364,800</u>	<u>\$ (173,600)</u>

The deferred tax asset resulted from a charitable contribution expense carryforward which expires in 1999 The unused carryforward as of September 30, 1995 and 1994 was \$345,000 and \$425,000, respectively The actual provision for income taxes differs from that expected using the federal statutory rate, due primarily to the effect of state income taxes

6. *Retirement Plan*

The Company has a 401(k) profit sharing plan which covers substantially all employees The Company makes contributions based upon employee compensation. Total employer contributions to the plan were \$195,000 and \$180,000 for the years ended September 30, 1995 and 1994, respectively

UNIVERSITY RESEARCH CORPORATION

NOTES TO FINANCIAL STATEMENTS

7. *Commitments*

The Company leases office space and equipment under operating leases which expire at various dates through November, 1999. The future minimum annual rental payments for these leases as of September 30, 1995 are as follows for the years ending

September 30, 1996	\$ 698,389
September 30, 1997	698,389
September 30, 1998	698,389
September 30, 1999	642,221
September 30, 2000	<u>2,030</u>
Future minimum rental payments	<u>\$2,739,418</u>

Rent expense amounted to \$863,000 and \$911,000 for the years ended September 30, 1995 and 1994, respectively