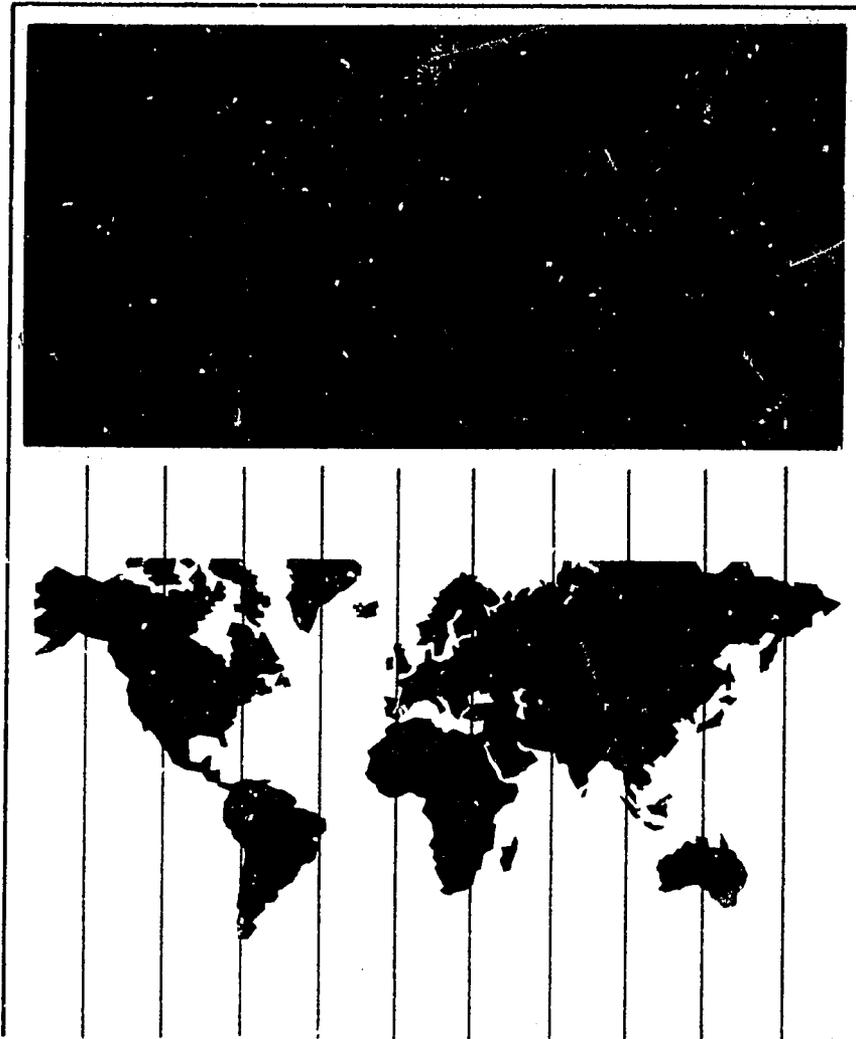


UNITED STATES
AGENCY FOR INTERNATIONAL DEVELOPMENT

THE
INSPECTOR
GENERAL



Regional Inspector General for Audit
NAIROBI

IG AUDITS CONTINUE TO SHOW THAT
HOST COUNTRY CONTRACTING PROCEDURES
WASTE AID FUNDS

AUDIT REPORT NO. 3-000-83-13
MARCH 30, 1983

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT
RIG/A/NAIROBI

March 30, 1983

TO :Mr. Herbert L. Beckington, Inspector General
FROM :Ray D. Cramer, RIG/A/Nairobi *R.D. Cramer*
SUBJECT: Memorandum Audit Report: IG Audits Continue To Show That
Host Country Contracting Procedures Waste AID Funds.
Audit Report No. 3-000-83-13

Our two recent audits of the PRC Harris (Harris) and the three Louis Berger International Inc. (LBII) host country contracts have again surfaced the inability of host governments and the Agency to effectively use host country contracting as a cost efficient management tool. (See A.R. 3-632-83-11, 3/18/83; and A.R. 3-623-83-12, 3/25/83.)

Significant problems with host country contracting were also noted in two prior IG audit reports. An audit report dated September 19, 1978 titled, "Implementation Of AID's Policy On Preference Of Mode Of Contracting In Bilateral Assistance Projects" contained the following statements regarding host country contracting:

- "Host country procurement personnel do not, as a rule, have the capability to perform the task of contracting under the policy."
- "It will be a long time, however, until most host governments are capable of effectively letting and administering AID-financed contracts at a reasonable cost."

Audit Report No. 79-71, dated May 19, 1979 titled "Review Of The Applications Of Host Country Contracting Mode" stated the following:

- "Although we are not able to quantify the additional costs, Borrower contracting for professional and technical services appears to have reduced the cost effectiveness of many AID-financed projects without measurable improvement on the Borrower's contracting capability."

- "Lack of Borrower contracting capability has delayed project implementation because of excessive time spent contracting."
- "The Missions are having to compensate for failure to properly evaluate Borrower contracting capability by providing assistance to the Borrower at all phases of the contracting process because no alternative courses of action were designed into the projects. This places an additional burden on Mission staff and uses time that would normally be spent monitoring the project."
- "The policy in its present form does not lend itself to practicality and cost effectiveness."

Although similar findings have been pointed out since 1978 little has been done to rectify the situation. Our two recent audits of Harris and LBII show that host government selection procedures are weak, that AID's right of recovery for non-performance is jeopardized, that cost effective contracts are not being negotiated, and that AID contracting assistance is ineffective. The net result is that AID funds are being wasted. These deficiencies are discussed in more detail in the following sections of this report.

Host Government Contractor Selection Procedures Are Weak

AID regulations require selection of a prospective contractor to be based exclusively on professional qualifications. Price is not a basis for competition. A price proposal is requested from the offeror submitting the highest ranked technical proposal, and then price is negotiated.

On two of the three LBII contracts we found that technical selection was based primarily on personnel to be provided. On one contract, over 60 percent of the overall criteria for selection was for proposed personnel. On the other, 70 percent. On these two contracts only one of the 22 technicians named in the proposals was eventually employed on the projects. The result is the technical selection was invalid, and LBII was awarded two contracts based on faulty technical evaluations. Host government's lack the capability to develop effective technical evaluation criteria to select the most technically qualified firm.

The inability of the contractor to provide the specific personnel included in the proposal is not unusual because of the long time lag between developing and submitting a proposal and providing the technicians to do the work. It is not unusual for this process to take up to a year. In fact, it is unreasonable to expect the proposed technicians to be available a year later. We conclude that giving personnel much weight in selecting a contractor is a weak

basis for selection. The USAID project officers and REDSO/EA contract personnel took no exception to this basis of selection, even though they were fully aware that it is virtually impossible for contractors to provide the technicians it proposes when a team is fielded.

We question the validity of the technical proposal and evaluation requirement as a sound basis for contractor selection when the contractor is merely providing bodies. The contractor has no way of guaranteeing that the bodies it provides will function effectively or will be technically capable. The Harris contract is a prime example of a technical proposal and selection process that resulted in the provision of bodies that were incapable of performing the duties required.

Technical proposals in conjunction with price proposals would be a more sound basis for contractor selection because it is virtually impossible to evaluate a technical proposal if there is no price tag associated with it. The technical proposal may be based on a cost significantly higher than available project funding. Without a price proposal this is not known. As costs are shaved during negotiation on the "best technical proposal", certain aspects of the proposal are undoubtedly deleted; thus the quality of the technical proposal diminishes making the original basis for selection questionable.

The Regional Economic Development Services Office/East Africa (REDSO/EA) Legal Advisor and Contracting Officer stated:

"... lack of price competition in the selection of host country contractors financed by AID is a drain on the U.S. Treasury. It is doubtful that the contractor selected for the procurements involved in this memo 1/ could compete successfully in terms of price with other U.S. contractors, based on previous direct contract bids (where price competition is required by statute) in other REDSO countries. If the resulting contract price for some or all of these contracts is higher than might be paid had there been price competition and more AID control in the contracting process, it is AID's world-wide policies in favor of host country contracting and its rule (exceptions authorized only by the Regional Assistant Administrator) not to consider price in the selection of host country contractors which are more at fault than the approving actions of the USAID officials involved."

1/ The memo referred to was a record of audit finding presented to REDSO/EA for their comments in connection with our audit of LBII.

AID's Procurement Policy Advisory Panel recently decided to not pursue further a procedure that would allow host countries, with the approval of the AID Mission Director, to consider cost as a factor in the selection of host country contractors to provide technical or professional services. The decision to not pursue further was based on opposition from the architect-engineering society, BIFAD and within AID. The policy which allows the Assistant Administrators to approve consideration of cost on a case-by-case basis will remain in effect.

In our opinion, if the host government must do the contracting, they should be given the opportunity to obtain for AID the most reasonable price. The current negotiation procedures are costing AID millions of dollars. Price competition, which the Government of Kenya favored for the Kenya ASAL project, appears to be a sound basis for final contractor selection.

Price competition would require two separate proposals -- a technical proposal and a price proposal. Under this concept the technical proposals are reviewed and the firms are ranked. Upon completion of the technical ranking, the price envelopes for the highest ranked firms are opened and price is then considered along with the technical proposals. This procedure is used by many state governments and by AID in some countries.

Inappropriate Types of Contracts Are Wasting AID Funds

We found that an inappropriate type of contract is being used by host governments -- time rate contracts are being negotiated which are costing the U.S. government millions of dollars. On the three LBII time rate contracts we estimate that over \$2 million in windfall profits will be made by the contractor and his employees.

The primary problem with time rate contracts is that the contractor can provide technicians who are paid much less than the salary on which the rate is based.

There are several reasons why windfall profits are being made. Host governments generally have no incentive to negotiate cost effective contracts because it's not their money. AID-missions have not demonstrated an incentive to save funds once obligated. Their attitude seems to be "as long as it is within the budget, spend it". The host governments have no basis for determining a reasonable price for a U.S. technical assistance team. AID, on the other hand, is ineffective in providing assistance because AID personnel in the field have no better idea what a good price is than does the host country. As a result, if the contractor gives a few concessions the host government and AID feels it has negotiated effectively.

Time rate contracts require less administrative surveillance because all that has to be shown by the contractor is that the technician has worked and that the fixed time rate was billed. Overhead and other cost principles, which the host government does not understand or have the capability to audit, can be ignored.

The net result is millions of dollars of AID funds are being wasted because inappropriate type contracts are used and approved by AID.

Host Country Contracts Limit AID's Legal Right Of Recovery

On the Harris contract AID's legal advisors provided verbal opinions that AID may not have an identifiable legal recourse criminally or civilly against Harris for violations committed by the technicians it supplied. This is apparently due to the concept that:

- AID was not a party to the contract.
- The laws of the host government apply.
- Team members recruited by Harris may in fact be employees of the Host Government.
- Nonperformance under the Suppliers Certificate is unquestionable because all the contractor has agreed to do is supply "warm bodies".

GC/TE made the following general comment to the Harris contract:

"The referenced case points out a virtually unavoidable cost associated with the 'host country contracting' mode. Despite significant indications of improper actions by the U.S. contractor to the Government of Lesotho, our sole - and possibly worthless - remedy against the contractor is through the AID 1440-3 (Suppliers Certificate). Because PRC Harris has no contractual relationship with AID we cannot recover on the contract. However, the AID 1440-3 provides a vehicle for civil recovery of the monies improperly certified if the Department of Justice will take this case."

The same situation applies to most host country contracts because the boiler plate provisions are the same on most contracts. This places AID in the position of not being able to protect itself against fraud, waste and abuse.

We believe consideration should be given to putting a clause in host country contracts to assign the same rights to AID as the host government has, or putting a clause in the project agreements to assign the rights of the host countries to AID. This would provide AID with the legal right to go against the contractor for waste, fraud or abuse.

AID Contracting Assistance Is Ineffective

These four host country contracts show how ineffective AID is in ensuring that it is approving a contract that is in the **best** interest of AID.

Host country contracting takes the primary responsibility for the whole contracting process away from AID. AID's major role is seeing that the contract is in accordance with Agency policy and law. The contracts are reviewed by AID legal advisors, contract officers, and project officers; and are approved by AID Mission Directors. These reviews and approval, in effect, are meaningless because the persons who make them are never held responsible when the contracts are found to be extremely poor and waste AID funds.

According to USAID/Lesotho, REDSO/EA pressured the host country into signing the supervisory work for Phase III of the project with Harris. The host government was reluctant to use Harris on Phase III because of the poor work Harris had done on the design phase. As noted in AR 3-623-83-12, USAID/Kenya pressured the host government to enter into the contract with IBII without attempting to obtain price competition because of the additional time it would take to get a waiver to include price competition and to get priced bids. In the Kenya situation, AID was more interested in getting the contractor on board and the project moving than it was in assuring that a cost effective contract was let. In the Lesotho situation, the project would have been further delayed until another contract was bid and let. There is considerable pressure in AID to get projects started within planned time frames.

AID lacks a personnel evaluation system that penalizes AID employees for bad judgement and poor contracting. This lack of responsibility management is costing the U.S. government millions of dollars.

Conclusion

Host country contracting continues to be done poorly. The host country contracting mode has taken away management responsibility and incentive. On the three LBII contracts, about \$2 million will be wasted. On the Harris contract we found instances of fraud, waste and abuse amounting to more than \$400,000, but AID has no recourse against the contractor or its employees because these funds were not paid under a Suppliers Certificate. Even when AID funds are paid under the Suppliers Certificate, AID legal counsels appear to be doubtful about AID's ability to recover monies improperly certified.

Technical proposals, which are the keystone to the contracting process, are ineffective. Price competition, which can make host country contracting more cost effective, requires a waiver before it can be used. The waiver requirement has proven in the past to be an effective deterrent to the application of an alternative procedure. Finally, AID personnel in the field have been unable to make host country contracting cost effective. This is partly due to a personnel evaluation system which fails to judge performance in the area of host country contracting.

Previously we were unable to put a price tag on the cost of poor host country contracting. Our two recent audits disclosed that on those four host country contracts, AID wasted almost \$3 million.

You may wish to raise the issues of this report with AID management so that the Agency's vulnerability to waste, fraud and abuse associated with host country contracting can again be addressed.

cc: AA/M 2
AA/PPC 1
AA/AFR 2
LEG 1
GC 2
OPA 1
M/FM 2
M/SER/CM 3
FM/ASD 2
PPC/E 1
S&T/DIU 4