UNITED STATES

AGENCY FOR INTERNATIONAL DEVELOPMENT

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ADDIS ABABA, ETHIOPIA PD-AAF-121-C1

REPORT OF AUDIT

No. 70 - 7

AID Loan No. 663-H-013

Malaria Eradication Project No. 663-61-511-006

For the Period February 29, 1968 to June 30, 1969

AUDIT BRANCH

OFFICE OF THE CONTROLLER

October 24, 1969

USAID/ETHIOPIA

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SCOPE OF EXAMINATION

In accordance with Manual Order 791.1, an initial audit was made of AID Loan No. 663-H-013. We considered, as appropriate, the audit program of Manual Order 794.1 to (a) verify compliance with applicable laws, Agency regulations, and terms of the loan agreement, and (b) identify and report on any procedure or problems which may adversely affect the orderly progress of loan implementation. The audit was performed during May, June and July, 1969.

GENERAL COMMENTS

Background Information

The loan agreement, between the Imperial Ethiopian Government (IEG) and the United States Government acting through the Agency for International Development (AID) which was signed October 23, 1967, provided foreign currency assistance for Fiscal Years 1968 and 1969 for support of the IEG Malaria Eradication Program administered by the Malaria Eradication Service (MES).

AID agreed to lend US$5,800,000 to finance U.S. dollar and local currency costs for goods and services required for the program. The amount to finance eligible local costs was held to the equivalent of US$2,600,000. The balance of $3,200,000 was allocated for the purchase of goods and services of U.S. origin.

The loan is repayable in U.S. dollars within 40 years with interest of one percent per annum for ten years following the first disbursement and two and one-half percent per annum thereafter. The first payment of interest shall be due no later than six months after the first disbursement and the initial payment of principal shall be due nine and one-half years after the date on which the first interest payment is due.

Summary of Major Findings

The requirement that at least 50% of the goods shipped from the U.S. be on U.S. flag vessels was not observed by the borrower. Page 2.

The borrower's quarterly shipping statements, submitted as of March 31, 1969, were not properly prepared. Page 3.

Purchase authorizations (PIO/Cs) did not contain all the insurance provisions or shipping conditions stated in the loan agreement. Pages 2 and 3.

The audit findings and subsequent correspondence with the U.S. Procurement Agent confirmed that loan funds were use[illegible] o pay for ocean transportation costs for shipments carried by foreign flag vessels-- this being contrary to the provisions of the first loan implementation letter. Page 4.

There existed the need to advise the borrower of the AID marking requirements .at operating sites. Page 4.

A review of the vehicle maintenance support provided to other government entities without reimbursement to the MES is required. Pages 5 & 6.

Follow-up on Prior Audits

A Report of Survey was issued on March 21, 1968 for the period May 31, 1966 to February 28, 1968, and mainly covered the activity during the formulation stage and the period during which the borrower and AID were completing the conditions precedent requirements.

FINDINGS AND RECOMMENDATIONS

Loan Shipping Limitation

Paragraph No. 6.03 (b) of the loan agreement requires that the borrower ship at least 50% of the gross tonnage of goods procured in the United States on U.S. flag vessels (or aircraft). In our review of the shipment activity up to the end of the audit period, the June 30, 1969 shipping statement showed that 2413 tons of the 3675 tons shipped from the U.S. had been carried by foreign vessels. Although shipments were arranged by the General Services Administration, acting for the U.S. Public Health Service, the authorized agent, there was no evidence at MES that the 50% requirement was followed or that the condition for waiver stated in the loan was observed.

The procurement authorization (PIO/Cs) did not contain any reference to the 50% requirement stated in the loan agreement or related conditions. Instead the standard AID ocean transportation clauses were used wherein a summary extract of Public Law 664 was stated. The AID clauses were not the same as those of the loan agreement. Since procurement and related shipment actions by GSA are based on those contained in the authorization, it is necessary that the specific loan conditions regulating shipments be stated in the PIO/C's.

Based upon the audit findings action was taken to (1) notify the authorized agent of the loan conditions, (2) acquire a waiver for the past foreign carrier shipments, and (3) issue new shipping instructions based on the loan conditions.

Borrower's Quarterly Shipping Statement

The quarterly shipping statement is used mainly as an instrument to control and show progress by the borrower in complying with the "50% shipment on U.S. Vessels" clause of the loan. The statements for FY 1969, submitted by MES as of March 31, 1969, were not prepared according to the instructions contained in SectionII, B. 1. of Implementation Letter No. 1. The errors and omissions we noted were:

(1) The details of each bill of lading: date, description of cargo, tonnage and costs, were not always shown in part two.

(2) Shipments made by other than water were shown on the statement.

(3) No notations were made on the statement to show actions being taken or contemplated to meet the "50% shipment on U.S. vessels" requirement when a less than 50% situation prevailed.

(4) Statements were not submitted to AID/W through the Mission Program Office.

Regarding No. (3) above, MES did not consider the notation requirement applied because the U.S. agency was booking all shipments from the U.S. We were unable to determine from available records that waivers of the "50% shipment on U.S. vessels" clause of the loan were issued as permitted under paragraph 6.08(b) of the loan agreement.

Prior to the completion of the audit report, the General Manager, MES, submitted revised Quarterly Shipping Statements for FY 1969. The revised statements were reviewed and the MES was advised of the minor discrepancies that required correction. Based on a query to AID/W, the Mission was advised that the borrower was excused from the 50% requirement when the U.S. agent arranging shipment fully justified the non-availability of U.S. vessels.

Loan Insurance Provisions

Loan provisions require insurance coverage on shipments from the U.S. to the point of use within the country of the borrower. Our check of the available insurance policies revealed that this provision was not always followed. Several policies on file showed that coverage was purchased only for the transit time between sea ports. The procurement authorizations (PIO/Cs) required cost/insurance/freight coverage to Addis Ababa and a clause stating that no more than 1% of the commodity cost would be used for insurance costs. Neither the loan agreement nor the implementation letters contained a limitation on the cost of insurance. On the other hand, the procurement authorizations did not contain all the pertinent loan conditions on insurance such as the requirements to purchase from a U.S. company, and to procure consistent to sound commercial practices and insure at full value. Policies were not available for all shipments in the files of MES. This finding left doubt as to whether all shipments were insured.

During the course of the audit, action was taken to request the missing policies and place the loan conditions on insurance coverage in the general conditions annex of the PIO/C's.

Use of Loan Proceeds for Payment of Ocean Transportation Costs on Foreign Carriers

Section IV.A,B, and C, Implementation Letter No. 1, states that to the extent that U.S. flag vessels are used to ship eligible items, ocean freight is payable from the loan proceeds. The summary section on the June 30, 1969 quarterly shipping report indicated that 65.7% of shipments were made on other than U.S. bottoms. While we were unable to verify from the MES records that loan proceeds were utilized, the MES was unable to establish that it had paid the freight costs incurred on shipments on foreign vessels from its own resources. We have concluded, therefore, that loan funds were being used to pay for transportation costs on foreign carriers. Aside from the arrangement whereby the U.S. agent settles all costs for purchases and related services including transportation, the conclusion is also supported by the finding that the costs for foreign bills of lading were included on the General Services Administration export invoices. These invoices, which usually show all charges plus a 7% surcharge, will eventually be used by the U.S. agent to bill AID/W who settles the bills by charging loan funds. We also noted that certain foreign bills of lading contained the statement "send bill to GSA Finance Division, Washington, D. C." Copies of the final U.S. agent billings were not available at MES or the Mission. The quarterly shipping statements issued as of June 30, 1969 showed an amount of U.S.$396,578.00 as freight costs for foreign flag vessels.

If any loan funds were paid to foreign carriers, we believe that this occurred because of a misunderstanding of the loan conditions by MES and the improper use by the USAID Mission of the standard AID ocean transportation provisions. MES considered that the payment of all ocean transportation costs were allowable from loan proceeds, the requirements of the Implementation Letter No. 1 notwithstanding.

Based on our recommendation that the borrower clarify its position on the use of loan funds for foreign shipping costs, the MES took action, prior to issuance of the audit report, to (1) follow the Implementation Letter No. 1 clause which limits the use of loan proceeds for payment of ocean transportation costs, and (2) prepare a request for waiver, as directed by AID/W, to let stand the charges made in the past to the loan for foreign shipping costs.

AID Marking Requirement at Project Sites

The loan provides financing for commodities and local costs of operations of the MES headquarters and field operations. Section 6.11 of the loan agreement states "the borrower shall give publicity to the loan and the project as a program of the United States and . . . mark goods financed under the loan as prescribed in the implementation letters."

Attachment D to Implementation Letter No. 1 issued for this loan only covers the marking requirements for commodities. This requirement was observed by the borrower as commodities and MES vehicles carried the AID clasped hand emblem.

In general, no AID marking or notice of AID assistance was present at the MES headquarters or transportation division area in Addis Ababa. A Mission sign used to show AID participation on construction projects, placed on the prefab warehouse in the transportation area, had fallen to the ground and was not visible. At sector and operating sites in the provinces the AID assistance was generally identified by the application of emblems and signs. Neither the loan agreement nor the implementation letters issued to date specifically covered marking at the project sites.

We believe that the AID financing of local costs for this project type activity warrants the inclusion of marking requirements for operating locations. In this instance we refer to Section 6.12 of the sample loan agreement, Attachment A, M.O. 1262.1.1 and Attachment K of the sample implementation letter, page K-1, Annex A, M.O. 1263.1, which state the requirements for marking project sites when an AID loan finances dollar costs or dollar and local costs. Paragraph 11 b, Sub-section D, Section V, M.O. 1263.1 also cites the requirement for signs at project sites when AID is financing a physical project.

Prior to issuance of this report, the Mission recommended in an airgram to AID/W that the marking requirements for project sites be included in the implementation letter for the first amendment of the loan.

The Chief Malaria Advisor has raised the question with the General Manager of MES of having adequate signs placed at the project sites prior to formal notice of the requirement through the First Amendment to the Loan Agreement and the Implementation Letter thereunder. Favorable action is anticipated in the near future.

MES Transport Division Operations

The Malaria Eradication Transport Division operates a central garage compound in Addis Ababa (Motor Pool) and a fleet of some 450 vehicles. This operation includes a repair and maintenance shop, a spare parts warehouse, a gasoline pump and a mechanics/driver training area. There are 50 employees assigned to the central garage compound in Addis Ababa consisting of 23 mechanics, 9 office workers and 18 warehousemen/store-keepers. These employees are paid by the MES and MES is reimbursed by USAID/Ethiopia under the loan agreement. The spare parts that are used in fixing the MES vehicles are also purchased and paid from AID loan funds.

During our discussions with the Chief Malaria Advisor, he indicated that the MES central garage compound (Motor Pool) in Addis Ababa was also providing some maintenance support to the Ministry of Health (MPH) and UNICEF vehicles, and he estimated that some 20% of the MES transport budget was used for the support of these vehicles. We were informed that the combined fleet of the MPH and UNICEF is approximately 250 vehicles.

We were told by the Chief of the MES Transport Division that the normal procedure for repairing or maintaining an MPH or UNICEF vehicle was for them (MPH/UNICEF) to furnish their own parts but the MES central garage compound would furnish the required facilities and manpower. Although we found no evidence that MES loan financed spare parts were used in repairing MPH or UNICEF vehicles, the chance of this happening is quite high. This is due to the fact that all spare parts are kept in one warehouse location with supposedly separate racks for the various spare parts, although at the time of our visit there was some difficulty in identifying what racks belonged to MES, MPH, and UNICEF. The Chief of the MES Transport Division did state, however, that MPH and UNICEF were not charged for labor or overhead costs for the repair and maintenance of their vehicles, and as mentioned above, the labor costs are reimbursed from loan funds by USAID/Ethiopia.

In order for MES properly to control the labor costs that are used as a basis for reimbursement under the loan funds, we believe that a study should be made to determine the extent of the support that the Transport Division is rendering to MPH and UNICEF, and that this factor (percentage) be applied against payroll vouchers prior to submission to AID for reimbursement. During the course of this audit, a review was initiated by MES to determine the dollar value of the support provided to MPH and UNICEF. In addition, we believe that MES Transport Division should exercise greater control over the storage of USAID loan financed spare parts in order to minimize the possibility of their misuse. This can be accomplished by building a partition in the spare parts warehouse to separate the MES spare parts from those owned by MPH and UNICEF.

<u>Recommendation No. 1</u>

It is recommended that the Chief Malaria Advisor and t Office, a) determine the percentage of MES Transport Divi. garage compound labor costs rendered in support of MPH and . vehicles and apply that percentage to payroll vouchers prioı to submission to AID for reimbursement under the loan, b) arrange for a partition in the spare parts warehouse in order to segregate the MES, MPH and UNICEF spare parts, and c) determine if reimbursement for support of MPH and UNICEF vehicles rendered in the past is deemed necessary.

Expenditures and Repayment Status

As of June 30, 1969, loan disbursements amounted to $2,164,415.41 of which $1,930,987.22 represented expenditures for local costs. The first semi-annual interest installment of $5,514.33, billed to the IEG by AID/W, was paid on February 25, 1969. The first payment of principal is due on August 23, 1978.

Attachment
Distribution of Audit Report - Exhibit "A"

AID Loan No. 663-H-013
Malaria Eradication Project No. 663-51-511-006

Distribution of Audit Report

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J. L. Withers, Acting Deputy Director (1)
R. Cohen, Acting Program Officer (2)
D. E. Goubleman, Controller (10)
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