

PD-AAZ-574

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**Non-Federal Audit
of
U.S. Agency for International Development (A.I.D.)
Grant No. HSH-1335-G-SS-3067-00
to
The People-to-People Health Foundation, Inc.
(Project Hope)
Clement J. Zablocki Center/American Children's
Hospital, Krakow, Poland**

**Audit Report No. 0-000-89-06-N
August 23, 1989**

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

August 23, 1989

MEMORANDUM FOR Director, FVA/ASHA, David A. Santos

FROM: RIG/A/W, John P. Competello



SUBJECT: Non-Federal Audit of A.I.D. Grant HSH-1335-G-SS-3067-00 to the People-to-People Health Foundation, Inc. for the Clement J. Zablocki Center/American Children's Hospital, Krakow, Poland.
(Report No. 0-000-89-06-N dated August 23, 1989)

RIG/A/W is transmitting an audit report prepared by Deloitte Haskins & Sells, Certified Public Accountants, Washington, D.C. The audit report is on the A.I.D. grant made to the People-to-People Health Foundation, Inc. (Project Hope) for the construction of the Clement J. Zablocki Center/American Children's Hospital, Krakow, Poland. The audit covers the period from the inception of the grant through March 31, 1989.

The Department of the Treasury has been working in coordination with A.I.D.'s Office of American Schools and Hospitals Abroad and Project Hope to complete the Zablocki Center. In early 1989, the Department of the Treasury expressed concern about the escalating cost estimates to finish the facility and of the possible need for an independent audit of the project costs. Agreement was subsequently reached among your office, Project Hope, and RIG/A/W that Deloitte Haskins & Sells, the independent public accountant for the People-to-People Foundation, Inc. would perform a financial audit of project costs and review the budget estimates to complete the facility.

The auditors' report consists of the following:

- Statement of Support, Revenue and Expenses
- Independent Auditor's Report on Internal Control Structure
- Independent Auditor's Report on Compliance With Laws and Regulations
- Agreed-Upon Procedures applied to the budget for the estimated zloty costs to be incurred subsequent to December 31, 1988 to complete the construction of the Clement J. Zablocki Outpatient Center

Deloitte Haskins & Sells concluded that (1) the statement of support, revenue and expenses presented fairly, in all material respects, the revenue and expenses from the inception of the grant through March 31, 1989 in conformity with generally accepted accounting principles, (2) there were no material weaknesses in the internal control structure and its operation in those categories relating to the support, revenue and expenses under the grant, and (3) the grantee had complied, in all material respects, with CMB Circular A-110 requirements relating to (i) Standards for Financial Management Systems, (ii) Financial Reporting Requirements, (iii) Property Management Standards, and (iv) Procurement Standards. The auditors did, however, identify several internal control and compliance exceptions which they considered to be insignificant. Also, the auditors believed that the budget estimates to complete the facility should be modified due to the impact of inflation, continuing design work, and exchange rate fluctuation.

We have considered the auditors' report including their findings on internal controls, compliance and the budget and are making the following recommendations which will be entered into the Inspector General's recommendation follow-up system.

Recommendation No. 1

We recommend that the Director, FVA/ASHA ensure that the People-to-People Health Foundation, Inc. correct the internal control weaknesses noted in the auditors report by revising the prime contract to include provision for performance bonding, and access to any books, documents, papers and records of the contractor.

Recommendation No. 2

We recommend that the Director, FVA/ASHA ensure that the People-to-People Health Foundation, Inc. correct the compliance exceptions noted in the auditors report by (1) obtaining documentation to support exceptions to grant requirements, including reporting, and (2) periodically reporting action taken to deposit federal funds, denominated in Polish zloties, in interest bearing checking accounts.

Recommendation No. 3

We recommend that the Director, FVA/ASHA require the People-to-People Health Foundation, Inc. to revise the budget for completing the facility considering the auditors' concerns regarding the impact of inflation, continuing design work, and exchange rate fluctuation.

Please let us know within 30 days of your action taken to implement these recommendations.

Attachment:

Non-federal audit report on People-to-People Health Foundation, Inc. -- Grant No. HSH 1335-G-SS-3067-00

Deloitte Haskins-Sells

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INDEPENDENT AUDITORS' REPORT

The People-to-People Health Foundation, Inc.

We have audited the accompanying statement of support, revenue and expenses of The People-to-People Health Foundation, Inc. (Foundation) relating to the Agency for International Development Grant Number HSH-1335-G-SS-3067-00 (Grant) from the inception of the grant through March 31, 1989. This financial statement is the responsibility of the Foundation's management. Our responsibility is to express an opinion on this financial statement based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statement of support, revenue and expenses is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the statement of support, revenue and expenses. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall statement of support, revenue and expenses presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such statement of support, revenue and expenses presents fairly, in all material respects, the revenue and expenses from the inception of the grant through March 31, 1989 in conformity with generally accepted accounting principles.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental combining schedule of grant support, revenue and expenses from the inception of the grant through March 31, 1989 is presented for purposes of additional analysis and is not a required part of the financial statements. Such supplemental schedule has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects when considered in relation to the basic financial statement taken as a whole.

Yours truly,

Deloitte Haskins & Sells

June 14, 1989

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THE PEOPLE-TO-PEOPLE HEALTH FOUNDATION, INC.

AGENCY FOR INTERNATIONAL DEVELOPMENT GRANT NO. HSH-1335-G-SS-3067-00
STATEMENT OF SUPPORT, REVENUE AND EXPENSES
FROM INCEPTION OF THE GRANT THROUGH MARCH 31, 1989

SUPPORT AND REVENUE - Federal grant funds awarded:	
U.S. Dollars	\$ 6,000,000
Polish Zloties	<u>16,841,082</u>
Total	22,841,082
Unexpended Grant Awards	<u>(3,787,726)</u>
TOTAL SUPPORT AND REVENUE	<u>19,053,356</u>
 EXPENSES:	
Hospital Construction	12,461,814
Medical Equipment and Supplies	4,465,502
Professional Fees	1,226,620
Salaries and Employee Benefits	353,389
Indirect Costs	184,277
Occupancy	232,285
Postage and Shipping	23,444
Travel and Conferences	70,735
Printing and Artwork	11,104
Miscellaneous	<u>24,186</u>
TOTAL EXPENSES	<u>19,053,356</u>
EXCESS OF REVENUE OVER EXPENSES	<u>\$ - 0 -</u>

See accompanying notes.

THE PEOPLE-TO-PEOPLE HEALTH FOUNDATION, INC.

AGENCY FOR INTERNATIONAL DEVELOPMENT GRANT NO. HSH-1335-G-SS-3067-00
NOTES TO THE STATEMENT OF SUPPORT, REVENUE AND EXPENSES
FROM INCEPTION OF THE GRANT THROUGH MARCH 31, 1989

1. GRANT DESCRIPTION

The purpose of the grant is to further cooperative efforts in the field of pediatrics between the United States and Poland through the following programs:

- . Design and construct the Clement J. Zablocki Outpatient Center at the American Children's Hospital in Krakow, Poland. Funding for the program is in Polish zloties.
- . Procurement in the United States of medical equipment, furnishings and related commodities for the Clement J. Zablocki Outpatient Center.
- . Procurement in the United States of medical equipment, furnishings and related commodities to improve the existing facilities of the American Children's Hospital.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting - The accompanying statement of support, revenue and expenses is prepared on the accrual basis of accounting in conformity with generally accepted accounting principles.

Revenue Recognition - Grant revenue is recognized as related expenses are incurred.

Indirect Costs - Indirect costs represent material handling costs and are allocated based upon a percentage of the value of goods shipped through the Foundation's warehouse in Winchester, Virginia. Indirect costs of the Foundation representing program management and general and administrative costs are not charged to the grant.

Exchange Rates - Polish zloty denominated revenue and expenses are translated at the average rate of exchange in effect during the month such revenue and expenses are recorded.

3. UNEXPENDED GRANT FUNDS

Unexpended grant funds at March 31, 1989 were composed of:

Undisbursed grant funds (U.S. dollars)	\$ 1,336,331
Undisbursed grant funds (Polish zloties)	1,968,089
Cash, net of accounts payable (Polish zloties)	684,214
Unreimbursed expenses (U.S. dollars)	<u>(200,908)</u>
Total	<u>\$ 3,787,726</u>

THE PEOPLE-TO-PEOPLE HEALTH FOUNDATION, INC.

AGENCY FOR INTERNATIONAL DEVELOPMENT GRANT NO. HSH-1335-G-SS-3067-00
SUPPLEMENTAL COMBINING SCHEDULE OF SUPPORT, REVENUE AND EXPENSES
FROM INCEPTION OF THE GRANT THROUGH MARCH 31, 1989

	<u>Polish Zloty Award</u>		<u>U.S. Dollar</u>	<u>Total</u>
	<u>Polish</u>	<u>U.S. Dollar</u>	<u>Award</u>	
	<u>Zloties</u>	<u>Equivalentents</u>		
SUPPORT AND REVENUE - Federal grant funds:				
U.S. Dollars			\$6,000,000	\$ 6,000,000
Polish Zloties	<u>Z 5,990,694,000</u>	<u>\$16,841,082</u>		<u>16,841,082</u>
Total	5,990,694,000	16,841,082	6,000,000	22,841,082
Unexpended Grant Awards	<u>(1,604,643,032)</u>	<u>(2,652,303)</u>	<u>(1,135,423)</u>	<u>(3,787,726)</u>
TOTAL SUPPORT AND REVENUE	<u>4,386,050,968</u>	<u>14,188,779</u>	<u>4,864,577</u>	<u>19,053,356</u>
EXPENSES:				
Hospital Construction	3,941,046,039	12,338,973	122,841	12,461,814
Medical Equipment and Supplies	4,908,492	22,535	4,442,967	4,465,502
Professional Fees	305,853,979	1,226,620		1,226,620
Salaries and Benefits	85,727,353	329,155	24,234	353,389
Indirect Costs			184,277	184,277
Occupancy	35,937,247	227,548	4,737	232,285
Postage and Shipping			23,444	23,444
Travel and Conferences	5,096,158	23,715	47,020	70,735
Printing and Artwork			11,104	11,104
Miscellaneous	<u>7,481,700</u>	<u>20,233</u>	<u>3,953</u>	<u>24,186</u>
TOTAL EXPENSES	<u>4,386,050,968</u>	<u>14,188,779</u>	<u>4,864,577</u>	<u>19,053,356</u>
EXCESS OF REVENUE OVER EXPENSES	<u>Z - 0 -</u>	<u>\$ - 0 -</u>	<u>\$ - 0 -</u>	<u>\$ - 0 -</u>

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL STRUCTURE

The People-to-People Health Foundation, Inc.:

We have audited the statement of support, revenue and expenses of The People-to-People Health Foundation, Inc. (The Foundation) relating to the Agency for International Development Grant Number HSH-1335-G-SS-3067-00 (the Grant) from the inception of the grant through March 31, 1989, and have issued our report thereon dated June 14, 1989.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statement of support, revenue and expenses is free of material misstatement.

In planning and performing our audit of the statement of support, revenue and expenses of the Foundation from the inception of the grant through March 31, 1989, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the statement of support, revenue and expenses and not to provide assurance on the internal control structure.

The management of the Foundation is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of 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 the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

- . Revenues and accounts receivable
- . Journal entries and general ledger
- . Cash receipts
- . Cash disbursements
- . Purchases and payables
- . Payrolls
- . Property and equipment

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures, 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 financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving the internal control structure and its operation that we consider to be material weaknesses as defined above.

We also submit the following recommendation concerning certain accounting, administrative and operating matters, which resulted from our observations made in connection with our audit of the statement of support, revenues and expenses from the inception of the grant to March 31, 1989 and is not based on a special study:

Current contracts with the prime contractor do not include provisions for:

- . Performance bonding, or
- . Access to any books, documents, papers and records of the contractor.

We recommend that the contracts be revised to include such provisions.

This report is intended for the information of management, the U.S. Agency for International Development and other Federal agencies. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Deloitte Haskins & Sells

June 14, 1989

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

The People-to-People Health Foundation:

We have audited the statement of support, revenue and expenses of The People-to-People Health Foundation, Inc. (Foundation) relating to the Agency for International Development Grant Number HSH-1335-G-SS-3067-00 (Grant) from the inception of the grant through March 31, 1989 and have issued our report thereon dated June 14, 1989.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statement of support, revenue and expenses is free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to the Foundation is the responsibility of the Foundation's management. As part of obtaining reasonable assurance about whether the statement of support, revenue and expenses is free of material misstatement, we performed tests of the Foundation's compliance with certain provisions of laws, regulations, contracts, and grants. However, our objective was not to provide an opinion on overall compliance with such provisions.

Although the Grant is not subject to the provisions of OMB Circular A-110, we performed tests of the Foundation's compliance with the provisions of the following attachments to OMB Circular A-110 at your request:

- Attachment F - Standards for Financial Management Systems
(including OMB Circular A-122, Cost Principles for
Nonprofit Institutions)
- Attachment G - Financial Reporting Requirements
- Attachment N - Property Management Standards
- Attachment O - Procurement Standards

The results of our tests indicate that, with respect to the items tested, the Foundation complied, in all material respects, with the provisions referred to in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that the Foundation had not complied, in all material respects, with those provisions. However, we noted certain immaterial instances of noncompliance which are described, accompanied by our recommendations and Foundation management's responses, in Exhibit A. Our summarized recommendations, which should be read in conjunction with Exhibit A, are as follows:

- . Documentation - Document exceptions to grant provisions and agreements and any other significant matters which had previously been discussed with and approved by AID/ASHA.
- . Reporting - Obtain, in writing, any necessary approval of exceptions to grant reporting requirements.
- . Bank Accounts - Continue to investigate the possibility of placing federal funds, denominated in Polish zloties, in interest bearing bank accounts.

This report is intended solely for the use of the Foundation, the U.S. Agency for International Development and other Federal agencies. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Deloitte Haskins & Sells

June 14, 1989

FINDINGS

Material Cost Increases

Observation: A letter agreement between the Foundation and the Ministry of Health and Social Welfare of Poland (Ministry), dated March 18, 1986, guarantees that the Ministry will finance increases in construction material costs in excess of 10% annually. Calculations of the project financing which could be requested from the Ministry have not been prepared. Such agreement was not required by the grant.

Based upon discussions with representatives of the Foundation and American Schools and Hospitals Abroad (ASHA), we understand that the Foundation and ASHA had previously discussed the issue and concluded that such agreement between the Foundation and the Ministry would not be enforced and that project financing would not be requested from the Ministry.

Recommendation: Document ASHA's conclusion that such agreement between the Foundation and the Ministry will not be enforced.

Management
Response:

The Foundation, in an attempt to put a ceiling on certain costs, obtained the letter agreement discussed above. After circulating the letter to AID/ASHA and the drafters of the legislation that enabled the Grant, we were instructed that the Clement J. Zablocki Outpatient Center (Center) is to be a gift of the American people and that no financial assistance from the government of Poland was desired for the construction of the Center. Since there was no requirement or request by AID/ASHA to obtain such a letter and since the letter was obtained after the grant was made, we believed that it was not necessary to obtain any written representations from AID/ASHA with respect to this matter.

Exceptions to Grant Provisions

Observation: The following exceptions to grant provisions were noted:

- . An expenditure for approximately \$13,000 relating to construction costs of the Rehabilitation Center was charged to this Grant, but not covered in the Grant provisions. The construction of the Rehabilitation Center was principally funded under a previous AID grant.

- . Approximately \$1.1 million of the U.S. dollar grant funds designated in the grant for equipment and commodities for the Zablocki Center were used to purchase equipment which is now located in the the existing hospital. Equipment and commodities for the existing structure were to be funded by another portion of the Grant.
- . For the Polish zloty portion of the grant, certain materials related to hospital construction and purchased with Grant funds were produced in communist countries, other than Yugoslavia. Procurement of commodities produced in or containing, to the best of the Foundation's knowledge, components from any communist country excluding Yugoslavia, are not authorized under the terms of the Grant.
- . For the Polish zloty portion of the grant, the Foundation receives Grant funding when amendments are executed, which has been generally on an annual basis. This funding process is not consistent with grant provisions, which state that the grantee shall not have available in the bank more monies than required for three months of expenditures.

Based upon discussions with representatives of the Foundation and ASHA, we understand that the Foundation and ASHA had previously discussed these grant exceptions and that they were approved by ASHA.

Recommendation: Obtain, in writing, any necessary approval of exceptions to grant provisions.

Management
Response:

With respect to the above observations, we would like to provide the following additional information:

- . The expenditure for construction costs of the Rehabilitation Center related to incentive payments to construction workers to complete the project. During the construction of the Rehabilitation Center, we experienced difficulty in obtaining an adequate number of construction workers to complete the Project on a timely basis. In planning the construction of the Center, we considered the use of incentive pay to improve the timeliness of the project's completion. ASHA agreed that we would test the effectiveness of incentive pay on the final

construction of the Rehabilitation Center and charge the cost to the Grant. Based on the success of this test, we included incentive pay in our contracts with the Contractor for this Grant.

- . The major item physically located in the existing hospital which was charged against the portion of the grant relating to the Center was a CAT scanner. The CAT scanner is used primarily for outpatients and trauma victims, both of which are groups intended to be benefitted by the Center. The personnel required to operate the CAT scanner are otherwise employed in the Radiology Department. Accordingly, the equipment, although functionally part of the Center's activities, was installed in the Radiology Department of the existing hospital. We believe that this is an appropriate equipment location with respect to any hospital complex.
- . The Grant provided funds in both U.S. and Polish currencies. We were informed by AID/ASHA that the grant provisions relating to the purchase of equipment produced in communist countries were not applicable to the Polish zloty portion of the Grant.
- . We were informed by AID/ASHA that the Grant provisions relating to the disbursement of funds from the Grant were not applicable to the Polish zloty portion of the Grant.

Since these items had been discussed and approved by AID/ASHA, we did not believe that it was necessary to obtain such approval in writing.

Reporting

Observation: The Foundation did not meet federal reporting requirements for the following:

- . Several quarterly reports on Grant expenditures and quarterly reports on capital improvements were not submitted within the 15 day requirement of the grant provisions.
- . Annual institutional reports for the years prior to the year ended September 30, 1988 have not been filed.
- . Quarterly reports on capital improvements did not include commodity procurement information prior to September 30, 1987.

Based upon discussions with representatives of the Foundation and ASHA, we understand that the Foundation and ASHA had previously discussed these Grant exceptions and that they were approved by ASHA.

Recommendation: Obtain, in writing, any necessary approval of exceptions to Grant provisions.

Management

Response: Over the years of this project, we have conducted ongoing discussions with AID/ASHA concerning their reporting requirements. We believe that we have improved our compliance with the technical reporting requirements under the Grant and that the content of our reports complies with the Grant requirements. We have informed AID/ASHA of the logistical problems concerning the timely filing of reports. We understand that although AID/ASHA does not want to change the formal reporting requirements, they agree that timeliness of the reports is not a problem to them.

Non-Interest Bearing Bank Accounts

Observation: The Foundation maintains Federal funds denominated in Polish zloties in a Polish bank in non-interest-bearing bank accounts. We understand that the Foundation was not able to obtain interest bearing accounts. However, as a result of recent changes in Polish currency laws, the banks may offer interest bearing accounts. The Foundation is currently investigating the availability of interest bearing accounts.

Recommendation: Continue investigating the possibility of using interest bearing accounts and, if possible, maintain funds in interest bearing accounts.

Management

Response: We are currently investigating the possibility of using interest bearing checking accounts and will maintain funds in interest bearing accounts, if found to be available.

Deloitte Haskins-Sells

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The People-to-People Health Foundation, Inc.

Dear Sirs:

We have performed the procedures requested by you, as described in Exhibit B, with respect to your budget (Exhibit A), dated January 1989, for the estimated Polish zloty costs to be incurred subsequent to December 31, 1988 to complete the construction of the Clement J. Zablocki Outpatient Center (based upon estimated 1989 zloty price levels) (Budget) as provided for under Agency for International Development Grant Number HSH-1335-G-SS-3067-00 (the Grant). Such Budget excludes those items that are expected to be acquired with the unexpended portion of the U.S. dollar portion of the grant. These procedures, which were specified by you and the Agency for International Development (AID), were performed solely to assist you in evaluating the continued appropriateness of the Budget. It is understood that this report is solely for your information and should not be used by those who did not participate in determining the procedures.

Because the procedures described in Exhibit B do not constitute an examination of prospective financial statements in accordance with standards established by the American Institute of Certified Public Accountants (AICPA), we do not express an opinion on whether the Budget referred to above is presented in conformity with AICPA presentation guidelines or on whether the underlying assumptions provide a reasonable basis for the presentation.

In connection with the procedures referred to in Exhibit B, the matters described at exhibit C came to our attention and caused us to believe that the Budget should be modified. Our summarization of these matters, which should be read in conjunction with Exhibit C, are as follows:

- . Inflation - The high inflation rate in Poland since the Budget was prepared may materially impact the total cost to construct the Clement J. Zablocki Outpatient Center.
- . Continuing Design Work - To accelerate the construction of the Center, certain portions of the Center are being constructed while detail designs for other portions are still being prepared, resulting in more subjective cost estimates for areas under design.

- Exchange rates - With respect to the consideration of using U.S. dollars to complete the construction, the available exchange rate for converting such funds could materially affect the ultimate cost to complete the construction of the Center.

Had we performed additional procedures that might have been requested by AID or other Federal Agencies or had we made an examination of the Budget in accordance with standards established by the American Institute of Certified Public Accountants, other matters might have come to our attention that would have been reported to you. Furthermore, there will usually be differences between the budgeted and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

Deloitte Haskins & Sells

June 14, 1989

THE PEOPLE-TO-PEOPLE HEALTH FOUNDATION, INC.

BUDGET, DATED JANUARY 1989, FOR THE ESTIMATED POLISH ZLOTY COSTS TO BE INCURRED SUBSEQUENT TO DECEMBER 31, 1988 TO COMPLETE THE CONSTRUCTION OF THE CLEMENT J. ZABLOCKI OUTPATIENT CENTER (BASED UPON ESTIMATED 1989 ZLOTY PRICE LEVELS) AS PROVIDED FOR UNDER AGENCY FOR INTERNATIONAL DEVELOPMENT GRANT NO. HSH-1335-G-SS-3067-00

	<u>(000's)</u>
Construction	Z 8,129,534
Furniture and equipment	1,691,191
Architectural and design costs	341,480
Incentives	499,317
Other Costs:	
Construction Manager's	
Office	321,772
Institute expenses	17,458
Miscellaneous	28,862
Contingency Reserve	<u>1,061,479</u>
Total	<u>Z 12,091,093</u>

See Pages A-2 and A-3 for the Summary of Significant Budget Assumptions.

THE PEOPLE-TO-PEOPLE HEALTH FOUNDATION, INC.

AGENCY FOR INTERNATIONAL DEVELOPMENT GRANT NO. HSH-1335-G-SS-3067-00
SUMMARY OF SIGNIFICANT BUDGET ASSUMPTIONS

General

This Budget presents, to the best of the knowledge and belief of the management (Management) of The People-to-People Health Foundation, Inc. (Foundation), the estimated Polish zloty costs to be incurred subsequent to December 31, 1988 to complete the construction of the Clement J. Zablocki Outpatient Center in Krakow, Poland (Project) based upon estimated 1989 zloty price levels. Such Budget excludes those items that are expected to be acquired with the unexpended portion of the U.S. dollar portion of the grant. Accordingly, the Budget reflects management's judgement as of December 31, 1988, the effective date of the Budget, of existing conditions and its expected course of action. The assumptions disclosed herein are those that management believes are significant to the Budget. Management believes that there may be differences between the Budget and actual results because events and circumstances frequently do not occur as expected and those differences may be material.

Methods for Estimating Costs

The initial basis for estimating costs used in the Budget is Annex No. 7 (Annex), dated January 5, 1989, to the construction contract between the Foundation and Exbud-Kielce, the prime construction contractor (Contractor). The Annex includes a listing, which was prepared by the Contractor, of major construction components identified by the architects and the estimated cost to complete (based on estimated 1989 zloty price levels). The listing was reviewed in detail and computations tested by the Office of the Project Construction Manager (COM) and reviewed by Walter Kaplan (Consulting Architect) and Management of the Foundation.

Certain cost estimates are based upon detailed calculations. First, the architects prepared lists of the construction tasks to be completed. For each of the construction tasks, the estimated costs were calculated based upon standard labor hours, material quantities and equipment hours published by the Polish Ministry of Construction and Communal Economy in a Bill of Quantities Catalog, using a labor rate of 850 Zloties per hour and the material and equipment costs in effect during October and November of 1988. The labor rate was agreed upon by the Foundation and the Contractor for all construction in 1989, subject to upward or downward adjustment to the extent that the actual average 1989 labor cost differs from the 850 zloty per hour rate by more than ten percent. These construction tasks have a total estimated cost of 2,851,364,000 zloties.

Other costs included in the Annex were prepared using general cost estimates based upon the combined judgment and experience of the Contractor and the CMD, since the final designs had not been completed for all components of the Project. Certain of these costs were based upon estimated amounts supplied by subcontractors and upon fixed price contracts with subcontractors. Such costs based upon general cost estimates, which were included in the Annex, amounted to 2,492,297,000 zloties. The Annex also included 500,000,000 zloties as provision for estimated increases in material and equipment costs during 1989.

Some components of the design were not sufficiently completed at the time that the Budget was prepared to permit the Contractor to prepare an estimated cost. For such items, the CMD and the Consulting Architect estimated the costs based upon their combined judgement and experience. In several instances, additional general cost estimates costs were included in the Budget that related to items included in the Annex, upon the recommendation of the Consulting Architect.

A breakdown of the source of the estimated costs included in the Budget is as follows:

Construction and equipment costs included
in the Annex:

	<u>(000's)</u>
Based upon detailed cost estimate	Z 2,851,364
Based upon general cost estimate	1,992,297
Provision for estimated increases in material and equipment costs for 1989	<u>500,000</u>
Total	<u>5,343,661</u>

Additional general cost estimates for:

Construction	2,961,723 (a)
Furniture & equipment	1,515,341
Architectural and design costs	341,480
Incentives	499,317 (b)
Other Costs:	
Construction Manager's Office	321,772
Institute expenses	17,458
Miscellaneous	28,862
Contingency Reserve	<u>1,061,479 (c)</u>
Total	<u>Z 12,091,093</u>

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- (a) Includes a provision for estimated material and equipment price increases in 1989 of Z 650,000,000
 - (b) Approximately 5% of the total of construction, furniture and equipment, Construction Manager's Office, and architectural and design costs
 - (c) Approximately 10% of the total of construction, furniture and equipment, architectural and design, and incentive costs.
-

AGREED-UPON PROCEDURES APPLIED

1. Read the Budget for compliance in regard to format with the preparation guidelines established by the American Institute of Certified Public Accountants (AICPA) for presentation of a forecast.
2. Proved the arithmetical accuracy of the Budget summary included as Exhibit A.
3. Randomly selected ten major cost components included in Annex 7 of the contract between the Foundation and the Contractor. Such costs represented approximately 44% of the total Budget. We subsampled such cost components where necessary to obtain specific items or tasks. For each cost component or sub-component selected, we performed the following procedures, based upon the type of cost:

Detailed calculation based upon a bill of materials- computer generated (prepared by the Contractor) (5 selections)

- a. Agreed the number of standard units used in calculating the cost component or sub-component to the bill of materials.
- b. Agreed selected components included in the bills of materials to inclusion in building blueprints.
- c. Agreed the quantity of labor hours, materials, and equipment hours used in the Budget calculation to the standards listed in the respective Bill of Quantities Catalog for the specified task.
- d. Agreed the labor rate used in the calculation (850 zloties per hour) to the contract between The Foundation and Exbud-Kielce.
- e. Obtained a verbal representation from the Chief Engineer of the Project that the material and equipment costs used by the Contractor were reasonable during the months of October and November of 1988
- f. Arithmetically proved the calculation of the cost component or sub-component.
- g. Agreed the current cost of five selected materials included in the CMD's listing of prices to recent invoices.
- h. For one cost component, we footed the sub-components to obtain total estimated labor, material, and equipment costs for the cost component, agreeing such total to the amount included in the Annex.

Detailed calculation based upon a bill of materials - manually computed

(prepared by the Contractor) (3 selections)

- a. Agreed amount per the detailed calculation to the amount included in the Budget, noting that the method of calculation was the same as that described above for the computerized calculations.

Estimates prepared by subcontractors (2 selections)

- a. Agreed the amount included in the Budget to an estimate prepared by the subcontractor.
4. Discussed the basis for the estimated costs of each major cost component included in the Budget with the Construction Project Manager. Based on the representations of the Construction Project Manager regarding the source of the estimated costs, traced each major cost component into its appropriate classification in worksheets prepared by the CMO and the Foundation. Footed such worksheets, agreeing the total of each cost classification to the corresponding amounts included in the breakdown of Budget costs appearing on page A-3 of this report.
5. Discussed the completeness of the major cost components included in the Budget with the consulting architect.

SUMMARY OF FINDINGS

While performing the procedures described in Exhibit B, we noted the following factors that may have a material impact on the estimated costs included in the Budget:

1. Inflation - The inflation rate in Poland has had a significant impact upon the total cost of the Project. Estimates provided by the U.S. Department of Commerce indicate an annual inflation rate of up to 120% for the twelve month period ended March 31, 1989. The Budget was prepared based on estimates (made in January) of price levels for 1989. Such estimates may no longer be appropriate for estimating Budget costs due to inflation experienced since the Budget was prepared. Although it is difficult to determine the precise effect of inflation on the Budget through the date of this report, the ultimate cost to complete the project may already be materially greater than the Budget, expressed in zloties. Future inflation would cause further increases in the completion costs expressed in zloties, the extent of which cannot be estimated at this time.
2. Continuing Design Work - To accelerate the construction of the Center, certain portions of the Center are being constructed while detail designs of other portions of the Center are still being prepared. As a result, the cost estimates used for those areas under design are more subjective than those for which detailed designs have been prepared. We understand that the final designs will not be complete until September 1989. Given the subjectivity of the estimated costs, ultimate costs may materially differ from the Budget. For example, based on the final design of the milk kitchen (completed after the Budget was prepared), the architect's initial estimate to construct the milk kitchen was approximately 450 million zloties more than the 750 million general estimate included in the Budget.
3. Exchange Rates - With respect to the consideration of using U.S. dollars to complete the construction, the available exchange rate for converting such funds could materially affect the ultimate cost to complete the project. In addition to the "official" exchange rate, a "premium" rate was recently implemented. Certain restrictions are placed upon the expenditure of currency exchanged at the "premium" rate. Management of the Foundation has represented to us that additional currency restrictions may be applicable which would limit the numbers of dollars that could be converted at the "premium" rate, if large sums of money were to be converted. As of the date of this report, the "official" rate was approximately 850 zloties per dollar and the "premium" rate was approximately 3,850 zloties per dollar. The ultimate cost to complete the construction, if dollars are used, will depend upon such factors as the rate at which dollars can be converted by the Foundation or, if the Contractor would be paid in dollars, the degree to which the Contractor can use the dollars to pay subcontractors or the rates at which the Contractor expects to be able to convert such funds into zloties.

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