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Audit of the Enterprise in Community Development Project No. 492-0395

Audit Report No. 2-492-91-06
August 29, 1991

USAID/Philippines was not able to measure the extent of project accomplishments, needed to improve its progress reporting and utilization of monitoring information, and should address project sustainability prior to completion of A.I.D. assistance.

UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT
RESIDENT AUDIT OFFICE
MANILA

UNITED STATES POSTAL ADDRESS
USAID/RAO/Manila
APO AP 96440

INTERNATIONAL POSTAL ADDRESS
c/o AMERICAN EMBASSY
MANILA, PHILIPPINES

Date: August 29, 1991

MEMORANDUM

TO: Mr. Malcolm Butler
Director, USAID/Philippines

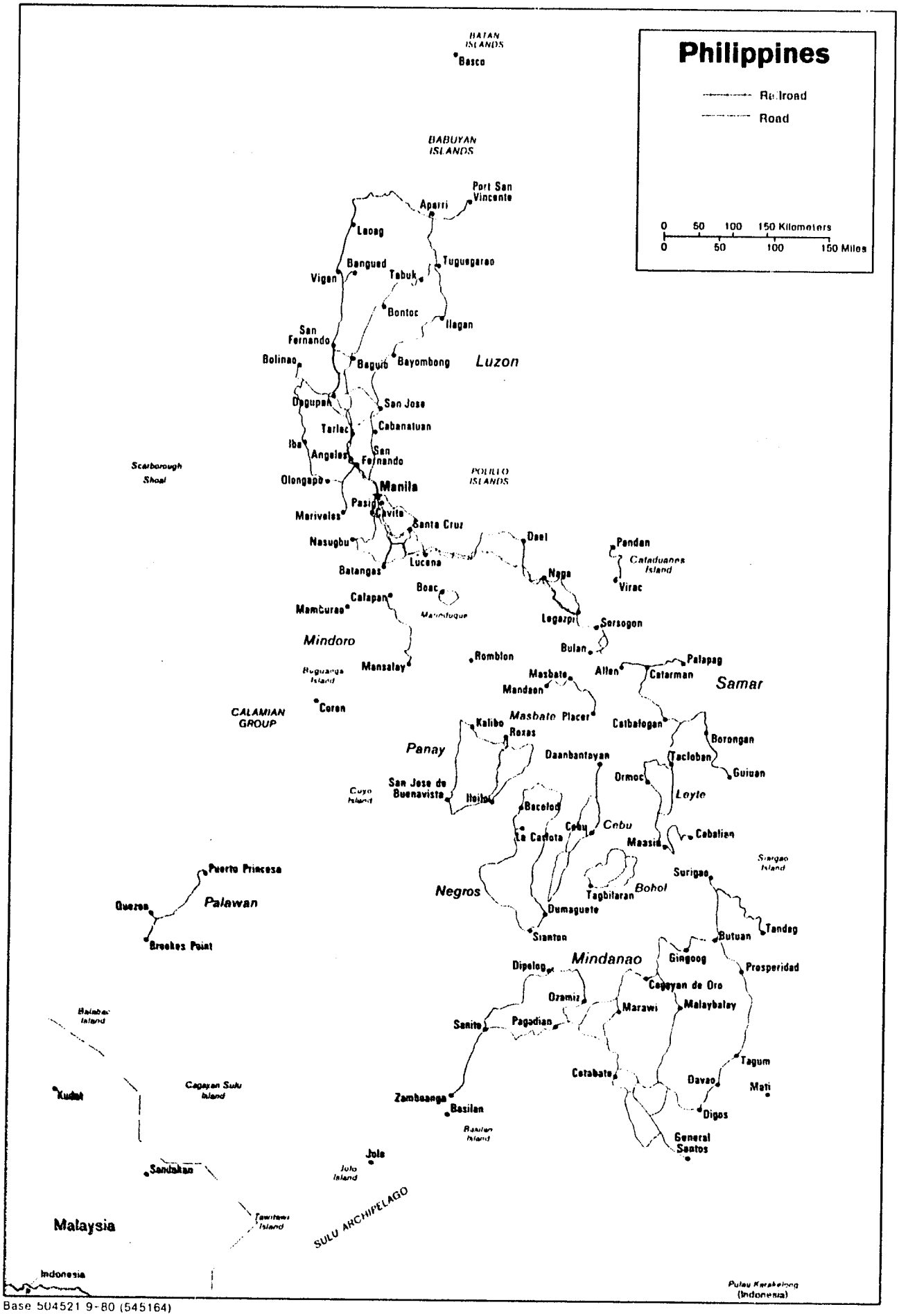
FROM: Dennis L. Smith
Resident Auditor

SUBJECT: Audit of the Enterprise in Community Development
Project No. 492-0395
Audit Report No. 2-492-91-06

The Resident Audit Office/Manila has completed its Audit of the Enterprise in Community Development Project. Comments provided by the Mission on the draft report were considered and included in this report as Appendix II.

There are seven recommendations. Recommendation No. 3 is closed on issuance of this report. Recommendations No. 1, 2, 4, 5 and 7 are resolved and can be closed when actions in process are completed. Recommendation No. 6 will remain open pending the outcome of an ongoing investigation. The report also identifies about $270,000, in overstated and unsupported counterpart contributions and invalid reimbursed costs, including host-country taxes, which were discussed with you during the exit conference. Please advise me within 30 days on the status of actions in process to close the recommendations.

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



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EXECUTIVE SUMMARY

Initiated in September 1986, the Enterprise in Community Development Project has the goal of improving the living conditions in rural areas. The project seeks to achieve this goal through $11 million in A.I.D. grants to the Philippine private sector and through counterpart contributions provided by the private sector equalling the amount of grant funds provided by USAID/Philippines. Its purpose is to assist the development efforts of the private sector in areas outside of Metro Manila by fostering business and civic involvement in participatory community development activities.

The field work for this audit was conducted from February through April 1991 and was performed in accordance with generally accepted government auditing standards. The audit has two audit objectives which are enumerated on page 2 of the report. Likewise, the scope and examination techniques used to answer these objectives are discussed in Appendix I, Scope and Methodology.

Audit work disclosed that, although a system for monitoring progress was established by USAID/Philippines, it was not effective as it could have been because

- the project purpose was not expressed quantitatively and the project's design was not amended to reflect changes made during implementation which resulted in outputs that were not relevant to those outputs visualized in the original project design (pp. 4-6),

- site visit and grantee progress reports were not expressed quantitatively and identified problems were not always addressed (pp. 6-9) and

- sustainability was not addressed prior to completion of A.I.D. assistance (pp. 9-15).

Moreover, USAID/Philippines has established control procedures to ensure that counterpart contributions were provided and that A.I.D. funds were accounted for. These procedures were being utilized with satisfactory results except that deficiencies in the verification process resulted in about $240,000 in unverified contributions and $28,000 in invalid payments (pp. 16-21).

This report contains seven recommendations to correct problem areas. Our assessments of internal controls related to the audit objectives and compliance with applicable provisions of grants, laws and regulations are discussed in the "Report on Internal Controls" and "Report on Compliance" sections of the report, respectively.

USAID/Philippines reviewed the draft report and concurred with its findings and conclusions. Management has initiated actions to implement all recommendations except one which relates to an ongoing investigation by the A.I.D. Inspector General. Management comments shown in Appendix II were considered in preparing the final report.

Office of the Inspector General

Office of the Inspector General
August 29, 1991

INTRODUCTION

Background

The Enterprise in Community Development (ECD) Project began on September 8, 1986, and was scheduled to be completed on August 31, 1992. However, its completion date was subsequently extended to August 31, 1994, to accommodate increasing interest in the ECD project within the business community. The project's goal is to improve the living conditions in rural areas. Its purpose is to assist the development efforts of the Philippine private sector in areas outside of Metro Manila by fostering business and civic involvement in participatory community development activities. End-of-project expectations were 60-90 community development activities jointly undertaken by private firms and communities, with USAID/Philippines assistance; 60 private firms with improved capability to design and manage community organizations; and 50-100 small and developmentally-sound activities sponsored by civic groups and organizations.

The original grant agreement authorized $4.5 million in A.I.D. funds but this amount was increased to $11 million in January 1991. The private sector was to provide cash and in-kind contributions on a "50/50" basis equal to the amount of grant funds provided by USAID/Philippines. As of December 31, 1990, $6.9 million in A.I.D. funds had been committed and $1.3 million had been disbursed. The amount of counterpart contributions provided as of December 31, 1990, totaled about $1 million. USAID/Philippines' Office of Food for Peace and Voluntary Cooperation is responsible for the management of this project while the Government of the Philippines, through the respective Regional Development Councils, is responsible for reviewing and endorsing the community development subproject proposals. Implementation of subprojects is the responsibility of the grantees.

Audit Objectives

The Resident Audit Office/Manila conducted an audit of the ECD Project to answer the following audit objectives:

1. Did USAID/Philippines provide monitoring, reporting and evaluating of project activities in accordance with the grant agreements and A.I.D. policies and procedures?

2. Did USAID/Philippines ensure that participating grantees contributed to the project as agreed and that A.I.D. funds were used and accounted for in accordance with A.I.D. procedures and the grant agreements?

In answering the audit objectives, we tested whether USAID/Philippines followed applicable internal control procedures and complied with applicable provisions of laws, regulations, grants and contracts. Our tests were sufficient to provide reasonable--but not absolute--assurance of detecting abuse or illegal acts that could significantly affect the audit objectives. However, because of limited time and resources, we did not continue testing when we found that, for the items tested, USAID/Philippines followed A.I.D. procedures and complied with grant requirements. Therefore, we limited our conclusions concerning these positive findings to items actually tested. But, when we found problem areas, we performed additional work to

- conclusively determine whether USAID/Philippines was following procedures or complying with grant requirements,

- identify the cause and effect of the problems and

- correct the conditions and causes of the problems by making recommendations.

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

REPORT OF AUDIT FINDINGS

Did USAID/Philippines provide monitoring, reporting and evaluating of project activities in accordance with the grant agreements and A.I.D. policies and procedures?

USAID/Philippines established a monitoring, reporting and evaluating system to ensure that subproject activities were being implemented in accordance with the grant agreements and A.I.D. policies and procedures. This system, however, was not as effective as it could have been.

For the items tested, the system used by USAID/Philippines to monitor and report on grantee activities was sufficient to satisfy A.I.D. monitoring requirements. These procedures included submission of progress reports by the grantees, site inspections conducted by Mission personnel and frequent consultations with the grantees. Progress reports were being collected on a regular basis from grantees responsible for implementing subprojects. These reports contained statistical information and other details needed to describe ongoing project activities. Field trips were conducted by Mission personnel, at least annually, and were documented. Project records indicated that A.I.D. management was apprised of project activities as they occurred. The mid-term evaluation, scheduled for 1991, had not been performed at the time of our audit.

Although a system for monitoring and reporting on project progress was established by USAID/Philippines, it was not as effective as it could have been because the project purpose was not expressed quantitatively and changes made during project implementation resulted in outputs that were not relevant to those outputs visualized in the original project design. The Mission had not amended the project design to reflect these changes. Our audit also showed that data collected from progress and trip reports were not being utilized productively by the Mission. These reports were generally void of quantitative techniques

essential for assessing project accomplishments--such as measurements for comparing accomplishments with projected milestones. Even when implementation problems were identified by the reports, USAID/Philippines did not always take actions to remedy the identified problems. Finally, tests at six subproject locations showed that sustainability needs to be addressed prior to completion of A.I.D. assistance.

Indicators of Progress Need Revision

A.I.D. procedures specify that project design should permit and facilitate the measurement of progress toward planned targets. Although a system for measuring project accomplishments was established by USAID/Philippines, it was not as effective as it could have been because the project purpose was not expressed quantitatively and major changes in project design altered outputs to the point where project accomplishments could not be measured. Because the progress indicators were not revised, USAID/Philippines could not measure the extent to which project objectives were being achieved.

> **Recommendation No. 1: We recommend that USAID/Philippines amend the project design to include new quantitative indicators of progress, a quantitative project purpose, and a new logical framework.**

A.I.D. Handbook 3, Chapter 3 defines project objectives as the highest order of design tasks and states that their subsequent pursuit should be the central focus about which all other project aspects are molded. It also provides that project design should contain a precise definition of project objectives and permit and facilitate the measurement of progress toward achieving the objectives. When project outputs are not modified to reflect major design changes that occur during project implementation, it becomes virtually impossible to measure project accomplishments.

Our audit work showed that the initial project design contained a well-defined project description, including quantitative indicators for planned outputs. The project purpose, however, was not quantified and did little to facilitate the measurement of progress toward achieving project objectives. To illustrate, the

project purpose was to assist the development efforts of the Philippine private sector in areas outside of Metro Manila by fostering business and civic involvement in participatory community development activities. Such vagueness does not realistically identify what results are expected from the project. Although the indicators expressed in the project design are quantitative, they are no longer relevant to results now being achieved from project activities. For example, under the community development component, the project was to fund 60 to 90 community development subprojects, including public works, small-scale infrastructure or income generating activities over a five-year period. Average grant size was to range from $35,000 to $50,000. In reality, the project funded only 12 grants having an average size of over $520,000. Another important part of the project called for USAID/Philippines to co-finance up to 75 percent of the total cost of activities which promote social and economic growth and development of the poor in areas outside of Metro Manila. Project design called for the creation of 50 to 100 small, worthwhile, developmentally-sound activities costing less than $5,000. Through the time of our audit, only five of these subproject activities had started.

Because of the changes made during project implementation, outputs no longer appear to be relevant to those outputs visualized in the original project design. One Mission official remarked that the size of the community development activities was much larger than planned because no grantees were interested in co-financing small subprojects costing less than $50,000. He added, however, that the $50,000 level was never intended to be the maximum grant ceiling available. Because this project broke new ground for the Mission, funding was supposed to be somewhat flexible. Another official believed that the quantitative indicators identified in all subproject grant agreements were sufficient to measure project accomplishments; therefore, formal amendment of the project design was not needed. We do not agree because subproject indicators involve localized situations and generally deal with performance indicators such as the number of wells to be dug or how many hectares of crops should be planted. These indicators are extremely limited because they do not address the overall objectives of the project.

USAID/Philippines can not measure or evaluate project accomplishments because the indicators of progress established during project design are no longer valid for the existing project. As a result, the developmental benefits derived from the

$11 million A.I.D. grant can not be measured. The ability to measure project accomplishments is essential to properly monitor project progress and evaluate the extent that the project has attained its intended purpose. This point is clearly illustrated by A.I.D. Handbook 3, Chapter 14 which emphasizes that a project can only be considered complete when it is successfully generating a stream of benefits and helping the intended beneficiaries in the manner and at the rate envisioned in the initial project or, if modified, final project design.

Mission Comments and Our Evaluation

Mission officials agreed with the audit finding and recommendation. They plan to amend the project design to include new quantitative indicators of progress, a quantitative project purpose, and a revised logical framework. Actions planned by USAID/Philippines are responsive to the recommendation; therefore, Recommendation No. 1 is resolved on issuance of this report and can be closed when the planned actions have been completed.

Improvements Needed in Reporting and Use of Reported Information

A.I.D. Handbook 3, Chapter 11 requires the comparison of quantitative data with planned targets to identify and address potential implementation problems. Even though the system established by USAID/Philippines to monitor grantee activities was able to fulfill most reporting requirements, it was not as effective as it could have been. Quarterly progress reports and site visit reports did not equate accomplishments with planned outputs, and some problems identified through these reports were left unaddressed by the Mission. Reports did not assess planned accomplishments because the grantees' quarterly progress reports were not quantitative, and identified problems were not always addressed because no formal system for follow-up had been established. As a result, some community development activities were less effective than planned.

Recommendation No. 2: We recommend that USAID/Philippines improve its monitoring by requiring grantees to submit quarterly progress reports and Mission personnel to prepare site visit

reports, which identify quantitative data critical to project success and compare the quantitative data to plans and schedules for the purpose of alerting management to potential problems.

<u>Recommendation No. 3:</u> We recommend that USAID/Philippines establish a procedure for confirming that problem areas identified in monitoring reports are acted on and that appropriate follow-up actions are taken.

A.I.D. Handbook 3, Chapter 11 describes monitoring as the timely gathering of information regarding inputs, outputs and actions that are critical to project success and the comparison of such information with plans and schedules for the purpose of alerting management about potential implementation problems. A.I.D. Handbook 13, Chapter 1 also sets forth procedures for monitoring and reporting on the performance of grantees. Both criteria stress the need for quantitative reporting requirements and the use of such data to assist in the resolution of management problems, whenever possible.

The progress reports submitted by grantees are not very useful as management tools. None of the six reports reviewed compared actual accomplishments against planned targets and only three of the six reports were quantitative; therefore, they did not show the status of progress toward the achievement of subproject objectives. These reports were vague and did not appear to have a clear purpose. To illustrate, one quarterly report of a grantee, dealing with water drilling and community development activities, just identified the locations of deep wells constructed and rehabilitated without quantifying and comparing them against the overall targets set in the grant. Furthermore, its narrative portion discussed only the importance of constructing deep wells rather than assessing its current percentage of completion. In another report, a grantee quantified day care centers, health centers, and water pumps constructed but did not compare such activities to planned milestones and accomplishments in order to measure project progress.

Both Mission and grantee officials agreed that the preparation of these progress reports, as structured, provide insufficient information and need to be improved. Mission officials contend that, in order to augment progress data, other sources of information are used as management tools--such as meetings, telephone calls

or special reports. In any event, these progress reports are not meaningful monitoring tools.

Site visits are conducted annually by mission personnel; the average number of days per visit is three. Such trips are documented with problems addressed and recommendations made. However, follow-up actions were not always taken to remedy the problems. For example, a site visit to a subproject was performed in July 1989. A report was prepared which contained a recommendation to improve grantee interdepartmental communications. At the time of the audit, the same communications problem which prompted the 1989 recommendation still existed. During this period no corrective actions had been initiated by the Mission because there were no procedures established to confirm that problem areas identified were acted on and that appropriate follow-up actions were taken. In fact, the grantee said that the lack of coordination between its departments caused project activities to be delayed by about 50 percent. Had there been follow-up actions to correct this problem, the project probably would not have been so far behind schedule.

Mission officials conducted three site visits to another subproject. As a result of the first visit in July 1989, a potability problem was identified in the two deep wells constructed. The site visit report contained no recommendation on how this should be resolved. In January 1990, another site visit report identified the same problem--the number of wells affected had increased to eight--and no specific course of action was recommended in the report. Likewise, the last inspection conducted in November of the same year reported nine deep wells having potability problems and concluded that future projects dealing with this type of activity require adequate technical studies before construction begins or that fault-free services be obtained from third party subcontractors. However, the report did not address corrective actions necessary to remedy the potability problem. As a result, this problem is present in 17 of the 20 deep wells constructed by the project at a cost of about $27,000. The audit disclosed that very little effort was made by the Mission to address the problem when it was first identified. In fact, had attention been focused on corrective measures at the earliest stage, the recurrence of the same problem may have been avoided or at least minimized.

Lack of effective follow-up on identified problems occurred because no systems or procedures existed for evaluating site visit reports to confirm that problem areas were addressed and that effective actions were taken to resolve the problems. Moreover, nine of the 12 site visit reports reviewed did not equate accomplishments with planned outputs. Only activities being performed and completed were cited in the reports without comparing the activities to expected targets. Since the objective of the site visits is to assess the subproject progress, comparing planned and actual progress should be an essential element of any site visit report.

USAID/Philippines established a monitoring system sufficient to satisfy A.I.D. reporting requirements. This system, however, was not as effective as it could have been because data collected from monitoring and field trip reports were of limited value in assessing progress and were not being utilized by project management to resolve identified problems. If this arrangement continues, A.I.D. can not be assured that project objectives are being met, that identified problems are being addressed and that the project's overall impact is being properly gauged.

Mission Comments and Our Evaluation

USAID/Philippines concurred with the audit findings and recommendations. Mission officials agreed to improve site visit reporting and to revise the format of the quarterly progress report and to conduct training on the use of the revised report format. The actions of the Mission are responsive to Recommendation No. 2, which is resolved on issuance of this report and can be closed when the actions in process have been completed. For Recommendation No. 3, USAID/Philippines has established a tracking system for evaluating site visit reports to ensure that problem areas are recognized and appropriate follow-up actions are taken. This action is responsive to Recommendation No. 3, which is closed on issuance of this report.

Sustainability Needs to be Addressed

A.I.D. Handbook 3, Chapter 14 states that before completion of A.I.D. assistance, the grantees' continuing responsibilities must be considered, including recurrent costs and the adequacy of funding for the continued operation of project

activities. Although much progress has been made in completing grantee activities, USAID/Philippines has not been planning for the sustainability of successful projects and has not monitored grantee activities in this regard. Because grantees have not prepared plans or provided additional funding to ensure that project efforts will be continued, these efforts are in jeopardy of not being supported after A.I.D. funding ceases. Unless these issues are addressed, thousands of dollars in project funds may have been spent on successful activities that will not be continued.

> **Recommendation No. 4: We recommend that USAID/Philippines in coordination with the grantees develop, prior to project completion, a plan for phasing out A.I.D. support for project activities which includes a financial commitment from the grantees to support priority activities.**

The position that grantees must assume continuing responsibilities after project completion is affirmed by agency policy and legislation. Section 101 (a) (2) of the Foreign Assistance Act states that foreign assistance funding is provided to promote conditions which enable developing countries to achieve self-sustaining growth. This goal was also included in the A.I.D. Policy Paper on Food and Agricultural Development which states that the overall objective of United States bilateral economic assistance is to stimulate self-sustaining economic growth. Likewise, A.I.D.'s Policy on Recurrent Costs states that the ultimate objective of A.I.D. assistance is for each project to move from dependence on Mission funding to permanent financial independence. Accordingly, projects should include plans for ensuring that this objective is achieved. Finally, A.I.D. Handbook 3, Chapter 14 states that, prior to the completion of A.I.D. assistance, the grantees continuing responsibilities must be considered, including the provision of recurrent costs and the adequacy of funding for the continued operation of the project.

Our audit tests at six of the 12 subproject locations confirmed the need for assurance by the grantees of a continuing responsibility after A.I.D. assistance ends. We identified several activities that would require continued maintenance, beneficiary participation and additional funding. To illustrate:

- At one location, grantee officials said that recent water potability testing conducted by the Department of Health disclosed that water from 17 of 20 artesian wells was not potable. The total cost of constructing the 17 deep wells amounted to about $27,000. Our site inspection of seven constructed wells and interviews with beneficiaries confirmed water potability problems in three of the wells. In addition, our review of income generating activities disclosed that only one of three initiated activities proved successful. A.I.D. assistance ended in February 1991 and all activities had been completed prior to our audit. A phase out plan was submitted to A.I.D. as required by the grant agreement; however, this plan contained only requests to retain custody and administration of A.I.D. funds to sustain the income generating activities and to use program income to continue other subproject activities. The Mission did not require the grantee to solve the potability problems of the wells nor assess whether any of the income generating activity should be continued. Grantee officials expressed their willingness to remedy the potability problems, but they were unable to provide any plan or financial commitment to ensure that these problems would be addressed after A.I.D. funding ceases.

Artesian Well Constructed in Kinamagan,
Santo Thomas, Davao del Norte - Water Not Potable

- Another grant activity was the construction of a reservoir, costing about $3,600, to provide safe and convenient water delivery to two communities. The reservoir was poorly constructed, leaked and was only able to provide water at a greatly reduced capacity. A grantee official said that lack of coordination between its project office and engineering department resulted in the defective design of the reservoir. This problem was disclosed by site visit reports but no follow-up action was taken to remedy the problem. At the time of our audit, the reservoir had not been used for several months. A.I.D. assistance is scheduled to end in June 1991, but the grantee plans to request a one-year extension. We were told by a grantee official that, eventually, the grantee would repair the reservoir. However, funding for repairs and maintenance has not yet been addressed by either A.I.D. or the grantee. As a result, the sustainability of this activity is in doubt.

Poorly Constructed Water Reservoir
in Alae, Bukidnon

- Another activity was the reforestation of 494 acres of land. This effort was considered complete 15 months ahead of its planned schedule. Despite the early completion, a phase out plan had not been developed because USAID/Philippines has not been monitoring the sustainability of successful project activities. An interview with grantee officials revealed no commitment to maintaining this activity although they said that it was worth pursuing. We also learned that some private individuals claimed ownership of the reforested site which hinders the issuance of certificates of stewardship to beneficiary farmers. Considering that reforestation is a long-term effort and will require plant maintenance and care, the absence of proprietary rights to the reforested site by the farmers poses additional sustainability problems.

Reforested Area in Borbon, Cebu
Without Stewardship Certificates Issued

- A similar problem was identified at another reforestation site. This activity was about 94 percent complete, but only about half of the beneficiary farmers had been issued certificates of stewardship. This

occurred because the Philippine Department of Environment and Natural Resources declared the reforestation site a critical watershed area and prohibited the issuance of the remaining certificates. A site inspection report by Mission personnel identified this problem, but actions taken by the grantee to ensure that certificates were issued was not monitored by USAID/Philippines. Interviews with grantee officials confirmed that an alternative claim to the land had been initiated on behalf of the farmers, but at the time of the audit the issuance of additional certificates remained uncertain. When questioned about sustainability, grantee officials commented that they intend to continue subproject activities, but they had not developed any formal phase-out plan or made any budgetary commitment to sustain the subproject.

- The availability of funds after A.I.D. assistance ends is questionable in another subproject where the grant is being implemented through a foundation. This subproject was designed to establish diversified income producing activities. Although it is progressing favorably, the subproject's success is attributable to the foundation's effective administrative and monitoring staffs--76 percent of whom are paid with A.I.D. funds. The audit also showed that the subproject's income generating activities were 100 percent A.I.D. funded since counterpart contributions by the grantee were for labor, tools and implements donated by the beneficiary farmers. USAID/Philippines' monitoring had not highlighted the economic factors that contributed to the success of these activities. Although foundation officials expressed interest in continuing activities after A.I.D. assistance ends, continuation of these activities is contingent upon finding other donors.

USAID officials agreed that developing a strategy is necessary if the grantee is to sustain subproject activities after A.I.D. participation ceases. Although the project design addressed the sustainability aspects of its activities, the grants only required grantees to submit a report describing their continuing responsibilities and activities within 90 days after the grant expired. At the time of our audit, only one of the subprojects had fallen within this 90-day period.

A sustainability plan developed within 90 days after project completion does not ensure that project activities will continue. Secondly, it is not logical to wait

until all activities have been concluded before developing a plan for continuation of subproject activities when it was obvious from the beginning that many activities would require continued support. Waiting until the end of a subproject to plan for its sustainability does not promote conditions which enable beneficiaries to achieve self-sustaining growth nor does it ensure the adequacy of funding for the continued operation of project activities.

In conclusion, considerable progress was made to benefit rural recipients, but these achievements may be short-lived. Despite the fact that grantees have expressed their desire to continue participation, no plans or budgets for these activities have been developed or approved. To ensure continuation of successful subproject activities, USAID/Philippines should initiate the planning for A.I.D. phase-out, which identifies continuing responsibilities and cost considerations necessary to ensure project sustainability, before the subprojects are completed.

Mission Comments and Our Evaluation

Mission officials believe that most of the grants had addressed the sustainability issue in the implementation section of the grant agreements. However, USAID/Philippines is developing guidelines to formalize the requirement that sustainability be addressed prior to project completion. Mission actions are responsive to the recommendation; therefore, Recommendation No. 4 is resolved on issuance of the report. It can be closed when the actions in process are completed.

Did USAID/Philippines ensure that participating grantees contributed to the project as agreed and that A.I.D. funds were used and accounted for in accordance with A.I.D. procedures and the grant agreements?

USAID/Philippines has established control procedures to ensure that counterpart contributions were provided by the grantees as agreed and that A.I.D. funds were used and accounted for in accordance with the grant provisions and A.I.D. procedures. However, USAID/Philippines could improve its process for verifying counterpart contributions and validating grantee expenditures.

For the items tested, USAID/Philippines has established control procedures to ensure sound financial management. A financial manual has been developed by the Mission which contains control measures for both counterpart contributions and A.I.D. funds. Each grantee was provided with a copy and was trained to use it as a guide in its operations. Because the project stressed counterpart contributions, criteria for allowable counterpart contributions were incorporated in the individual grant agreements. USAID/Philippines also required submission of quarterly disbursement reports showing the details of counterpart contributions. We examined counterpart contributions amounting to $326,110, representing about 30 percent of the total contributions as of December 31, 1990. Procedures governing the use of A.I.D. funds were likewise included in the grant agreements. For A.I.D. disbursements, we reviewed $326,365, which is 25 percent of the total expenditures as of December 31, 1990.

Although an internal control system exists, verification procedures need to be implemented annually as prescribed in agency guidance. Tests to ensure compliance with prescribed control procedures were not always conducted by the Mission. Because verification wasn't performed, about 23 percent of counterpart contributions reviewed were overstated while 51 percent were not authenticated and about nine percent of sampled payments made by USAID/Philippines for goods and services could not be validated.

Need For Improved Verification

A.I.D. guidance requires that annual payment verification be performed to test whether control measures are effective. Likewise, the provisions of the grant

agreements enumerate the criteria for allowable counterpart contributions and reimbursable costs. Our audit demonstrated that counterpart contributions amounting to about $240,000 were overstated and not documented properly and payments for goods and services costing about $28,000 could not be validated. Verification of counterpart contributions has not been performed by USAID/Philippines and payment verification is not conducted until the grant closeout process. Only one of the grants has been completed. Verification procedures need to be improved to better ensure that A.I.D. resources are utilized effectively.

> **Recommendation No. 5: We recommend that USAID/Philippines establish procedures to conduct routine tests of grantee financial records to determine whether internal control measures are ensuring that counterpart contributions are verifiable and that cost reimbursements are for valid expenditures.**
>
> **Recommendation No. 6: We recommend that USAID/Philippines, based on the results of an investigation conducted by the A.I.D. Inspector General's Office of Investigations, recover any misused funds from the grantees.**
>
> **Recommendation No. 7: We recommend that USAID/Philippines obtain a refund of $1,100 representing tax payments reimbursed to a grantee.**

A.I.D. Handbook 19, Chapter 1, Appendix 1D requires that payment verification tests be performed annually to determine whether control measures are implemented effectively and funds are accounted for. Likewise, Handbook 13, Chapter 1 and the individual grant agreements provide that all contributions shall be accepted as part of the grantee's cost sharing when such contributions are verifiable from the grantee's records; are not included as contributions for any other program assisted by the U.S. Government; are necessary and reasonable for the accomplishment of project objectives; are the types of charges that would be allowable under U.S. Government cost principles; are not financed by the U.S. Government under any other grant or agreement, unless approved by USAID/Philippines; and are provided for in the budget. In addition, the Standard Provisions of the grant agreements provide that charges to the grants shall be

sufficiently documented and that periodic examination should be conducted to determine whether financial controls have been implemented.

During our review of the financial records of six grantees, we identified approximately $74,000 in overstated counterpart contributions and about $168,000 in contributions that were not documented adequately. These examples represent about 74 percent of all counterpart contributions reviewed.

- An in-kind contribution of about $69,000 was claimed for a dump truck and land intended to be used in a plant nursery. At the time of our audit, the land was not being used by the project because an alternative site had been selected. Also, a grantee official informed us that the truck was no longer being used by the project. We believe that including unused contributed property overstates the value of counterpart resources.

- Another grantee contributed a pick-up van having a rental cost of $11,300 and claimed $5,000 for repairs and maintenance of the van. The purchase cost for the same vehicle is about $8,900. Rental agreements in the Philippines provide that the vehicle owner absorbs the costs of repairs and maintenance. Valuing a vehicle at more than its cost and inclusion of repair costs as counterpart contributions overstates the value of counterpart resources.

- About 38 percent of another grantee's counterpart share, or approximately $88,000, lacked valid documentation. This contribution consisted of labor donated by the beneficiaries, costed at the sum of their daily rates, and the value of implements, tools, and working animals used. No time records, invoices or receipts to support these costs were available. Interviews with the beneficiaries regarding the donations revealed that they were asked only to sign summary forms by the grantee indicating their participation in the subproject.

- Another grantee claimed it provided $60,000 for fertilizer. However, we were unable to verify that the fertilizer was provided or its cost because there was no documentation--such as invoices or receipts--to support its purchase.

- Other items, including two land cruisers costing about $20,000 and an unutilized dump truck were contributed to the project. Although the vehicles were provided, their value may be overstated because there was no documentation to support the costs nor was there an assessment made by an independent appraiser to establish their value as required by agency guidance. According to the ECD Financial Management Manual, donated property with values not supported by documentation are considered to be unallowable counterpart contributions.

Our tests of the six grants also showed that verification of reimbursements made to the grantees needs to be improved. Although the examples illustrated here are for relatively small dollar amounts, the obvious manner in which the funding was manipulated highlights the need for improved control procedures.

- At one grantee location, payment records were overstated by about $19,000. Disbursement records showed a $29,000 payment for seedling production costs at $.05 per seedling. Discussions with payee farmers revealed that they were paid only $.03 per seedling, or a total of $16,000--a difference of $13,000. The same grantee, in support of wages paid to farmers, had payroll sheets showing that farmers were paid a daily wage of $2.29 for site preparation and seed planting. Our discussions with farmers indicated they were paid a daily wage of only $1.82. This amounts to an overstatement of about $6,000. Currently, a case is being filed in court by the grantee against the employees involved in these incidents, and the A.I.D. Inspector General's Office of Investigations (IG/I) is investigating the case. As a result, $5,000 was recovered and the grantee proposed to settle the balance in question by contributing an additional $11,000 to the subproject, equivalent to about 80 percent of the $14,000 balance. The Mission is evaluating the grantee's proposal.

- At another grantee location, a supplier received a payment of $7,000 for 20 pump cylinder assembly units at $348 per unit, equivalent to 50 percent of the original price quotation of $696 per unit. A 50 percent discount was agreed to by the supplier and the grantee. We compared this price with a quote given by a Manila-based supplier which showed

a unit cost of $167. It appears that there still might be overpricing of about $3,600 by the supplier. IG/I is investigating this matter.

- A drilling contract in the amount of $4,200 was awarded even though the three competing quotations used in the bid process appeared to be suspicious. All had apparently been prepared from the same typewriter. Interviews with grantee personnel disclosed that these quotations were made up in order to comply with A.I.D. requirements. No competitive bidding was conducted. Likewise, IG/I is investigating.

- A grantee purchased seven units of motorcycles costing about $12,000. Of this amount about $1,100 were paid for value-added taxes. Taxes are not reimbursable costs under the terms of the grant agreement.

Payment verification procedures were to be performed only during the grant closeout process. Since routine verification was not regularly performed, misuse of A.I.D. resources went undetected--depriving the beneficiaries of the maximum realizable benefits. Also, the Mission is not assured that the grantees contributed the required counterpart resources.

Mission Comments and Our Evaluation

USAID/Philippines agreed with the findings and recommendations. The Mission will amend its contract with a local management consulting firm to include regular payment verification procedural tests of grantees' counterpart funds and A.I.D. funds to determine that all relevant internal control measures are complied with. This planned action is responsive to Recommendation No. 5, which is resolved on issuance of the report. It can be closed when the contract is amended. The Mission has requested two grantees to refund amounts representing tax payments and misused funds in response to Recommendations No. 6 & 7. However, Recommendation No. 6 must remain open pending the outcome of the IG/I investigation. Actions to recover the amounts identified by the investigation will resolve the recommendation. Recommendation No. 7 is

resolved and can be closed when the grantee has refunded the identified taxes or when this amount has been deducted from a grantee payment request.

REPORT ON INTERNAL CONTROLS

This section provides a summary of our assessment of internal controls for the audit objectives.

Scope of Our Internal Control Assessment

We conducted our audit in accordance with generally accepted government auditing standards which require that we assess the applicable internal controls when necessary to satisfy the audit objectives and report on the controls assessed, the scope of our work, and any significant weaknesses found during the audit.

In planning and performing our audit, we limited our assessment of internal controls to those applicable to the audit objectives and not to provide assurance on USAID/Philippines' overall internal control structure.

For the purposes of this report, we have classified significant internal control policies and procedures applicable to each of the audit objectives. We obtained an understanding of the design of relevant policies and procedures to determined whether they have been placed in operation--and we assessed control risk. We have reported weaknesses under the applicable section for each audit objective.

General Background on Internal Controls

The management of A.I.D., including USAID/Philippines, is responsible for establishing and maintaining adequate internal controls. Recognizing the need to re-emphasize the importance of internal controls in the Federal Government,

Congress enacted the Federal Manager's Financial Integrity Act in September 1982. Also, the General Accounting Office has issued "Standards for Internal Controls in the Federal Government" to be used by agencies in establishing and maintaining such controls.

The objectives of internal controls and procedures for federal foreign assistance programs are to provide management with reasonable--but not absolute--assurance that resource use is consistent with laws, regulations, and policies; resources are safeguarded against waste, loss, and misuse; and reliable data is obtained, maintained, and fairly disclosed in reports. Because of inherent limitations in any internal control structure, errors or irregularities may occur and not be detected. Moreover, predicting whether a system will work in the future is risky because (1) changes in conditions may require additional procedures or (2) the effectiveness of the design and operation of policies and procedures may deteriorate.

Conclusions for Audit Objectives

Audit Objective One

The first objective was to determine whether a system for monitoring, reporting and evaluating project activities had been established. We reviewed the project design and tested controls related to project monitoring and reporting. Project evaluation had been provided for but the mid-term evaluation had not yet been initiated. The monitoring and reporting system in place included submission of progress reports by the grantees, site inspections conducted by project staffs and consultations with the grantees. Controls assessed included the adequacy of documentation, provision of supervision and assignment of responsibility for resources. We performed site visits to confirm the status of the project as indicated in progress reports and checked whether problems identified in the reports were addressed and resolved. We reviewed site inspection reports to determine whether implementation problems were addressed and resolved. Progress reports were analyzed to determine whether quantifiable indicators were used to measure accomplishments against planned outputs. Our tests showed that controls were logically designed and consistently applied except that the project purpose was not expressed quantitatively, project design was not always modified

to reflect changes made during implementation, data collected from the monitoring reports was not quantitative and was not being utilized productively by management. Although we found that progress had been made in achieving the project objectives, this progress may not continue after A.I.D. funding ends because a phase-out strategy had not been developed to ensure sustainability of project activities.

Audit Objective Two

Objective two assessed whether USAID/Philippines ensured that participating grantees contributed to the project as agreed and that funds were used and accounted for in accordance with A.I.D. procedures and the grant agreement. We reviewed internal controls relating to the provision of counterpart contributions and the accountability for funds provided by A.I.D.. These controls related to grantees' quarterly disbursements reports, supporting documents for counterpart contributions and A.I.D. disbursements, and closeout procedures to determine whether transactions were documented, recorded and executed. We conducted tests to determine that counterpart contributions and reimbursed costs were not overstated and were supported by valid documentation. Our tests showed that controls were logically designed and consistently applied, except that deficiencies in the verification process resulted in about $240,0000 in overstated and unauthenticated counterpart contributions and about $28,000 in invalid payments for goods, services and taxes.

REPORT ON COMPLIANCE

This section summarizes our conclusions on USAID/Philippines' compliance with applicable laws and regulations.

Scope of Our Compliance Assessment

We conducted our audit in accordance with generally accepted government auditing standards, which require that we

- assess compliance with applicable requirements of laws and regulations when necessary to satisfy the audit objectives (which includes designing the audit to provide reasonable assurance of detecting abuse or illegal acts that could significantly affect the audit objectives) and

- report all significant instances of noncompliance and abuse and all indications or instances of illegal acts that could result in criminal prosecution that were found during or in connection with the audit.

We tested whether USAID/Philippines ensured that the grantees complied with grant agreements as they could affect our audit objectives. However, our objectives were not designed to provide an opinion on USAID/Philippines' overall assurance that the grantees complied with grant agreements and A.I.D. policies and procedures.

General Background on Compliance

Noncompliance is a failure to follow requirements or a violation of prohibitions contained in statutes, regulations, contracts, grants and binding policies and procedures governing an organization's conduct. It constitutes an illegal act when there is a failure to follow requirements of laws or implementing regulations, including intentional and unintentional noncompliance and criminal acts. Not following internal control policies and procedures in the A.I.D. Handbooks generally does not fit into this definition of noncompliance and is included in our report on internal controls. Abuse is distinguished from noncompliance in that abusive conditions may not directly violate laws or regulations. Abusive activities may be within the letter of the laws and regulations but violate either their spirit or the more general standards of impartial and ethical behavior.

Compliance with the grant agreements is the overall responsibility of USAID/Philippines' management.

Conclusions on Compliance

USAID/Philippines ensured that the grantees complied with the grant agreements except that host-country taxes were billed and reimbursed as discussed on page 20 of this report. Section X of the grant agreements provide that grant funds shall not be used to pay identifiable taxes.

SCOPE AND METHODOLOGY

Scope

We audited USAID/Philippines' Enterprise in Community Development Project in accordance with generally accepted government auditing standards. Audit field work was conducted from February through April 1991 and covered disbursements of $323,365, or about 25 percent of $1.3 million of A.I.D. expenditures as of December 31, 1990. Likewise, counterpart contributions examined amounted to $326,119, or about 30 percent of total agreed-to counterpart contributions. Field work was conducted at USAID/Philippines and at six subprojects located in five provinces--(1) Marsman Estate Plantation, Inc. in Santo Thomas, Davao del Norte; (2) Del Monte Philippines, Inc. in Manolo Fortich, Bukidnon; (3) Victorias Milling Company, Inc. in Victoria, Negros Occidental; (4) International Pharmaceuticals, Inc. in Mabolo, Cebu City and (5) Dole Philippines, Inc. in Polomolok, South Cotabato.

Documents provided by USAID/Philippines and the grantees were the project paper, grant agreements, correspondence, progress reports, site visit reports, and payment vouchers. The audit team conducted site inspections; compared actual accomplishments against planned targets; analyzed the project paper, progress reports and site visit reports; validated documents supporting payment vouchers; and interviewed Mission and grantee officials and project beneficiaries to verify the evidence provided. We also reviewed Mission and grantee internal controls and considered the observations disclosed by a local management consulting firm, which was contracted by USAID/Philippines to conduct financial reviews of the grantees.

The Fiscal Year 1991 Audit Plan identified only two audit objectives for this project audit--monitoring and technical assistance. Subsequent changes in project design made the technical assistance objective no longer applicable. Therefore,

we substituted an audit objective to assess counterpart contributions and financial accountability. There was no prior audit of this project.

Methodology

The project had 12 subprojects at the time of the audit. Six were chosen for review because of their high dollar value, nearness of completion and extensiveness of subproject activities. Disbursements for this sample amounted to $854,497, or about 66 percent of total project expenditures.

The methodology for each audit objective follows:

Audit Objective One

To accomplished the first audit objective, we (1) reviewed the project paper, including the logical framework, and grant agreements to determine monitoring, reporting and evaluating plans, (2) discussed with USAID/Philippines and grantee officials methods and procedures established to monitor, evaluate and report on the status and progress of the subproject activities and (3) concluded whether the system provides for:

- monitoring grantees' compliance with the grant agreements and A.I.D. policies and procedures,
- identifying potential problems by timely gathering of quantitative information critical to project success,
- assuring that AID-financed commodities and services are used effectively to produced intended benefits,
- identifying implementation problems and recommending corrective actions,
- ensuring sustainability of subproject activities after A.I.D. funding ends and
- phasing out A.I.D. funding of subprojects.

To answer the audit objective, we (1) analyzed the latest quarterly implementation plans and progress reports of the six sampled grantees, (2) reviewed 12 of the 16 site visit reports prepared by Mission personnel, (3) compared actual subproject accomplishments against planned targets, (4) visited six subprojects in five locations, (5) conducted interviews with subproject beneficiaries and (6) held discussions with USAID/Philippines and grantee officials to identify plans for correcting implementation problems and phasing out A.I.D. funding.

Audit Objective Two

The second objective was to assess controls in place to ensure that grantees contributed to the project as agreed and that A.I.D. funds were used and accounted for in accordance with A.I.D. procedures and the grant agreements. To accomplish the second objective, we determined whether (1) the grantees submitted quarterly disbursement reports in compliance with the grant agreements, (2) counterpart contributions claimed and A.I.D. disbursements made were supported by valid and authenticated documents, (3) A.I.D. payments were made in accordance with the commitment documents and were charged to the commitment liquidation records of subprojects and (4) disallowed costs were refunded to A.I.D. in an expeditious manner.

To answer the audit objective, we (1) reviewed the project paper, grant agreements, evaluation reports on internal controls and other correspondence; (2) examined the quarterly disbursement reports and supporting schedules, commitment liquidation records, payment vouchers and their supporting documentation, and grantees' books of accounts; (3) interviewed A.I.D. and grantee officials and project beneficiaries and (4) visited project sites and inspected major commodity items funded by A.I.D. or contributed by the grantees. Judgmental sampling was used in the selection of payment vouchers to determine the validity and authenticity of disbursements.

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5010-108

UNITED STATES GOVERNMENT

Memorandum

APPENDIX II

TO : Mr. Dennis Smith
Resident Auditor, RAO/M

DATE: JUL 3 1991

FROM : Malcolm Butler
Director, USAID/Manila

SUBJECT : Enterprise in Community Development Project; USAID comments on Draft Audit Report No. 2-492-91-242 dated June 5, 1991

I. What follows are USAID's comments on the subject audit. We appreciate the cooperation that you and your staff provided throughout the audit process. USAID concurs with the substance of the draft report. While we take no exception to the seven recommendations, this memo provides some additional information on the Enterprise in Community Development (ECD) Project so that both the problems identified and the project's many accomplishments can be better understood. We request that recommendations 1, 2, 4, 5, 6, and 7 be considered resolved upon issuance of the final report. This memo also requests that recommendation No. 3 be closed upon issuance of the final report.

II. Recommendations and Responses

A. Recommendation No. 1: "We recommend that USAID/Philippines amend the project design to include new quantitative indicators of progress, a quantitative project purpose, and a new logical framework."

USAID will amend the project design to include more quantitative indicators of progress, a quantitative project purpose and a revised logical framework. USAID will incorporate the recommendations of the recently completed ECD Strategic Assessment into the redesign process. We anticipate that the revised project design and indicators will better reflect the current project reality, that is, we have been doing more with fewer grantees as highlighted in the draft audit report.

Based on the above, USAID requests that recommendation No. 1 be resolved upon issuance of the final report. USAID will request closure of recommendation No. 1 when the project design of ECD is amended.

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B. Recommendation No. 2: "We recommend that USAID/Philippines improve its monitoring information by requiring Grantees to submit quantitative quarterly progress reports, which identify information critical to project success and compare it to plans and schedules for the purpose of alerting management to potential problems."

OFFPVC is currently revising the ECD Quarterly Progress Report to make it a more efficient monitoring tool in terms of measuring project progress against planned project outputs.

We believe that changing the form alone will not necessarily produce the kind of data required by the Mission staff. Therefore, USAID will train Grantees in the use of the revised report during its on site and live-in training seminars such as the 1991 Fiscal and Program Management Workshop scheduled for Davao in July, 1991.

Based on the above, USAID requests that recommendation No. 2 be resolved upon issuance of the final report. USAID will request closure of recommendation No. 2 when the July 1991 workshop is completed.

C. Recommendation No. 3: "We recommend that USAID/Philippines establish a procedure for evaluating site visit reports to confirm the status of the project activities and that problem areas are recognized and appropriate follow-up actions are taken."

OFFPVC has already strengthened its internal procedures for evaluating site visit reports to ensure that problem areas are recognized and appropriate follow-up actions are taken expeditiously. This is being accomplished by implementing a tracking system for recommendations from site visit reports as described in Annex A attached for your review. USAID requests that the RAO close Recommendation No. 3 upon issuance of the final report.

D. Recommendation No. 4: "We recommend that USAID/Philippines in coordination with the grantees develop a plan and budget for phasing out A.I.D. support for project activities. The plan should be developed prior to the project completion date and require a commitment from the grantees to support priority activities."

While we find this recommendation helpful, we do not believe that current USAID and grantee efforts to plan for and implement sustainability were reflected in the draft audit report. Several steps have already been taken in this regard. For example:

1) The majority of our grants already deal with the sustainability issue in the implementation section of the grant, such as our grants with Davao Union Cement Corporation (signed June 21, 1989), Section 3.3, page 9; Del Monte Philippines (signed June 23, 1988), Section 3, pages 5-6; and Victorias Milling Company (signed May 16, 1989), Section 3, page 8.

2) Our most recent grant is with Aboitiz and Company, Inc. (ACO). This grant was signed on July 11, 1990. Section 3.5 of this grant agreement is titled "Sustainability" and includes a sustainability plan for each project component.

Having said that, guidelines are currently being developed to formalize the requirement that sustainability needs to be treated in advance of project completion. These guidelines will accomplish the following:

1. An initial sustainability plan will now be required in all future ECD project proposals;

2. During the mid-term evaluation of each ECD project, this initial sustainability plan will be reviewed and revised as appropriate; and

3. ECD staffers will meet individually with all existing Grantees in order to draw up sustainability plans for each grant subcomponent and to strengthen those plans which require it.

In sum, we believe that it is important that prospective Grantees consider sustainability issues when they are initially designing their proposals and that a mid-term review of their plans would be appropriate as circumstances frequently change.

Based on the above, USAID requests that recommendation No. 4 be resolved upon issuance of the final report. USAID will request closure of recommendation No. 4 when the above guidelines are formalized.

E. Recommendation No. 5: "We recommend that USAID/Philippines establish procedures to conduct regular payment verification procedural tests of Grantees counterpart contributions and A.I.D. funds to determine whether all relevant internal control measures are complied with fully."

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In addition to spot checks and close-out reviews, USAID conducts payment verification of Grantees' counterpart contribution through a local management consultancy firm (UICI). We contracted UICI "to assist USAID in helping its Grantees to set-up complete project accounting books and record-keeping systems and project reporting systems following generally accepted accounting and recording principles, including those books and records accounting for USAID funds and grantee counterpart", which consists of cash and non-cash contributions.

In addition, training for ECD Grantees is being stepped up in (a) financial management of ECD projects; (b) use and application of generally accepted and standard accounting systems; (c) record keeping systems, accounting books and reporting systems; and (d) the application of USAID regulations, policies and guidelines, such as those in the Grant Agreement and Handbook 13.

Recently, USAID published the Financial Management Manual for ECD Grantees which provides guidelines on accounting controls and procedures, USAID operating and financial guidelines, accounting for counterpart contribution and financial management reporting system. Copies of the manual were distributed to all ECD Grantees during the PVO/ECD Annual Meeting (September 1990), the Financial Management Workshop (January 1991) and the Project Development Workshop (February 1991). The same manual is being used by UICI as reference in conducting the on-site financial management training for ECD subproject staff.

A Fiscal and Program Management Workshop is scheduled in July this year for ECD Grantees. This will be handled by OFFPVC staff; technical support has been asked from the Controller and his staff; Development Resources Management (DRM) and Contracts Services Office (CSO) are also expected to provide technical support for this activity.

Based on this recommendation, we are amending our UICI contract to place additional emphasis on conducting regular payment verification procedural tests of grantees' counterpart contributions and AID funds to determine that all relevant internal control measures are fully complied with.

Based on the above, USAID requests that recommendation No. 5 be resolved upon issuance of the final report. USAID will request closure of recommendation No. 5 when the UICI contract is amended.

F. Recommendation No. 6: "We recommend that USAID/Philippines, based on the results of investigation conducted by the Inspector General/Investigations, recover any misused funds from the grantees."

We agree with the substance of this recommendation and are awaiting RIG/I's report. We have already requested one Grantee to reimburse misused funds. Please refer to Annex B. Based on the above, USAID requests that recommendation No. 6 be resolved upon issuance of the final report. USAID will request closure of recommendation No. 6 when any misused funds have been recovered or deducted from the Grantee' payment request.

G. Recommendation No. 7: "We recommend that USAID/Philippines request the grantee to refund the amount of $1,100 representing tax payments."

USAID has requested the Grantee to refund the amount representing tax payments (See Annex C). Based on the above, we request that this recommendation now be resolved upon issuance of the final report. USAID will close recommendation No. 7 when the Grantee has refunded $1,100 or deducted this amount from the Grantee's payment request.

Attachment: a/s

cc: IG/PPO
Mr. John Winn, ENE/DP/F
J. Rudasill-Bey, ENE/DP/F

ANNEX A

M E M O R A N D U M

TO: ECD Staff

DATE: June 25, 1991

THRU: Bryant George, Chief, O/FFPVC

FROM: Joshua V. Fliegel, ECD Coordinator

SUBJECT: New Procedure for Following-up on Actions/Problems Identified in ECD Site Visit Reports

The recent ECD draft audit report recommended that USAID/Philippines establish a procedure for evaluating site visit reports to confirm that problem areas are recognized and appropriate follow-up actions are taken. The audit acknowledged that while our field trip visits were adequately documented describing problems and identifying recommendations, follow-up actions were oftentimes not taken to remedy the problems. In view of these findings, the following procedures will be used by ECD staff for all future field-trip visits:

1. Aside from documenting progress made-to-date under each ECD project and comparing this information to the various implementation and progress reports submitted by the Grantee, the field trip report should continue to identify any problem areas, describing them in specific terms. (To the extent possible, please take advantage of visits to propose remedies for those problems which the staff have sufficient experience in dealing with. This information should also be included in the report.)

2. Please include in the report specific recommendations to resolve those problems which could not be handled in the field during the visit. The recommendations should be very specific so grantees subsequently receiving a copy of the report will understand precisely what corrective actions should be undertaken. The recommendations should also be practical to ensure that Grantees can undertake corrective measures easily. If the report contains more than one recommendation, they should be numbered for easy reference in future correspondence. We will review each report and its recommendations with the author to ensure these precepts are followed.

3. Once the report is finalized, a copy of the report will be sent to the Grantee along with a cover letter (drafted by the staffer who made the visit for Bryant George's signature) requesting the Grantee to respond to the recommendations within 45 days. If the problem identified is a very complex one, a longer deadline may be indicated in our cover letter for response/corrective actions.

4. A master listing will be maintained of all recommendations by Grantee, ECD field trip staffer, date of travel, and number of recommendations so that the status of each recommendation can be easily tracked.

5. Please note, however, that the ECD staffer who drafted each report and the cover letter to the Grantee will have to maintain contact with the Grantee and see to it that adequate corrective actions are taken by the Grantee on time. The Grantee will be requested in the initial cover letter to respond in writing describing their actions to rectify each problem/close the recommendation. Once their response is deemed adequate following staff review, the ECD staffer who drafted the report will draft another letter to the Grantee (for Mr. George's signature) notifying them that the recommendation has been closed. Staff are encouraged to look into the matter in the next field trip to confirm whether actions taken were indeed adequate. If not, it may be decided that the recommendation will be re-opened.

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U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

Ramon Magsaysay Center
1680 Roxas Boulevard
Ermita 1000, Manila
Philippines

Fax No.: 632-521-5241
Tel. No.: 632-521-7116

June 26, 1991

Mr. Pio Castillo, Sr.
President
International Pharmaceuticals, Inc.
Juan Luna Avenue, Mabolo
6000 Cebu City

SUBJECT: Grant No. AID 492-0395-G-SS-9059-00

Dear Mr. Castillo:

We appreciate your continued efforts to adhere to the provisions of the grant agreement in the implementation of the Reforestation and Water Drilling Project. USAID, for its part, is committed to improving our mutual project management performance. The training programs and workshops that USAID initiated for ECD Grantees are geared toward this objective.

At this point, however, we have one problem. The results of the recent audit of the Enterprise in Community Development (ECD) Project conducted by our Auditors show that IPI paid P29,845.00 in value added taxes (VAT) in the purchase of seven units of motorcycles.

As you may know, Section 9.2 of the Grant Agreement provides that grant funds cannot be used to pay any identifiable taxes. In this regard, we request that IPI refund this amount to USAID within 30 days from receipt of this letter. There are two options that IPI may wish to consider:

a. Request the dealer/supplier to refund to IPI the amount paid for VAT by presenting a copy of Section 9.2 of the Grant Agreement, and remit the same amount to USAID; or

b. Use company funds to refund the amount to USAID; this will be considered as part of your counterpart contribution for the grant.

In any event, the refund check should be made payable to the Treasurer of the United States.

If there is anything that we can do to assist the project staff in implementing the project, please do not hesitate to contact the ECD staff at 521-7116 loc. 2444/2445/2446.

Sincerely,

J. C. Stanford
Controller

cc: Ms. Flor Abillo

MASTER LIST: ECD Field Trip Recommendations

ECD Staffer	Grantee Visited	Date of Visit	Number of Recommendations	Deadline	Status (open/closed)

March 22, 1991

Mr. Pio V. Castillo
President
International Pharmaceuticals, Inc.
Juan Luna Avenue
Mabolo, Cebu City

Subject: Grant No. AID 492-0395-G-SS-9059-00
Reforestation and Water Project

Dear Mr. Castillo:

This is to acknowledge receipt of your letter to Mr. Bryant George indicating that you have investigated and filed charges against former Project staff assigned to implement the subject grant. We believe you have acted prudently by doing so.

The activities of these individuals have seriously jeopardized the relationship between USAID and IPI. Their actions could lead to the immediate suspension and or termination of activities under this grant. I understand that your staff has been working to determine the specific amount of project funds involved in any anomaly. We will conduct a review also. We recommend that those persons responsible pay this amount back to the project within 30 days. If they are unable or unwilling to do so, IPI must pay the amount in question back to the project.

The USAID Regional Inspector General's Office for Audit (RIG/A) is sending a team composed of Mr. Ramon Saguinsin and Ms. Inma Tipgos to IPI from April 3 to 10, 1991. Please ensure that your staff answers any questions they have about the implementation of the grant.

We do hope you will give this matter your most immediate attention and trust that should you have any questions, you will not hesitate to contact us.

Sincerely,

S.D. Heishman
Contracting Officer

OFFPVC:JLFliegel:CMI
1236F (p.41) 03/18/91

Clearances: O/FFPVC:BGeorge (draft)
OLA: LChiles (draft)
OFM:JCStanford (draft)

APPENDIX III

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