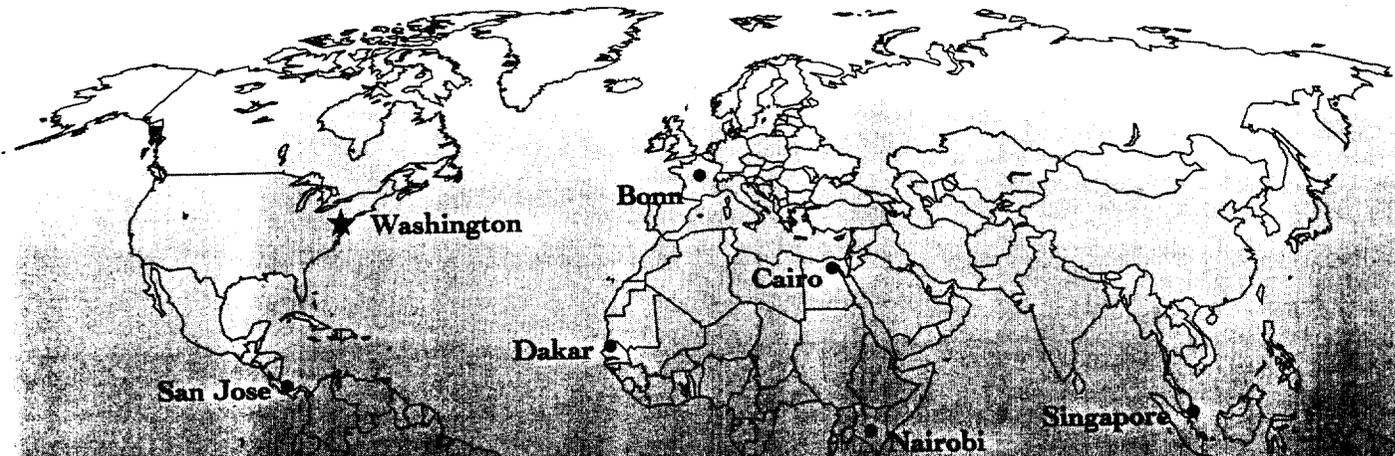


Regional Inspector General for Audit
Cairo, Egypt

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Financial Audit of the Science and Technology Cooperation, Expenditures Incurred Under the Scientific Research and Technology Cooperation Project (USAID/Egypt Project No. 263-0140)

Report No. 6-263-96-21-N
May 16, 1996



U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT



**UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT
OFFICE OF THE REGIONAL INSPECTOR GENERAL/AUDIT**

CAIRO, EGYPT

May 16, 1996

MEMORANDUM

TO : DIRECTOR USAID/Egypt, John R. Westley
FROM: RIG/A/C, Lou Mundy *Lou Mundy*
SUBJECT: Financial Audit of the Science and Technology Cooperation, Expenditures Incurred Under the Scientific Research and Technology Cooperation Project (USAID/ Egypt Project No. 263-0140)

The attached report, transmitted March 17, 1996, by KPMG Hazem Hassan, presents the results of a financial audit of the Science and Technology Cooperation (STC) under Project Implementation Letters Nos. 4 and 7 of the Scientific Research and Technology Cooperation Project, USAID/Egypt Project No. 263-0140. The objectives of PIL Nos. 4 and 7 are to support the activities of STC's management system and to redirect Egyptian science and technology programs to solving critical production problems of public and private industries.

We engaged KPMG Hazem Hassan to perform a financial audit of STC's incurred expenditures of \$509,371 for the period October 1, 1992 through November 30, 1994 for PIL No. 4 and \$251,439 for the period November 1, 1991 through February 28, 1995 for PIL No. 7. The purpose of the audit was to evaluate the propriety of costs incurred during this period. KPMG Hazem Hassan also evaluated STC's internal controls and its compliance with applicable laws, regulations and agreement terms as necessary, in forming their opinion regarding the Fund Accountability Statement.

The audit report questions \$204 and \$630 in costs billed to USAID/Egypt by the STC under PIL Nos. 4 and 7 respectively. The auditors did not note any material weaknesses in STC's internal control structure nor any material instances of noncompliance with applicable laws, regulations and agreement terms. The auditors did note, however, two reportable conditions in STC's internal controls.

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In response to the draft report, responsible STC officials provided additional explanation to the report findings. KPMG Hazem Hassan officials reviewed STC's response to the findings and where applicable made adjustments to the report or provided further clarification of their position (see Appendices I and II).

The following recommendation is included in the Office of the Inspector General's recommendation follow-up system.

Recommendation No. 1: We recommend that USAID/Egypt resolve the questioned costs of \$834 (ineligible costs of \$564 and unsupported costs of \$270) detailed on pages 14 through 18 of the KPMG Hazem Hassan audit report, and recover from the Science and Technology Cooperation the amounts determined to be unallowable.

In its response to the audit report, the Mission determined that \$321 of the costs questioned is considered allowable. The remaining questioned costs of \$513 is sustained and deducted from two vouchers billed by STC to USAID/Egypt (see Appendix III). Therefore, recommendation No. 1 is resolved and closed.

The reportable conditions identified by the auditor's review of STC's internal control structure should be handled directly between Mission and STC officials.

Thank you for the cooperation and assistance extended to the audit staff on this engagement and your continued support of the financial audit program in Egypt.

Attachment: a/s

Financial Audit of the
Science and Technology Cooperation
(STC)
Project Implementation Letters (PILs) Nos.4 and 7
Under the Scientific Research and Technology
Cooperation Project No.263-0140.01
for the Period from October 1, 1992
through November 30, 1994 for PIL No.4 and
from November 1, 1991 through February 28, 1995 for
PIL No.7

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Financial Audit of the
Science and Technology Cooperation
(STC)
Project Implementation Letters (PILs) Nos.4 and 7
Under the Scientific Research and Technology
Cooperation Project No.263-0140.01
for the Period from October 1, 1992
through November 30, 1994 for PIL No.4 and
from November 1, 1991 through February 28, 1995 for
PIL No.7

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Mr. Lou Mundy
Regional Inspector General for Audit-Cairo
United States Agency for International Development
Cairo, Egypt.

March 17, 1996

Dear Mr. Mundy,

This report represents the results of our financial audit of the Science and Technology Cooperation (STC) pursuant to Project Implementation Letters (PILs) Nos.4 and 7 under the Scientific Research and Technology Cooperation Project No.263-0140.01 for the periods from October 1, 1992 through November 30, 1994 for PIL No. 4 and from November 1, 1991 through February 28, 1995 for PIL No.7.

Background

The project is directly administered by the Academy of Scientific Research and Technology (ASRT) and financed through Project Implementation Letters (PILs) Nos.4 and 7.

The objective of PIL No.4 is to support the activities of the management system of the Scientific and Technology Cooperation Project (STC). The objective of PIL No.7 is to redirect Egyptian Science and Technology programs to solving critical production problems of public and private industries.

On June 26, 1988 and October 25, 1989 USAID/Egypt initiated PILs Nos.4 and 7 respectively.

Both PILs were amended several times. On September 5, 1994 amendment No.10 for PIL No.4 was issued to increase the budget to LE4,459,000 (equivalent to \$1,328,665) and the PIL completion date became September 30, 1995.

Amendment No.9 was issued on September 5, 1994 for PIL No.7 to increase the budget to \$450,000. On October 4, 1994 amendment No.10 was issued to extend the PIL completion date to September 30, 1995.

A non-Federal audit was conducted for the Project and an audit report was issued on February 7, 1993. This report was for the period from June 26, 1988 through September 30, 1992 for PIL No.4 only.

Audit Objectives and Scope

The objective of this engagement was to conduct a financial audit of USAID/Egypt's resources, provided pursuant to PILs Nos.4 and 7 under the Scientific Research and Technology Cooperation Project No.263-0140.01. These resources were managed by STC. The audit covered the period from October 1, 1992 through November 30, 1994 for PIL No.4 and from November 1, 1991 through February 28, 1995 for PIL No.7. The audit encompassed an examination of STC expenses and whether they were in compliance with the terms of the PILs and a review of the internal controls.

The specific objectives were to:

1. express an opinion on whether the fund accountability statements for the USAID financed project of STC present fairly, in all material respects, project revenues received and costs incurred for the periods under audit, in conformity with generally accepted accounting principles or other comprehensive bases of accounting, including the cash receipts and disbursements basis and modifications of the cash basis;
2. determine if the costs reported as incurred under the agreement are, in fact, allowable, allocable, and reasonable in accordance with the terms of the agreement;

3. evaluate and obtain a sufficient understanding of the internal control structure of STC, assess control risk, and identify reportable conditions, including material internal control weaknesses; and
4. perform tests to determine whether STC complied, in all material respects, with the agreement terms and applicable laws and regulations;

Preliminary planning and review procedures started in July 1995 and consisted of:

- discussions with RIG/A/C;
- a review of the PILs;
- interviews and discussions with the STC key personnel concerning the status of the PILs, accomplishments during the period, the statutory reporting requirements, the budgets of the PILs, procedures governing actual expenditures by STC and reimbursement by USAID;
- reviews of the STC organizational structure, procurement and personnel manuals, financial and accounting policies, and procedures manual.

The field work was completed on October 1, 1995. The scope of our work was to audit costs incurred by STC and reimbursed by USAID/Egypt under PILs Nos.4 and 7. Within each budget line item, we selected amounts for testing on a judgmental basis to test the majority of the related amounts. We tested expenditures of \$65,021 out of total expenditures amounting to \$251,439 for PIL No.7. and LE417,280 (equivalent to \$124,338) out of total expenditures amounting to LE1,709,450 (equivalent to \$509,371) for PIL No.4.

Our tests of expenditures included, but were not limited to, the following:

1. Reconciling STC's accounting records to invoices issued to USAID/Egypt and testing costs for allowability, allocability, reasonableness, and appropriate support;
2. Determining whether payroll costs were appropriate and conformed with the terms of the PILs and the relevant regulations;

3. Determining whether meetings, consulting, equipment, travel, special studies and contingency charges were adequately supported and approved;
4. Checking the adequacy of STC's control over project equipment funded by USAID/Egypt.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the fund accountability statements are free of material misstatement.

We did not have an external quality control review by an unaffiliated audit organization, as required by paragraph 33 of Chapter 3 of Government Auditing Standards, because no such quality control review program is offered by professional organizations in Egypt. We believe that the effect of this departure from the financial audit requirements of Government Auditing Standards is not material because we have participated in the KPMG worldwide internal quality control program. This program requires our office to be subjected, every two years, to an extensive quality control review by partners and managers from other KPMG offices.

As part of our examination, we made a study and evaluation of relevant internal controls and reviewed STC's compliance with applicable laws and regulations.

Results of Audit

PIL No.4 Fund accountability statement

Our audit identified questioned costs totalling \$204 (equivalent to LE686) which are considered as ineligible costs.

PIL No.7 Fund accountability statement

Our audit identified questioned costs totalling \$630 which are divided into ineligible costs amounting to \$360 and an unsupported cost of \$270.

Internal Control

Our audit identified the following reportable conditions:

- Fund reconciliations for PIL No.4 were not prepared.
- STC does not maintain a chart of accounts.

Compliance with Laws and Regulations

Our tests of compliance disclosed certain instances of noncompliance with the terms of PIL No.4 regarding the allowability, allocability and reasonableness of costs charged to USAID/Egypt. These instances are not considered to be material instances of noncompliance.

Follow-up on the Previous NFA Report

We have followed up on the findings and recommendations identified in the previous NFA report for the period from June 26, 1988 through September 30, 1992 for PIL No.4, as required by paragraph 10 of Chapter 4 of Government Auditing Standards.

Findings and recommendations that may affect the fund accountability statement have been considered during our audit. Findings resolved and recommendations implemented, to our satisfaction, have not been mentioned in this report.

Supplementary Information

The supplementary fund accountability statements, presented in the functional currency, and schedules of questioned costs including dates, number of vouchers and amounts were communicated to STC's management and are available upon request.

Management Comment

We have reviewed STC's response to the Questioned Costs Incurred, which is included as Appendix I. Where applicable, we have made adjustments in our report or provided further clarification of our position in Appendix II. For those items not adjusted in the final report, the responses provided by STC's management have not changed our understanding of the fund accountability statements reportable conditions and material weaknesses in the Report on Internal Control Structure or our findings in the Report on Compliance with Laws and Regulations.

KPMG Hazem Hassan

This report is solely intended for the use of the United States Agency for International Development and may not be suitable for any other purpose.



Hazem Hassan & Co.
Cairo, Egypt



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Report on Fund Accountability Statements Independent Auditor's Report

Mr. Lou Mundy
Regional Inspector General for Audit-Cairo
United States Agency for International Development
Cairo, Egypt.

We have audited the accompanying fund accountability statements of the Science and Technology Cooperation (STC) pursuant to the Project Implementation Letters (PILs) Nos.4 and 7 under the Scientific Research and Technology Cooperation Project No.263-0140.01 for the period from October 1, 1992 through November 30, 1994 for PIL No.4 and from November 1, 1991 through February 28, 1995 for PIL No.7. These statements are the responsibility of STC's management. Our responsibility is to express an opinion on these statements based upon our audit.

Except as discussed in the following paragraph, we conducted our audit 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 fund accountability statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the fund accountability statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the presentation of the overall fund accountability statements presentation. We believe that our audit provides a reasonable basis for our opinion.

We did not have an external quality control review by an unaffiliated audit organization, as required by paragraph 33

of Chapter 3 of Government Auditing Standards, because no such quality control review program is offered by professional organizations in Egypt. We believe that the effect of this departure from the financial audit requirements of Government Auditing Standards is not material because we have participated in the KPMG worldwide internal quality control program. This program requires our office to be subjected, every two years, to an extensive quality control review by partners and managers from other KPMG offices.

The aforementioned fund accountability statements do not include the cost of USAID/Egypt's direct procurement of vehicles, equipment, and technical assistance provided by USAID/Egypt directly to STC or the total revenues and costs incurred by STC on an organization-wide basis.

As described in Note 1, the accompanying fund accountability statements have been prepared on the cash basis, which is a comprehensive basis of accounting other than the generally accepted accounting principles. Included in the fund accountability statements are questioned costs of \$204 and \$630 relating to the Project Implementation Letters (PILs) Nos.4 and 7, respectively. The basis for questioning these costs is more fully described in the "Details of Questioned Costs" section of this report.

In our opinion, except for the effects of the questioned costs as discussed in the preceding paragraph, the fund accountability statements referred to above present fairly, in all material respects, the amounts received and the costs incurred pursuant to the Project Implementation Letters (PILs) Nos.4 and 7 under the Scientific Research and Technology Cooperation Project No.263-0140.01 for the period from October 1, 1992 through November 30, 1994 for PIL No.4 and from November 1, 1991 through February 28, 1995 for PIL No.7 in conformity with the basis of accounting described in Note 1.



Hazem Hassan & Co.
Cairo, Egypt

October 1, 1995

THE SCIENTIFIC AND TECHNOLOGY COOPERATION (STC)
Fund Accountability Statement of Project Implementation Letter (PIL) No.4
Under the Science and Technology Cooperation Project No. 263-0140.01
For the Period from October 1, 1992 through November 30, 1994

USAID/Egypt fund received \$
486,233

<u>Expenditures</u>	<u>Questioned Costs</u>				<u>Finding No. & Pg.</u>
	<u>Budget</u>	<u>Actual</u>	<u>Ineligible</u>	<u>Unsupported</u>	
	\$	\$	\$	\$	
Salaries	790,226	308,631			
Meetings	17,878	906	-		
Consulting	73,004	11,779	45		2. b Pg. 14
Equipment & Supplies	153,456	29,055	-		
Travel & Training	49,166	22,425	71		4. a & b Pg. 15
Special Studies	161,502	89,699	88		5. c & d Pg. 16
Contingency & Misc.	83,433	46,876	-		
Total Expenditures	<u><u>1,328,665</u></u>	<u><u>509,371</u></u>	<u><u>204</u></u>	<u><u>---</u></u>	
 Expenditures over revenues		 23,138			
 USAID/Egypt Fund balance as of November 30, 1994		 <u><u>(23,138)</u></u>			

* The accompanying notes are an integral part of the fund accountability statement.

THE SCIENTIFIC AND TECHNOLOGY COOPERATION (STC)
Fund Accountability Statement of Project Implementation Letter (PIL) No.7
Under the Science and Technology Cooperation Project No. 263-0140.01
For the Period from November 1, 1991 through February 28, 1995

USAID/Egypt fund received \$
273,705

<u>Expenditures</u>	<u>Questioned Costs</u>				<u>Finding No. & Pg.</u>
	<u>Budget</u>	<u>Actual</u>	<u>Ineligible</u>	<u>Unsupported</u>	
	\$	\$	\$	\$	
Travel and Consultants	450,000	251,439	360	270	1. c & d Pg. 18
Total Expenditures	<u><u>450,000</u></u>	<u><u>251,439</u></u>	<u><u>360</u></u>	<u><u>270</u></u>	
Revenues over expenditures		22,266			
Line of Credit in NIB		12,913			
USAID/Egypt Fund balance as of February 28, 1995		<u><u>35,179</u></u>			

* The accompanying notes are an integral part of the fund accountability statement.

Scientific and Technology Cooperation
(STC)
Fund Accountability Statements
Project Implementation Letters (PILs) Nos.4 and 7

Notes to the Fund Accountability Statements

Note 1: Accounting Basis

The fund accountability statements have been prepared on the basis of cash receipts and disbursements. Consequently, revenues are recognized when they are actually received and expenditures are recognized when they are actually paid.

Note 2: Basis of Presentation

The fund accountability statements are the representation of STC's management and are the responsibility of the said management. The "Questioned Costs" columns represent the audit results and are included in the fund accountability statements for presentation purposes only.

Note 3: Translation Rate

The expenditures of PIL No. 4, which were paid in Egyptian Pounds (LE), have been translated into US Dollars (\$). The period average exchange rate method was used. This rate is \$1 = LE3.356. The original currency of PIL No.7 is US dollars.

Note 4: Questioned Costs

Questioned Costs are presented in two separate categories - ineligible or unsupported - and consist of audit findings made on the basis of the terms of the PILs and related regulations, which prescribe the nature and treatment of reimbursable

costs. Costs in the column labeled "Ineligible" are supported by vouchers or other documentation but are ineligible for reimbursement because they are either unreasonable, not program related, or are prohibited by the PILs or applicable laws and regulations.

Costs in the column labeled "Unsupported" are also included in the classification of "Questioned Costs" and are related to costs that are not supported by adequate documentation. All questioned costs are detailed in the "Details of Questioned Costs" section of this report.

Note 5: USAID/Egypt funds received

USAID/Egypt's funds received represent those received for the audited period from October 1, 1992 through November 30, 1994 for PIL No.4 and from November 1, 1991 through February 28, 1995 for PIL No.7.

Note 6: Line of Credit in the National Investment Bank (NIB) for PIL No.4

STC have one bank account for both PIL No.4 and the LE portion of PIL No.7. The LE portion of PIL No.7, was not included in the audit scope of work. Both PILs have one line of credit. Although the bank reconciliation was agreed to the bank statement, we were unable to separate between the line of credit for each PIL.

Note 7: Line of Credit in the National Bank of Egypt for PIL No.7

On November 2, 1990 the National Bank of Egypt opened a line of credit for the project amounting to \$40,000.

During the period from November 2, 1990 through October 31, 1991, STC used an amount of \$27,087 to cover the expenditures incurred in excess of the funds received from USAID/Egypt during the period. Consequently, the line of credit balance as of November 1, 1991 was \$12,913.

Note 8: Budget

The budget represents USAID/Egypt's approved budget in accordance with the most recent amendments of the PILs Nos.4 and 7 which were made within the audited period. It includes the total budget of the project from June 26, 1988 through November 30, 1994 for PIL No.4 and from October 25, 1989 through February 28, 1995 for PIL No.7.

Details of Questioned Costs
Project Implementation Letter No.4
Fund Accountability Statement

<u>Item Description</u>	<u>Questioned Costs</u>	
	<u>Ineligible</u>	<u>Unsupported</u>
	\$	\$
1. <u>Salaries</u>		
a) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.	---	
b) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.	---	
Total line item	<u>---</u>	<u>---</u>
2. <u>Consulting</u>		
a) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.	---	
b) The amount billed to USAID/Egypt was \$130. The actual amount paid to the consultant was \$85. The difference is \$45, which is considered to be unallowable.	45	
Total Line Item	<u>45</u>	

<u>Item Description</u>	<u>Questioned Costs</u>	
	<u>Ineligible</u>	<u>Unsupported</u>
	\$	\$
3. <u>Equipment and Supplies</u>		
a) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.	---	
Total line item	<u>---</u>	<u>---</u>
4. <u>Travel and Training</u>		
a) This amount represents an amount in excess of USAID/Egypt's per diem rates for local travel. No USAID/Egypt approval is available for this excessive amount. Therefore, this amount is considered to be unallowable.	51	
b) This amount represents taxes paid to a Hotel. Article 46, Attachment B of OMB Circular No.A-122 states that taxes are not allowable. Therefore, this amount is considered to be unallowable.	20	
Total Line Item	<u>71</u>	<u>---</u>

<u>Item Description</u>	<u>Questioned Costs</u>	
	<u>Ineligible</u>	<u>Unsupported</u>
	<u>\$</u>	<u>\$</u>
5. <u>Special Studies</u>		
a) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.		---
b) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.	---	
c) This amount represents taxes paid to a Hotel. Article 46, Attachment B of OMB Circular No.A-122 states that taxes are not allowable. Therefore, this amount is considered to be unallowable.	73	
d) This amount represents an amount in excess of USAID/Egypt's per diem rates for local travel. There was no approval given by USAID/Egypt for this excessive amount. Therefore, this amount is considered to be unallowable.	15	
Total Line Item	<u>88</u>	<u>---</u>

<u>Item Description</u>	<u>Questioned Costs</u>	
	<u>Ineligible</u>	<u>Unsupported</u>
	<u>\$</u>	<u>\$</u>
6. <u>Contingency and Misc.</u>		
a) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.	---	
Total Line Item	<u>---</u>	<u>---</u>
Total Questioned Costs	<u>204</u>	<u>---</u>
		<u>204</u>

Details of Questioned Costs
Project Implementation Letter No.7
Fund Accountability Statement

<u>Item Description</u>	<u>Questioned Costs</u>	
	<u>Ineligible</u>	<u>Unsupported</u>
	<u>\$</u>	<u>\$</u>
1. <u>Travel and Consultants</u>		
a) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.	---	
b) Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.	---	
c) This amount represents taxes on air tickets. Article 46, Attachment B of OMB Circular No.A-122 states that taxes are not allowable. Therefore, this amount is considered to be unallowable.	360	
d) This amount represents lodging expenses for an investigator during his trip to the USA. No supporting documents were available to support this expense. Therefore, we consider this amount to be unsupported.		270
Total Line Item	<u>360</u>	<u>270</u>
Total Questioned Costs	<u>360</u>	<u>270</u>
		<u>630</u>



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Report on the Internal Control Structure
Independent Auditor's Report

Mr. Lou Mundy
Regional Inspector General for Audit-Cairo
United States Agency for International Development
Cairo, Egypt.

We have audited the accompanying fund accountability statements of the Science and Technology Cooperation (STC) for Project Implementation Letters (PILs) Nos.4 and 7 under the Scientific Research and Technology Cooperation Project No.263-0140.01 for the period from October 1, 1992 through November 30, 1994 for PIL No.4 and from November 1, 1991 through February 28, 1995 for PIL No.7, and have issued our report thereon on October 1, 1995.

Except as discussed in the following paragraph, we conducted our audit 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 fund accountability statements are free of material misstatement.

We did not have an external quality control review by an unaffiliated audit organization, as required by paragraph 33 of Chapter 3 of Government Auditing Standards, because no such quality control review program is offered by professional organizations in Egypt. We believe that the effect of this departure from the financial audit requirements of Government Auditing Standards is not material because we have participated in the KPMG worldwide internal quality control program. This program requires our office to be subjected, every two years, to an extensive quality control review by partners and managers from other KPMG offices.

The management of STC 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 the transactions are executed in accordance with the management's authorization and recorded properly to permit the preparation of fund accountability statements in accordance with the cash basis of accounting. Because of the 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.

In planning and performing our audit of the fund accountability statements of the Science and Technology Cooperation (STC) for Project Implementation Letters (PILs) Nos.4 and 7 under the Scientific Research and Technology Cooperation Project No.263-0140.01 for the period from October 1, 1992 through November 30, 1994 for PIL No.4 and from November 1, 1991 through February 28, 1995 for PIL No.7, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the fund accountability statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

We noted certain matters, involving the internal control structure and its operation that we consider to be a reportable condition under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the fund accountability statements. Our audit disclosed the following reportable conditions:

Finding No.1

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

Finding No.2

A fund reconciliation between the fund balance and the bank balance, as per books, was not prepared.

A sound internal control system requires that fund reconciliations be prepared in order to insure that cash disbursements and revenues received from USAID/Egypt have been recorded.

STC's management believes that bank reconciliations are adequate to control all cash disbursements and cash receipts.

The lack of fund reconciliations may impair the fair presentation of the fund balance as per the fund accountability statement.

We recommend that STC's management prepare fund reconciliations on a timely basis.

Finding No.3

During our audit we noted that STC does not maintain a detailed accounting manual.

A detailed accounting manual should be prepared in order to determine what should be charged on each line item.

STC's management asserts that they rely upon budget line items in determining costs charged on each line item.

The lack of such an accounting manual led to the misclassification of certain costs among line items. Although these misclassifications have no financial effect, they impair the presentation of the fund accountability statements.

We recommend that STC develop an accounting manual detailing the types of costs to be included in each budget line item.

A material weakness is a condition in which the design or operation of one or more of the specific internal control

KPMG Hazem Hassan

elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the fund accountability statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe that the reportable conditions described above are not material weaknesses.

We also noted another matter involving the internal control structure and its operation that we have reported to the management of STC in a separate letter dated October 1, 1995.

This report is intended for the information of STC's management and others within the organization and the United States Agency for International Development. However, this report is a matter of public record, and its distribution is not limited.



Hazem Hassan & Co.
Cairo, Egypt

October 1, 1995



Hazem Hassan

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Report on Compliance with Laws and Regulations Independent Auditor's Report

Mr. Lou Mundy
Regional Inspector General for Audit-Cairo
United States Agency for International Development
Cairo, Egypt.

We have audited the accompanying fund accountability statements of the Science and Technology Cooperation (STC) pursuant to the Project Implementation Letters (PILs) Nos.4 and 7 under the Scientific Research and Technology Cooperation Project No.263-0140.01 for the period from October 1, 1992 through November 30, 1994 for PIL No.4 and from November 1, 1991 through February 28, 1995 for PIL No.7, and have issued our report thereon on October 1, 1995.

Except as discussed in the following paragraph, we conducted our audit 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 fund accountability statements are free of material misstatement.

We did not have an external quality control review by an unaffiliated audit organization, as required by paragraph 33 of Chapter 3 of Government Auditing Standards, because no such quality control review program is offered by professional organizations in Egypt. We believe that the effect of this departure from the financial audit requirements of Government Auditing Standards is not material because we have participated in the KPMG worldwide internal quality control program. This program requires our office to be subjected, every two years, to an extensive quality control review by partners and managers from other KPMG offices.

Compliance with laws, regulations, contracts, and grants applicable to STC is the responsibility of STC's management. As part of obtaining reasonable assurance about whether the fund accountability statements are free of material misstatement, we performed tests of STC's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the fund accountability statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed one instance of noncompliance that is required to be reported herein under Government Auditing Standards. This instance is as follows:

1. Instance of non-compliance with the provisions of the PILs Nos.4 and 7, and OMB Circular No. A-122

During our audit we noted that STC paid and charged USAID/Egypt certain costs that are not in compliance with the PILs provisions or OMB Circular No.A-122.

PILs Nos.4 and 7 listed the exact amounts and type of costs which should have been charged to USAID/Egypt.

STC's management believed that these amounts were essential to carry out its activities and therefore chargeable to USAID/Egypt.

We recommend that STC obtain USAID/Egypt approval for the amounts exceeding the budget, and take the correct actions for the unallowable costs charged to USAID.

We consider the instance of non-compliance in forming our opinion on whether STC's fund accountability statements pursuant to the Project Implementation Letters (PILs) Nos.4 and 7 under the Scientific Research and Technology Cooperation Project No.263-0140.01 for the period from October 1, 1992 through November 30, 1994 for PIL No.4 and from November 1, 1991 through February 28, 1995 for PIL No.7, are presented fairly, in all material respects, in conformity with Generally Accepted Accounting Principles, and this report does not affect our report dated October 1, 1995 on the fund accountability statements.

KPMG Hazem Hassan

This report is intended for the information of STC's management and others within the organization and the United States Agency for International Development. However, this report is a matter of public record, and its distribution is not limited.



Hazem Hassan & Co.
Cairo, Egypt

October 1, 1995

Follow-up on the Previous NFA Report

We have followed up on the findings and recommendations identified in the previous NFA report for the period from June 26, 1988 through September 30, 1992 for PIL No.4, as required by paragraph 10 of Chapter 4 of Government Auditing Standards.

Findings and recommendations that may affect the fund accountability statement have been considered during our audit. Findings resolved and recommendations implemented, to our satisfaction, have not been mentioned in this report.

APPENDIX I
STC'S MANAGEMENT RESPONSE

**Response to the Draft NFA Report on
Science and Technology Cooperation (STC),
PILs 4 and 7, Local Expenditures Incurred under the
Science and Technology Cooperation,
Project No. 263-0140.01.**

Project Implementation Letter No. 4

Finding 1:

Salaries:

a. Questioned cost of \$ 25,720

This amount represents one month's salaries paid to STC employees in excess of the approved budget. STC obtains a yearly approval form USAID/Egypt stating the exact salary for each position. The extra month's salaries paid to STC employees and charged to USAID/Egypt are considered to be unallowable.

b. Questioned cost of \$ 24,034

This amount represents the employee's share of social security insurance. This amount should be deducted from the employees salaries rather than charged to USAID/Egypt. Therefore, this amount is considered to be unallowable.

STC's Response:

- a. According to Article 4 (Contractor's Compensation), item 4.2 of the Host Country Personal Services Contract of the Executive Director and STC Managers, the compensation includes a one-month bonus equivalent to one month salary.**

The Project Officer has also approved the readjustment of the Executive Director, Prof. Dr. Ahmad Samieh El Nockrashy's salary which includes a basic salary plus one month bonus, in his letter dated May 3, 1990 (attached are both his letter as well as the request of Prof. Dr. Ahmad Samieh El Nockrashy dated March 15, 1990).

All STC staff contracts also include the same provision of being compensated on the basis of a basic salary and a one-month bonus.

The Project Officer approval on the monthly bonus for STC employees has also been obtained (copy of the approval attached).

- b. The employee's share of social security insurance is deducted from the employees salaries each month and has never been charged to USAID/Egypt. Therefore, this finding is not applicable to STC at all.

As to the employer's share of social security and in response to FAST findings, the employer's share of social security has been charged to the Government of Egypt (GOE) contribution and deducted from USAID/Egypt PIL 4 expenditure.

Attached is a sample salary sheet for one of the employees. As can be seen, the employee share of social security is deducted from the salary released to the employee. As for the employer share which used to be charged to USAID/Egypt, all the amounts deducted from USAID/Egypt were summed up and paid from GOE contribution to the STC account at the National Investment Bank and hence deducted from the Secretariat's expenses.

Finding 2:

Consultants:

a. Questioned cost of \$ 491

This amount represents payments to 4 consultants for attending the laser program. Although the Steering Committee approval indicates the names of the consultants attending this program, the names of these 4 consultants were not included in this approval. Therefore, this amount is considered to be unallowable.

b. Questioned cost of \$ 45

The amount billed to USAID/Egypt was \$ 130. The actual amount paid to the consultant was \$ 85. The difference is \$ 45, which is considered to be unallowable.

STC's Response:

- a.** The STC Steering Committee decided on March 25, 1992 to carry out a background study on Laser applications in the fields of Agriculture, Industry, Health and Communications. The Minister of scientific research has nominated Egyptian experts to carry out the study. In response to the nomination, the nominated consultants found it necessary to incorporate 4 other Egyptian experts to carry out the work in this field. A letter from STC's Executive Director was therefore prepared to acknowledge the participation of these 4 Egyptian experts in the study. (copy of the letter is attached).
- b.** This questioned cost is acknowledged by STC.

Finding 3:

Equipment and Supplies:

a. Questioned cost of \$ 4,470

This amount represents the cost of printing a book about ASRT activities. Although STC is one component of ASRT, STC charged the full amount of the printing cost to USAID/Egypt. Additionally, we were unable to determine STC's share, which should have been charged to USAID/Egypt. Therefore, this amount is considered to be unreasonable.

STC's Response:

STC is one component of the ASRT and it was necessary to introduce the new component to the Egyptian Production ,Services and Science and Technology communities. Therefore, it was decided to publish this book to introduce STC within the framework of the ASRT umbrella; the book had been prepared by STC, where STC is described within the framework of the ASRT. An approval from the project officer for the payment for the printing of this book by STC has been obtained (copy of approval is attached).

Finding 4:

Travel and Training:

a. Questioned cost of \$ 51

This amount represents an amount in excess of USAID/Egypt's per diem rates for local travel. No USAID/Egypt approval is available for this excessive amount. Therefore, this amount is considered to be unallowable.

b. Questioned cost of \$ 20

This amount represents taxes paid to the Ramada Hotel. Article 46, Attachment B of OMB Circular No. A-122 states that taxes are not allowable. Therefore, this amount is considered unallowable.

STC's Response:

a. The questioned cost is acknowledged by STC.

b. The questioned cost is acknowledged by STC.

Finding 5:

Special Studies:

a. Questioned cost of \$ 670

This amount represents the cost for 3 employees to attend the Sixth Arab International Aluminium Conference. This amount is supported only by check. Voucher and cash receipts are not available. Therefore, this amount is considered to be unsupported.

b. Questioned cost of \$161

This amount represents accommodation fees for a journalist to attend a workshop. However, this journalist is not a participant in the project. Therefore, this amount is considered to be unallowable.

c. Questioned cost of \$ 73

This amount represents taxes paid to the Ramada Hotel. Article 46, Attachment B of OMB Circular No.A-122 states that taxes are not allowable. Therefore, this amount is considered unallowable.

d. Questioned cost of \$ 15

This amount represents an amount in excess of USAID/Egypt's per diem rates for local travel. There was no approval given by USAID/Egypt for this excessive amount. Therefore, this amount is considered to be unallowable.

STC's Response:

- a. STC is implementing two projects at the Aluminium Company of Egypt (EGYPTALUM). The achievements of these two projects were discussed during the Sixth Arab International Aluminium Conference held in Cairo from 11-14 December 1993. Therefore, STC's Executive Director nominated three STC employees for the attendance of this conference.

The conference registration fee was paid by check no. 2440790 dated 21/11/1993 and was cashed out by the conference organization on 20/12/1993 from STC's account at the National Investment Bank. Attached please find the bank reconciliation for this amount.

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- b. One of STC's objectives is to disseminate information on its activities and achievements in the different areas it works in. The participation of the media and public relations people is of great importance in disseminating STC's achievements in these areas. Attached please find the Project Officer approval on the participation of the media and public relations people in STC's seminars.
- c. This questioned cost is acknowledged by STC.
- d. This questioned cost is acknowledged by STC.

Finding 6:

Contingency and Misc.:

a. Questioned cost of \$ 3,128

This amount represents the cost of printing a book about ASRT activities. Although STC is one component of ASRT, STC charged the full amount of the printing cost to USAID/Egypt. Additionally, we were unable to determine STC's share, which should have been charged to USAID/Egypt. Therefore, this amount is considered to be unreasonable.

STC's Response:

- a. As one of the components of the ASRT, it was necessary to describe the achievements of STC within the framework of the ASRT to be presented during the First Scientific Research Day, which was attended by H.E. President Hosni Mubarak, H.E. the Prime Minister and Ministers of several other Ministries. The book was prepared by STC and therefore, it was paid for by STC. The Project Officer has approved on paying for the printing of this book by STC (copy of approval is attached).

Project Implementation Letter No. 7:

Finding 1:

Travel and Consultants:

a. Questioned cost of \$ 667

This amount represents an amount in excess of USAID/Egypt's rates for consultants. There was no approval given by USAID/Egypt for this excessive amount. Therefore, this amount is considered to be unallowable.

b. Questioned cost of \$ 2,104

This amount represents per diem and lodging costs for 4 investigators during their trip to Singapore. Their stay in Singapore was not stated in the PI approval. Therefore, we consider this amount to be unallowable.

c. Questioned costs of \$ 360

This amount represents taxes on air tickets. Article 46, Attachment B of OMB Circular No.A-122 states that taxes are not allowable. Therefore, this amount is considered to be unallowable.

d. Questioned costs of \$ 270

This amount represents lodging expenses for an investigator during his trip to the USA. No supporting documents were available to support this expense. Therefore, we consider this amount to be unsupported.

STC's Response:

- a. The actual questioned cost was found to be only \$ 400. The difference between the \$ 667 questioned cost presented by the Hazem Hassan Audit team and the \$ 400 actual questioned cost stems from the fact that the audit team calculated the maximum per diem rate as \$ 274 /day while in fact it is \$ 280/day as stated in PIL 7. This will lead to a total excess of \$ \$ 174 (29 nights * \$ 6). The remaining \$ 93 in excess stems from the fact that this amount has been deducted by STC from the per diem rate released to the Consultant because of lack of cash at the time. Hence the total amount of questioned cost is only \$ 400.

However, STC has obtained the approval of the Project Officer on increasing the daily rate payable to American consultants to be equivalent to the maximum payable daily rate of a Foreign Service Officer Class FS-1 according to Contractor Notices issued by USAID, Cairo. (Attached is a copy of this approval).

An approval was also obtained from the Project Officer on a daily rate of \$ 297 for this consultant, Dr. Victor Apps (Attached is a copy of this approval).

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- b. Within the framework of the observation/consultation trip carried out by 4 members of the research team of C/A 47, it was necessary to stay one night in Singapore on the trip to and from their destination because of the plane times. The Principal Investigator has sent a letter to STC approving their stay in Singapore and requesting STC's approval. (Attached is a copy of the PI letter).
- c. This questioned cost is acknowledged by STC.
- d. A certificate was provided by the traveler stating the circumstances regarding the stolen supporting documents. The project director approved the amounts stated in the traveler's claim taking into consideration its reasonableness and allocability in comparison to similar costs incurred by other travelers for the same destination, which has been accepted by FAST according to their follow-up report No. 2 dated December 11, 1995 to their report No. 95-07 (copy is attached).

Internal Control Structure:

Finding No. 1:

During our audit, we noted that evidence of approval of certain bank reconciliations was lacking.

Proper authorization of bank reconciliations is a necessary element of their internal control structure.

STC's management asserted that the review was performed. However, this review was not documented.

Lack of written approval will create future confusion as to whether reconciliations were actually approved.

We recommend that, all bank reconciliations be approved, in writing, by the appropriate staff member.

STC's response:

All bank reconciliations are prepared by the appropriate accountant assigned this task and who is also in charge of registering everything in the accounting books.

All bank reconciliations are then revised and approved by STC's Financial Manager.

All bank reconciliations are kept in a specific file at STC and are available.

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Finding No. 2:

A fund reconciliation between the fund balance and the bank balance, as per books, was not prepared.

A sound internal control system requires that fund reconciliations be prepared in order to insure that cash disbursements and revenues received from USAID/Egypt have been recorded.

STC's management believes that bank reconciliations are adequate to control all cash disbursements and cash receipts.

The lack of fund reconciliations may impair the fair presentation of the fund balance as per the fund accountability statement.

We recommend that STC's management prepare fund reconciliations on a timely basis.

STC's response:

A fund reconciliation between the fund balance and the bank balance, as per books, was prepared and revised for PIL 7. †

A fund record between the fund balance and the bank balance is being prepared at present for PIL 4 which states the number and amount of each claim and the check with which the money was released from USAID/Egypt which enables the preparation of the required reconciliation at any specific time taking into consideration the balance for Egyptian Pounds at the National Investment Bank and the total cash on hand for subprojects at the same date. (Attached please find a copy of this fund reconciliation book).

Finding 3:

During our audit we noted that STC does not maintain a detailed accounting manual.

A detailed accounting manual should be prepared in order to determine what should be charged on each line item.

STC's management asserts that they rely upon budget line items in determining costs charged on each line item.

The lack of such an accounting manual led to the misclassification of certain costs among line items. Although these misclassifications have no financial effect, they impair the presentation of the fund accountability statements.

We recommend that STC develop an accounting manual detailing the types of costs to be included in each budget line item.

STC's response:

STC is taking the necessary actions to prepare a detailed accounting manual.

APPENDIX II
AUDITOR'S COMMENTS

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AUDITOR'S COMMENTS

Page 1 of 3

PIL No.4

Finding No.1 a

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

Finding No.1 b

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

Finding No.2 a

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

Finding No.2 b

STC's management agree with this finding. Therefore, this finding will remain the same.

Finding No.3 a

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

Finding No.4 a

STC's management agree with this finding. Therefore, this finding will remain the same.

Finding No.4 b

STC's management agree with this finding. Therefore, this finding will remain the same.

Finding No.5 a

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

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Finding No.5 b

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

Finding No.5 c

STC's management agree with this finding. Therefore, this finding will remain the same.

Finding No.5 d

STC's management agree with this finding. Therefore, this finding will remain the same.

Finding No.6 a

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

PIL No.7

Finding No.1 a

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

Finding No.2 b

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

Finding No.2 c

STC's management agree with this finding. Therefore, this finding will remain the same.

Finding No.2 d

STC's management did not provide us with the supporting documents of this amount. Therefore, this finding will remain the same.

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Internal Control Structure

Finding No. 1

Based on documents and clarifications provided to us, subsequent to the issuance of the draft report, this finding has been removed.

/Finding No. 2

Fund reconciliation for PIL No. 4 and the LE portion of PIL No.7 was not prepared until the date we received STC's management response. Therefore, this finding will remain the same.

/Finding No. 3

The detailed accounting manual was not prepared until the date we received STC's management response. Therefore, this finding will remain the same.

Compliance with Regulations and Laws

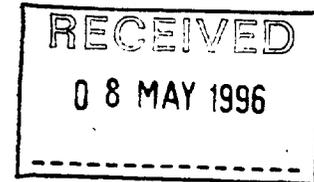
STC's management response did not address our finding on compliance with regulations and laws. Therefore, our position will remain the same.

APPENDIX III
MISSION'S COMMENTS



UNITED STATES AGENCY for INTERNATIONAL DEVELOPMENT

May 7, 1996

MEMORANDUM**TO:** Lou Mundy, RIG/A/C**FROM:** Shirley Hunter, OD/FM/FA **SUBJECT:** Financial Audit of the Science and Technology Cooperation, Expenditures Incurred Under the Scientific Research and Technology Cooperation Project (USAID/Egypt Project No. 263-0140). Draft Report dated March 27, 1996.

Following is the Mission's response to the draft report, including the actions taken by the Mission to resolve and close Recommendation No. 1 under the subject audit:

Recommendation No. 1:

We recommend that USAID/Egypt resolve questioned costs of \$834 (ineligible costs of \$564 and unsupported costs of \$270) detailed on pages 14 through 18 of the KPMG Hazem Hassan audit report, and recover from the Science and Technology Cooperation the amounts determined to be unallowable.

Mission Response:

Based on the Mission's review, of the \$834 questioned costs, \$321 is considered allowable, and \$513 is sustained. The amount sustained was refunded in the attached Voucher Nos. 92 dated 4/6/96, and 34 dated 5/6/96. Attached is a summary table showing the amounts allowed and amounts sustained. Accordingly, Mission requests closure of this recommendation.

Following are the details of the Mission's determination regarding the questioned costs:

PIL No. 4

2. Consultants:

b. The ineligible amount of \$45 (LE 150) page 14

* This amount represents the difference between the amount paid to a consultant and amount billed.

* STC has accepted this finding and has deducted the amount from voucher No. 92 for the month of April, 1996 (copy attached).

Therefore, Mission requests closure of this part of the recommendation.

4. Travel and Training:

a. The ineligible amount of \$51 (LE 173) page 15

* This amount represents an amount in excess of the USAID/Egypt's per diem rates for local travel.

* STC stated that this amount, although recorded in the ledger, was not billed to USAID. STC submitted a copy of the ledger as well as the billing for the same month (copies attached). FM/FA review has confirmed that the amount was never billed to USAID. Therefore, Mission believes that this amount is considered allowed. Attached is a copy of the ledger, the settlement, as well as the January 1993 billing.

Therefore, Mission requests closure of this part of the recommendation.

b. The ineligible amount of \$20 (LE 67) - page 15

* This amount represents taxes paid to a hotel.

* STC has accepted this finding and has deducted the amount from voucher No. 92 for the month of April, 1996 (copy attached).

Therefore, Mission requests closure of this part of the recommendation.

5. Special Studies:

c. The ineligible amount of \$73 (LE 246) - page 16

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- * This amount represents taxes paid to a hotel.
- * STC has accepted this finding and has deducted the amount from voucher No. 92 for the month of April, 1996 (copy attached).

Therefore, Mission requests closure of this part of the recommendation.

d. The ineligible amount of \$15 (LE 50) - page 16

- * This amount represents amount in excess of USAID/Egypt per diem rates.
- * STC has accepted this finding and has deducted the amount from voucher No. 92 for the month of April, 1996 (copy attached).

Therefore, Mission requests closure of this part of the recommendation.

PIL No. 7

1. Travel and Consultants:

c. The ineligible amount of \$360 - page 18

- * This amount represents taxes paid on air tickets.
- * STC has deducted this amount from voucher No. 34 for the month of April, 1996 (copy attached).

Therefore, Mission requests closure of this part of the recommendation.

d. The unsupported amount of \$270 - page 18

- * This amount represents unsupported lodging expenses for an investigator during his trip to the U.S.A.
- * STC has provided the following documents to support this expense, in lieu of the lodging receipts:
 - a. A certificate by the traveller stating the circumstances regarding the stolen documents,
 - b. A copy of the air ticket proving that the travel took place
 - c. The Project Director's approval of these expenses, taking into consideration its reasonableness and

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allocability in comparison to similar costs incurred by other travellers for the same destination.

Based on the above documents, Mission believes that the costs were actually incurred, are reasonable, and have served the Project purpose. Therefore, this amount is considered supported and Mission requests closure of this finding.

Attach. A/s

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