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**Audit of Local Expenditures
by Educational Innovation Systems
International, Inc. (EduSystems)
USAID/Egypt Project No. 263-0182
(Local Development II Program)**

**Audit Report No. 6-263-90-07-N
August 15, 1990**

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

August 15, 1990

MEMORANDUM FOR D/USAID/Egypt, Marshall D. Brown

FROM : RIG/A/C, F. A. Kalhammer *Kalhammer*

SUBJECT: Audit of Local Expenditures by Educational Innovation Systems International, Inc. (EduSystems) under USAID/Egypt Project No. 263-0182 (Local Development II Program)

The attached report, dated July 16, 1990, by Arthur Andersen & Co. presents the results of a financial audit of EduSystems' expenditures under USAID/Egypt's Local Development II project No. 263-0182. EduSystems assists the Government of Egypt in establishing vehicle and fixed plant maintenance systems in four governorates. EduSystems furnishes technical assistance in the design of management/financial systems, physical center specifications, and the erection of prefabricated buildings to house the maintenance centers.

We had Arthur Andersen & Co. make an audit of local expenditures totalling \$2.6 million for the period July 1, 1988 to December 31, 1989. Arthur Andersen & Co. concluded that, based on their tests, reimbursable costs reported as incurred by EduSystems were allowable, allocable and reasonable in accordance with the contract terms and other regulations.

Accordingly, there are no recommendations for your action.

I appreciate the courtesies extended to the staff of Arthur Andersen & Co. and our staff.

EDUCATIONAL INNOVATION SYSTEMS INTERNATIONAL, INC.
(EDUSYSTEMS)

FINANCIAL AND COMPLIANCE COST INCURRED
AUDIT UNDER USAID/EGYPT
PROJECT NO. 263-0182-C-00-9005-00

SHAWKI & CO.

Member Firm of Arthur Andersen & Co.

Members of the Egyptian Society of Accountants & Auditors

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Hala Rashed

Cairo, 16 July, 1990

Mr. F. A. Kalhammer
Office of the Inspector General
United States Agency for International Development
Mission to Egypt
Cairo Center Building
106, Kasr El Aini Street
Cairo - Egypt

Dear Sir,

We have completed the financial and compliance cost-incurred audit of EduSystems (Project no. 263 - 0182). Our audit covered local expenditures incurred by EduSystems from July 1, 1988 (inception) to December 31, 1989. Our audit was made in accordance with the requirements in the work order dated May 6, 1990.

Background

A cost plus fixed and award fee contract was signed between USAID and Educational Innovation Systems International Inc. on July 13, 1988. The total estimated cost inclusive of fee is US\$ 5,796,012 total.

The purpose of the contract is to provide, on a turnkey basis, to the Government of Egypt (GOE) a provincial governorate system for vehicle and fixed plant maintenance in four Egyptian governorates under the pilot maintenance centers component of USAID/Cairo's Local Development II Program (LD II). The four governorates are Qena, Assuit, Menoufia and Sharkia. The activity is divided into two principal parts:

- 1) Technical assistance which is the design of the system, including development of responsibilities for management-financial systems and specifications for physical centers together with appropriate equipment and training plans to assure competent staffing of the effort.

- 2) Supply and erection of a locally procured prefab building including all civil works to house the maintenance center, supply, installation of U.S. source and origin equipment and tools necessary for effective operation of the maintenance centers. The system includes the design and supply of facilities and associated equipment which includes installation of the managerial, financial and inventory systems required for the effective operation.

The pilot provincial maintenance center activity is a central component of an \$ 800 million Egyptian-American effort to increase the capacity of Egyptian local governments to meet the diverse demands for basic infrastructure and municipal services within their jurisdiction.

The pilot project activity is the first and most important, Government of Egypt-USAID initiative under the Local Development II Program to address the serious institutional, financial and technical issues that presently limit the ability of local governments to effectively maintain infrastructure, basic services and associated equipment.

The main function of the maintenance centers will be servicing of different types and sizes of service vehicles, earth moving construction equipment and fixed plants. The centers will have responsibility for providing all maintenance that is performed by the operators and user, up to and including second level maintenance (component exchange). Component repairs shall be done outside the centers through service contracts with suppliers/dealers of the equipment. One of the specific activities under this contract will be the design of model service contracts with equipment dealers including assisting participating governorates in developing and executing service contract arrangements with qualified dealers.

Objectives and scope of work performed

We have performed a financial and compliance cost-incurred audit of Educational Innovation Systems International, Inc. Contract No. 263-0182-C-00-9005-00 from July 1, 1988 (inception) to December 31, 1989. Our objectives were to determine whether:

1. the costs reported as incurred under the contract are in fact allowable, allocable and reasonable in accordance with the terms of the contract and OMB Circular No. A-122;
2. the internal control , accounting and management practices of EduSystems, Inc. are adequate for USAID/Egypt contracts;
3. EduSystems is in compliance with the contract terms.

The financial and compliance cost-incurred audit includes analytical review procedures, discussions with management and transaction testing considered necessary to assess the achievements of the objectives listed above.

The total value of items tested was as follows:

Expenditures tested	\$ 2,054,025	78%
Expenditures not tested	\$ 579,340	22%

Total expenditures as of December 1989	\$ 2,633,365	=====

Overview of the accounting and administration systems

The Organization structure of EduSystems is small in size. EduSystems employs five personnel responsible for monitoring the project activities. The accounting system is simple in nature and consists of:

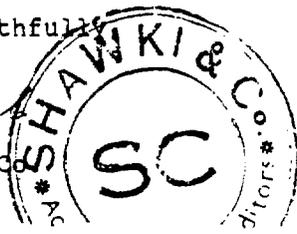
Three ledgers maintained by the company in the form of computer print-outs are the petty cash in L.E., bank account in L.E. and bank account in US Dollar. These ledgers are prepared monthly. EduSystems maintains a bank account in Hong Kong Bank in Egypt in Egyptian pounds and US Dollars. The chief of Party is authorized to sign cheques and approve all expenses.

Results of the audit

EduSystems has established appropriate procedures to ensure that expenditures are properly authorized and approved. Limited segregation of duties is achieved since there are few employees. Although EduSystems does not maintain written policies and procedures, the system of internal accounting controls is adequate. Two minor findings were noted during our examination. However, they do not modify the opinions expressed in our report. We have rendered clean opinions with regard to the statement of expenditures, compliance with grant agreement and applicable laws and regulations and internal control. This report is intended solely for the use of USAID in connection with the contract to EduSystems and may not be appropriate for any other purpose.

Yours faithfully

Shawki & Co.



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16 July, 1990

Regional Inspector General for Audit
USAID/Egypt
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Hala Rashed

We have performed a financial and compliance cost-incurred audit and examined the expenditure statement of Educational Innovation Systems International Inc. for the period from July 1, 1988 (inception) to December 31, 1989 relating to the United States Agency for International Development project No. 263-0182-C-00-9005-00. Our examination was made in accordance with generally accepted auditing standards and the standards for financial and compliance audits contained in the General Accounting office publication "Standards for Audits of Governmental Organizations, Programs, Activities and Functions" and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

We noted one weakness, which is discussed in finding 1.1. In our opinion, the expenditure statement of Educational Innovation Systems International Inc. for the period from July 1, 1988 (inception) to December 31, 1989 presents fairly the cost incurred relating to the project in conformity with generally accepted accounting principles.

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

Shawki & Co.

Shawki & Co.



Finding 1.1

Annual report of property in EduSystems' custody

The company does not comply with article 245-78 in the AID handbook 14 as it does not prepare an annual report of property in their custody.

Recommendation

We recommend that the company should comply with the instructions in the AID handbook 14.

Management comment

Management agreed with our comment.

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Rashad Hosny
Hala Rashed

16 July 1990

Regional Inspector General for Audit
USAID/Egypt
106, Kasr el Aini Street
Cairo - Egypt

We have performed a financial and compliance cost-incurred audit of Educational Innovation Systems International Inc. (EduSystems) for the period from July 1, 1988 (inception) to December 31, 1989 relating to the United States Agency for International Development project number 263-0182. Our examination was made in accordance with generally accepted auditing standards and the standards for financial and compliance audits contained in the General Accounting Office publication "Standards for Audits of Governmental Organizations, Programs, Activities and Functions" and other auditing procedures as we considered necessary in the circumstances.

The management of EduSystems is responsible for compliance with the terms of the above mentioned contract and applicable laws and regulations. In connection with our examination referred to above, we selected and tested transactions and records to determine EduSystems' compliance with agreement terms and applicable laws and regulations, non-compliance with which could have a material effect on the allowability of expenditures.

We noted one weakness, which is discussed in finding 2.1. In all other respects, the results of our tests indicate that for the transactions and records tested, EduSystems complied with those provisions of the contract and of laws and regulations, non-compliance with which could have had a material effect on the contract costs. Furthermore, for the items not tested, nothing came to our attention that caused us to believe that EduSystems was not in compliance with relevant laws and regulations.

Shawki &



Finding 2.1

Expatriates' salaries

Salaries paid to expatriates are not supported by payroll sheets or debit notes from the home office.

Recommendation

We recommend that supporting documents be filed in the Cairo office, e.g. copies of the transfer slips sent to these employees and the head office debit notes.

Management comment

Management agreed with our comment and has confirmed that payroll sheets will be communicated to Cairo office in the future.

STATEMENT OF EXPENDITURES
FROM JULY 1, 1988 (INCEPTION) TO DECEMBER 31, 1989

CLASSIFICATION	BUDGET U.S.\$	AMOUNT SINCE INCEPTION TILL DEC. 31, 1989 U.S.\$
Salaries & Wages	\$ 286,719	\$ 175,097
Fringe Benefits	83,559	51,271
Overhead	138,359	89,366
Consultants	33,430	4,924
Subcontracts	679,960	408,293
Buildings	2,075,104	413,249
Travel, Transport, and per diem	128,811	44,536
Other direct costs	266,176	250,212
	-----	-----
TOTAL	3,692,118	1,436,948
G & A @ 9%	332,291	129,325
	-----	-----
TOTAL COST	4,024,409	1,566,273
Fixed Fee	241,465	94,037
Award Fee	160,976	-
	-----	-----
TOTAL COST	4,426,850	1,660,310
Equipment	1,296,720	973,055
Spare parts	72,442	-
	-----	-----
TOTAL CONTRACT COST	<u>\$ 5,796,012</u>	<u>\$ 2,633,365</u>

The accompanying note is an integral part of this statement.

EDUCATIONAL INNOVATION SYSTEMS INTERNATIONAL INC.
(EDUSYSTEMS)

NOTE TO STATEMENT OF EXPENDITURES

Basis of presentation

The accompanying statement of expenditures has been prepared on the basis of cash disbursements; consequently, expenditures invoiced are recognized when submitted for payment rather than when the liability is incurred. Additionally, the statements have been prepared in accordance with the cost principles for expenditures reimbursable contracts set forth in "USAID Handbook 14" and the Federal Acquisition Regulation (FAR), which prescribes the nature of reimbursable expenditures not specifically defined in the contract.

Total costs invoiced by Educational Innovation Systems International Inc. (EduSystems) contract from July 1, 1988 inception to December 31, 1989 totaled \$ 2,633,365.

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16, July 1990

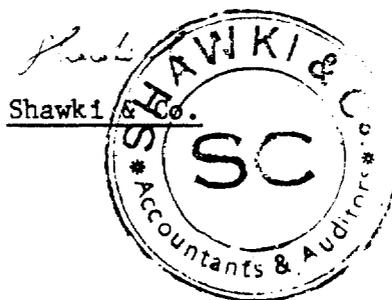
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We have made a study and evaluation of the system of internal accounting control of Educational Innovation Systems International Inc. (EduSystems) for the period from July 1, 1988 (inception) to December 31, 1989 relating to the United States Agency for International Development project No. 263-0182-C-00-9005-00. Our study and evaluation was conducted in accordance with standards established by the American Institute of Certified Public Accountants and the standards for financial and compliance audits contained in the General Accounting Office publication "Standards for Audits of Governmental Organizations, Programs, Activities and Functions" and other auditing procedures as we considered necessary in the circumstances.

The management of EduSystems is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgements by the management are required to assess the expected benefits and related costs of control procedures. The objectives of the system are to provide the management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with the procedures may deteriorate.

In our opinion, the system of internal accounting control of EduSystems in effect for the period from July 1, 1988 (inception) to December 31, 1989, taken as a whole, was sufficient to meet the objectives stated above insofar as those objectives pertain to the prevention of errors or irregularities in amounts that would be material in relation to contract costs.



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APPENDIX II

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