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BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Administrator Agency For International Development

AID Needs To Strengthen Management Of Commodity Import Programs

AID spends half a billion dollars a year to provide developing countries with the dollars needed to import essential commodities. Local currencies generated from the sale of these commodities also are made available to the recipient governments for developmental purposes. AID's planning, monitoring, and evaluation of the program should be improved and controls over commodity expenditures strengthened.

GAO recommends specific actions to improve management of commodity import programs, including additional guidance for planning and evaluating these programs and monitoring their implementation.

GAO/NSIAD-84-47
FEBRUARY 29, 1984

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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

NATIONAL SECURITY AND
INTERNATIONAL AFFAIRS DIVISION

B-213871

The Honorable M. Peter McPherson
Administrator, Agency for
International Development

Dear Mr. McPherson:

This report presents the results of our review of the management of AID's commodity import programs (CIPs). It suggests ways to strengthen the planning and evaluation of these programs and to improve the monitoring of CIP implementation and internal controls over payments for commodities.

We initiated this review to evaluate the Agency's programmatic and financial controls over a program that amounts to more than half a billion dollars a year. AID officials' responses indicate that positive actions are to be taken on our recommendations. (See the app.)

The report contains recommendations to you on pages 9, 19, 32, 39, 40, and 43. As you know, 31 U.S.C. §720 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the Agency's first request for appropriations made more than 60 days after the date of the report. We would appreciate receiving copies of your statements to the committees.

We are sending copies of the report to the Chairmen of the four above committees; interested House and Senate authorization committees; and the Director, Office of Management and Budget.

Sincerely yours,

Frank C. Conahan

Frank C. Conahan
Director

GENERAL ACCOUNTING OFFICE REPORT TO THE ADMINISTRATOR, AGENCY FOR INTERNATIONAL DEVELOPMENT

AID NEEDS TO STRENGTHEN MANAGEMENT OF COMMODITY IMPORT PROGRAMS

D I G E S T

The Agency for International Development (AID) spends half a billion dollars a year for the Commodity Import Program (CIP). This program provides less developed countries with (1) dollar exchange to import various commodities to help meet resource shortfalls and (2) local currency from the sale of these commodities.

The current program supplies U.S. commodities that assist primarily agricultural and industrial development--fertilizers, farm machinery, industrial equipment, transportation facilities, raw materials, and spare parts. AID is responsible for planning and evaluating the program and monitoring its implementation.

GAO initiated this study to evaluate the extent of AID's program and financial controls over the CIP and to respond to the growing congressional interest regarding the size and management of CIP. GAO reviewed five of the nine countries receiving CIP assistance in fiscal year 1982.

NEED FOR BETTER PLANNING OF COMMODITY DELIVERY

AID has not always adequately planned procurements and deliveries of the commodities. In some instances, commodities arrived too late and at increased cost. For example, in one country, fertilizer did not arrive in time for the intended planting season 2 years in a row and had to be stored at the port. This cost the host government nearly $500,000 in scarce foreign exchange. (See ch. 2.)

GAO recommends that AID establish procedures requiring more specific pre-implementation CIP planning which would include implementation schedules and would provide for modifying plans when established milestones can no longer be reasonably met. (See p. 9.)

OPPORTUNITIES TO IMPROVE INTERNAL CONTROLS

Although the law and regulations prescribe that AID-financed commodities must meet eligibility and price requirements, AID has not always used adequate internal controls to assure compliance. Insufficient reviews of commodity transactions have contributed to waste and improper expenditures that could amount to millions of dollars annually. In one case, AID deviated from established procedures and reimbursed $25 million to a recipient country before ascertaining whether the commodities qualified for AID financing. It took AID 1 year to obtain proper documentation. AID needs to strengthen its internal controls and auditing to lessen the risk of paying for unauthorized and excessively priced commodities. (See ch. 3.)

GAO recommends actions to improve internal controls, including increasing audit coverage and studying the need to transfer the voucher audit function from the Office of Commodity Management. (See p. 19.)

NEED TO STRENGTHEN MONITORING OF COMMODITIES AND LOCAL CURRENCY PROCEEDS

AID does not adequately monitor the implementation of commodity import programs and local currency generation and use. AID missions had not conducted or documented required evaluations of the host-government commodity arrival accounting systems nor systematically followed up on the distribution and end-use of commodities. As a result, AID cannot adequately account for the arrival and disposition of commodities. This occurs because missions do not have sufficient staff and guidance on monitoring CIP implementation. (See ch. 4.)

GAO recommends that AID issue specific guidance to AID missions on monitoring the implementation of commodity import programs, including the arrival accounting and disposition of commodities. (See p. 32.)

Also, AID missions are not effectively monitoring the proceeds from commodity sales. As a result, they do not know the amounts to be generated and deposited into special accounts or whether the proceeds are used for agreed upon purposes. In establishing guidance to the missions, AID needs to answer several basic questions dealing with local currency, such as which CIP transactions should generate local currency and how the proceeds should be used. (See ch. 5.)

GAO recommends that AID issue guidelines on the accounting for the generation of local currency proceeds resulting from the sale of AID-financed commodities and on monitoring the use of such proceeds. (See pp. 39 and 40.)

AID DOES NOT REQUIRE EVALUATION OF THE COMMODITY IMPORT PROGRAM

Despite legislative mandate to improve the assessment of AID programs, AID has not developed procedures for evaluating CIP assistance. As a result, AID does not have information on program performance which is needed for designing future programs. (See ch. 6.)

GAO recommends that AID require that CIP assistance be systematically evaluated and develop specific guidance to those performing such evaluations. (See p. 43.)

AGENCY COMMENTS

AID agreed with GAO recommendations for better planning of CIPs and improved monitoring of commodity arrival accounting and end use, as well as local currency generation and programming. AID also agreed to improve evaluation of CIPs and increase effectiveness of internal controls over payment for commodities. Some action is already underway or is being planned; the Agency is to issue appropriate guidance to personnel involved in these activities, but target dates have not been established. (See appendix.)

AID officials did not concur with the GAO proposed recommendation for transferring the commodity voucher review function from its present location but agreed that a further study of this matter has merit. GAO concurs with AID's suggestion and has modified the recommendation accordingly.

Also, AID commented that the narrative section of the report describing deviations from established procedures in reimbursing $25 million to a recipient country did not support a recommendation that appropriate controls are needed to prevent such deviations in the future. GAO believes additional controls are necessary because AID authorized the initial review of documents without determining whether mission personnel have the expertise to carry out these tasks and did not provide timely support and guidance.

AID provided detailed comments on specific issues discussed in the report. GAO considered these comments and revised the report as appropriate.

Contents

ABBREVIATIONS

AID	Agency for International Development
CIP	Commodity Import Program
GAO	General Accounting Office

CHAPTER 1

INTRODUCTION

Commodities are a fundamental element of the U.S. economic assistance program administered by the Agency for International Development (AID). Commodity Import Programs (CIPs) are financed under the Economic Support Fund authorized under the Foreign Assistance Act of 1961, as amended. Of nearly $2.8 billion available for the Support Fund in fiscal year 1982, about $548 million was allocated for CIPs in the following countries: Egypt, $300 million; Sudan, $100 million; Pakistan, $60 million; Zimbabwe, $50 million; Zambia, $15 million; Somalia, $15 million; Kenya, $4 million; Mauritius, $2 million; and Seychelles, $2 million.

The Commodity Import Program provides dollar exchange to less developed countries for the import of specified categories of commodities under grant or loan agreements to meet shortfalls in the external resources of these countries. Also, the law provides that local currencies generated from the sale of certain commodities be made available for use by the United States and the recipient government for mutually agreed upon purposes. In recent years, public sector enterprises and organizations have become increasingly important recipients of CIP resources.

CIP funds have been used to supply material for reconstruction and rehabilitation of plants and transportation facilities and purchases of various agriculture commodities and industrial equipment, such as tractors, buses, utility vehicles, and generators. CIP financing has also supplied raw materials, fertilizer, spare parts, and irrigation equipment as well as training, technical assistance, and other commodity-related services. Almost all CIP imports come from the United States.

THE PROCESS OF CIP ASSISTANCE

The legislative authority for the CIP is section 531 of the Foreign Assistance Act (22 U.S.C. §2346). Other sections of the act contain specific CIP program requirements. Among the key ones are section 604(f), which requires certification and AID approval of commodity eligibility prior to the disbursement of funds, and section 609, which requires that local currency proceeds resulting from the sale of grant-funded commodities be deposited in a special account. In addition, section 125 directs AID to improve its evaluation performance.

Policies, regulations, and guidelines for the CIP are formulated by AID offices and bureaus in Washington. Briefly, AID is responsible for planning the program, monitoring its implementation, and evaluating its management and impact.

The CIP process begins with a determination, often based on urgent or emergency reasons, that a relatively fast transfer of resources is necessary to close serious foreign exchange gaps and to meet security or other objectives in which the United States has a special interest. Requests for CIPs are generally initiated at AID overseas missions. The missions are responsible for the overall program design, including implementation planning. The process results in the preparation of the Program Assistance Approval Document. The responsibilities of AID and other participants and a plan for implementation are included in the document. The document undergoes review by the responsible geographic bureau before approval.

It is AID policy that, to the extent possible, the countries it assists should undertake the implementation of their assistance programs. AID policy for CIPs is that, where possible, the host country rather than AID should procure program commodities. AID retains the responsibility, however, for monitoring the implementation process.

After approval of the planning document, a Commodity Import Agreement is signed by AID and the host country, signaling the formal start of CIP implementation. The agreement establishes the framework of rules for implementing the CIP and describes the terms and conditions under which assistance will be provided. Its basic provisions describe the applicable commodity financing procedures, method of financing, deposit and use of local currencies generated, and maintenance of records, inspection procedures, remedies, and rights. Additional guidance is provided through implementation letters and procurement instructions. It is intended that the program should be evaluated periodically against stated objectives.

The basic responsibilities for monitoring the program are within AID's Bureau for Management, Directorate for Program Management Services, Office of Commodity Management, which assists in the planning and procurement of commodities, approves commodity procurement transactions, and conducts pre- and post-audits of suppliers' vouchers for compliance with statutory and AID requirements. The Bureau's Office of Financial Management is responsible for clearing availability of funds, issuing letters of commitment, maintaining official accounting records and reports, and making payments.

OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of our review was to evaluate AID's programmatic and financial controls over CIP activities. Accordingly, we examined whether AID adequately

--plans the implementation of CIP assistance;

--monitors, during implementation, the commodity arrival and accounting, distribution and end use, local currency generation and programming, and compliance with statutory and AID requirements; and

--evaluates the management and impact of CIPs.

The review was conducted in accordance with generally accepted government audit standards. Our review focused on the management of CIPs during fiscal years 1980, 1981, and 1982. The work was performed at AID headquarters in Washington, D.C., and in selected developing countries receiving CIP assistance--Egypt, Kenya, Sudan, Zambia, and Zimbabwe. These countries were chosen to provide a balanced mix of ongoing and new programs from the standpoint of cost and types of commodities provided. In-country work was performed between January and March 1983 and audit work in Washington was completed in May 1983.

We examined AID's policies and procedures for planning, monitoring, and evaluating CIP assistance; studied AID's Inspector General reports describing problems in providing this assistance to Egypt; and reviewed program records and files in Washington and at five missions. We interviewed AID Washington officials in the Bureaus for Management, Program and Policy Coordination, Africa, and Near East; and Offices of the Inspector General and General Counsel. At the missions, we interviewed AID and host-country officials dealing with CIP activities and visited selected port and commodity storage facilities.

The methodology used in analyzing AID's performance in planning, evaluating, and monitoring CIP activities and compliance with requirements included the following procedures.

--Examining AID policies and procedures for managing CIP.

--Examining, in the five countries, selected CIPs funded with fiscal year 1981 and 1982 appropriations.

--Examining selected fiscal year 1979, 1980, 1981, and 1982 planning documents for adequacy of AID's planning of these commodity programs.

--Following up on selected Inspector General recommendations made in 1980 and 1981 concerning Egypt's CIP activities.

--Identifying problems and determining their causes.

--Determining what AID should have done to improve the planning, evaluation, and monitoring of CIP activities.

--Assessing corrective action that should be taken to help avoid the problems found.

CHAPTER 2

BETTER PLANNING FOR COMMODITY IMPORT

PROGRAM ACTIVITIES NEEDED

Although AID procedures for planning CIP assistance outline principal implementation steps, specific planning and delivery schedules are seldom adjusted to meet changing conditions. As a result, program objectives were not achieved when, in some cases, commodities arrived too late and at increased cost. We believe pre-implementation planning procedures are needed to assure that CIP assistance provides maximum benefits to the developing countries.

INADEQUATE IMPLEMENTATION PLANNING DELAYS DELIVERY AND INCREASES COST OF NEEDED COMMODITIES

Although AID planning documents described program design and justification in detail, they often did not sufficiently develop such practical elements as flexible scheduling or solutions to previous problems. These shortcomings resulted in hundreds of thousands of dollars in lost commodity resources.

Documents reviewed for 10 commodity import programs in 4 countries contained considerable detail on the general design and analysis justifying the authorization of these programs and included milestones for procurement, shipping, and distribution of the commodities and generation of local currencies. The documents for three of the countries, however, did not include realistic estimates of the time needed for advertising the procurement of commodities, awarding the contracts, shipping the commodities to the port of entry, transporting them from the port to the distribution points in the recipient country, or selling the commodities with the aim of generating local currencies.

Also, the planning documents did not adequately reflect consideration of past performance in providing CIP assistance to the country. Although problems with implementing previous years' programs were discussed, the documents did not always include proposed solutions to these problems.

Commodity shipment experiences for Zambia and Sudan over several fiscal years are discussed below. They illustrate program inefficiencies and waste resulting from inadequate implementation planning.

Zambia

Schedule slippages of several months resulted in AID-financed fertilizers not arriving in Zambia in time to be used during the intended growing season. This inadequate planning cost the host government a total of nearly half a million dollars in avoidable foreign exchange outlays in fiscal years 1981 and 1982. We do not know how this affected the food production in Zambia.

Despite serious delays in meeting important program milestones, AID did not revise original implementation schedules for fiscal years 1981 and 1982. For example, invitations for bids were issued 5 and 7 months later than planned during their respective fiscal years. Although both years' programs were designed to provide fertilizer for a particular planting season, the delays in procurement prevented the fertilizers from arriving so they could be used when intended.

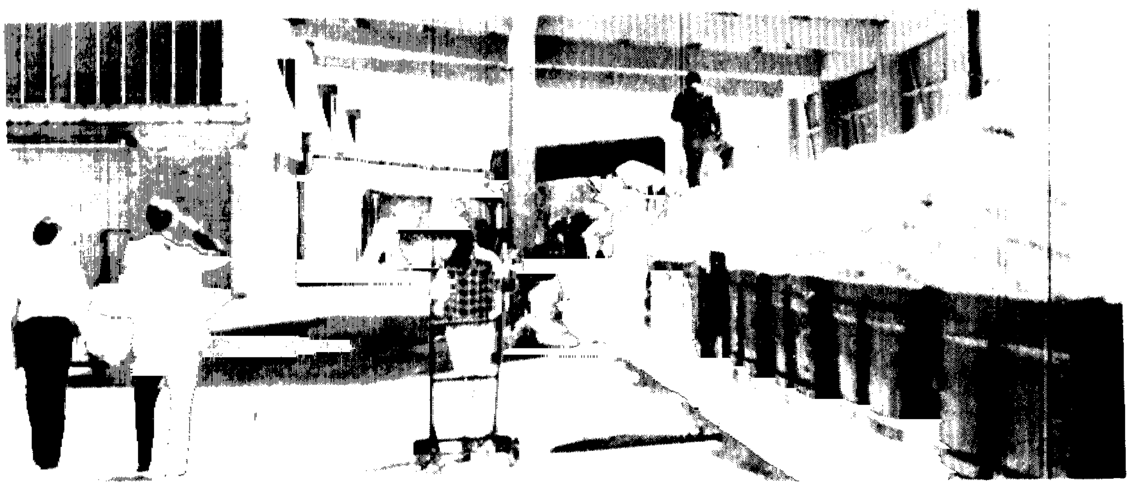
Also, the right type of fertilizer did not arrive in Zambia at the time it was needed. We were told in January 1983 that shipments of urea, the fertilizer desperately needed by the end of February, had been slow. Instead, compound R, fertilizer used for the October planting season, arrived and had to be stored for the next year.

Although planning documents discussed factors that could affect movement of commodities, such as the transportation problems of moving cargo from the ocean port to Zambia and timing of shipments, no solutions were proposed. For example, in the fiscal years 1980 and 1981 documents, AID's analysis showed that commodities did not reach Zambia timely because the country's scarce inland transportation resources were devoted to higher priority items. However, the fiscal year 1981 document did not discuss proposed action for better timing of commodity shipments and expeditious movement to distribution points in Zambia.

The three ships carrying the 1982 shipment of AID-financed fertilizer arrived at the South African port within a 5-week time period. Zambian government representatives told us that shipping the entire supply of fertilizer to arrive in such a short time causes serious problems in transportation due to the limited availability of railroad cars. They would prefer to see shipments evenly spaced throughout the year as long as the right type of fertilizer is received when needed.

The freight forwarder at the South African port of entry also told us that several ships bringing in fertilizer in a short time frame cause port congestion and the need to store these commodities at the port. The result is additional cost to the host government. For the fiscal year 1981 loan, at least $209,000 was paid to the freight forwarder for storing the fertilizer compounds at the port warehouse while awaiting transportation. For the fiscal year 1982 loan, about $284,000 in additional charges was incurred for storing the fertilizer at the port because sufficient funds for inland transportation were not provided. Thus, for these 2 years, the additional cost was about $500,000.

Zambian workers in Lusaka bag yellow corn supplied by the United States to help Zambia avert recent food crisis. CIP-financed fertilizer shipments are intended to increase the country's food production. (Photo-courtesy of AID.)



Loading AID-financed fertilizer into railcars at a port warehouse in East London, Republic of South Africa, for transshipment to Zambia. January 1983. (Photo by GAO staff.)

The fiscal year 1981 planning document described inland transportation bottlenecks but did not acknowledge that procurement and shipping of the raw materials could or should be spaced over a time period. Instead, the document predicted that fewer difficulties in transportation were expected than in past years.

Another planning deficiency was that not enough of the fiscal year 1982 loan was set aside for inland transportation. The planning document shows that AID was aware that the government's implementing agency had a poor record of obtaining foreign exchange for financing inland transportation. Yet there was a $1-million shortfall in covering the estimated cost of inland transportation. As stated above, this caused costly delays in transporting fertilizer from the port to Zambia.

AID/Zambia officials acknowledged that better planning for CIPs is needed to overcome these problems. The delays in moving commodities from the port to the final destination in this landlocked country could be minimized by providing adequate lead time and better coordination among the host government entities, freight forwarders, and AID.

Sudan

In Sudan, planning was not modified on the basis of known implementation problems--heavy congestion and large import backlogs at Port Sudan, the country's principal port, and the lack of transportation to move goods from the port to points inland. Despite these problems, AID planning provided that existing government cargo agents would clear all CIP imports through customs in the required 90-day time and that all AID-financed commodities would be used within a 12-month period. As discussed in chapter 4, these standards were not always met. This resulted in commodities reaching intended users late and required storage at port warehouses where the commodities were subjected to pilferage.

Also, despite the fact that neither the AID mission nor the Sudanese government had the necessary staff to monitor the arrival and accounting of commodities or to expedite inland transportation, AID planning provided that the mission would expedite the movement of cargo and carry out inspection and evaluation with available staffing, instead of securing outside assistance for performing these tasks.

CONCLUSIONS AND RECOMMENDATION

AID has not always adequately considered available information gained from past CIP performance and information obtained during the planning process. In most instances, the planning, as reflected in the planning documents and implementation letters, showed very little correlation in the scheduling and timing of commodity acquisition with the needs of the recipient country. Many of the plans were inflexible in that they did not provide alternatives for such variables as schedule delays or transportation problems. Instead, CIP planning documents focused primarily on synthesizing information to justify the authorization of the program and often did not address efficient and realistic delivery of this assistance.

Because planning is a dynamic, continuous process which can influence program results, AID needs a specific implementation plan of action to assure that CIP commodities are purchased, delivered, and used efficiently and effectively. Although AID regulations do not require such detailed implementation planning, in our view the planning documents should provide certain pre-implementation steps which can be monitored and verified so that plans can be amended to reflect a current assessment of the import environment. This would give AID greater assurance that the CIP will be properly implemented.

Accordingly, we recommend that the AID Administrator establish procedures requiring more specific pre-implementation CIP planning which would include realistic, time-phased implementation schedules and would provide for modifying plans when established milestones can no longer be reasonably met.

AGENCY COMMENTS AND OUR EVALUATION

AID agreed in principle with our recommendation but did not indicate what specific action would be taken. The response dealt exclusively with the commodity import program in Zambia.

The Agency provided us with a recent study on Zambia's fertilizer supply and distribution issues which addressed many of the problems discussed in our report. AID believes that, as a result of this study, the Zambian government now recognizes its own constraints that have adversely affected the planning of procurement and shipment of fertilizer. Also, AID stated that it plans to reinforce its efforts to prevail upon the government of Zambia to set aside sufficient loan funds for inland transportation.

AID questioned statements that an entire year's supply of AID-financed fertilizer was shipped at one time and said that shipments to Zambia usually move over at least a 2-month period in full shiploads. According to Zambian officials and the freight forwarder, the problem has been with several ships arriving at the port in a short time frame, as stated on page 6.

Some of AID's comments relate to monitoring the Zambia CIP. These matters are described in chapter 4 of our report. We have, where appropriate, revised the language in that chapter to reflect the Agency's position.

CHAPTER 3

INADEQUATE INTERNAL CONTROLS OVER COMMODITY TRANSACTIONS

LEAD TO WASTE AND IMPROPER EXPENDITURES

Although the law and regulations require that AID-financed commodities meet prescribed eligibility and price rules, AID has not used adequate checks and controls to assure compliance with these requirements. Although AID has recovered substantial sums (over $2 million annually) from reviews of commodity transactions, it may be paying millions of dollars more for ineligible and overpriced commodities and related services. In one case, AID reimbursed a developing country for $25 million in commodity purchases without assuring that these commodities qualified for AID financing. To lessen the risk of paying for unauthorized and excessively priced commodities, AID needs to strengthen its internal controls by reviewing more commodity transactions, clearly communicating AID requirements to commodity suppliers, and following regulations.

INSUFFICIENT REVIEWS CONTRIBUTE TO IMPROPER PAYMENTS

Although AID has procedures and controls for assuring that commodity transactions meet statutory, regulatory, and contractual requirements, they are not applied to a sufficient number of transactions to adequately protect U.S. government interests. This occurs despite evidence that suppliers' requests for payment often include errors and ineligible items.

The statutory requirements for commodity eligibility and price limitations stem from section 604 of the Foreign Assistance Act of 1961, as amended. AID implements these requirements through use of AID Regulation 1 (22 C.F.R. pt. 201 (1983)) which requires suppliers to furnish AID with certain documents attesting to commodity eligibility and price.

Reviewing the required documentation and suppliers' vouchers for commodity transactions is one of AID's principal controls in verifying that commodities, insurance, freight, and commissions comply with applicable regulations. This review is performed, primarily in AID's Office of Commodity Management, either before or after payment to suppliers.

Under the direct letter of commitment method, the Surveillance and Evaluation Division reviews all commodity vouchers and supporting documentation. If no irregularities are found, payment is approved. Under the bank letter of commitment method, the supplier is paid by the designated bank in accordance with instructions from AID. The bank then receives reimbursement from AID. Under this method, transactions are subject to review by AID after payment is made, and post audit of vouchers is made on a test basis only. In contrast, the direct letter of commitment method permits AID to review the documentation for compliance with statutory and AID regulations before making payment.

<u>Commodity transactions are vulnerable to waste, loss, and unauthorized expenditures</u>

Although the Surveillance and Evaluation Division reviews all commodity vouchers under direct letters of commitment, AID estimates that only about 12 percent of all commodity vouchers are reviewed. On the basis of the dollar value, the percentage of transactions reviewed is greater, but is not accurately known. As a result of these voucher reviews, the division has taken exception to a number of payments requested by suppliers and has recovered or not approved payments of over $2 million annually during the past several years.

For example, in 1982, the division's review of 810 transactions worth $252 million under direct letters of commitment covering CIP commodity billings revealed that $1.8 million (0.7 percent) did not qualify for AID financing. This amount was deducted from vouchers prior to payment.

Also in 1982, the division reviewed on a post-audit basis about 90 commodity transactions under bank letters of commitment and issued 22 bills of collection for $416,000. We could not establish an error rate, however, because AID does not record the dollar value of bank letter of commitment transactions reviewed. Actual recoveries amounted to $500,000, including recoveries from previous years. Thus, the total amount recovered or not approved for payment in 1982 was $2.3 million. These funds were restored to the appropriate loan and grant accounts for further use.

These deductions and recoveries were made for ineligible commodities, freight charges, fees, taxes, and commissions as well as for commodity overpricing and clerical errors. Particularly susceptible to errors are commodity ocean freight transactions, which amount to an estimated $100 million annually, and transactions under bank letters of commitment. In fiscal year 1982, AID certifying officers reported processing over $1.6 billion in bank letter of commitment vouchers. According to AID's 1982 assessment of vulnerability, about $1 billion was for commodities and related services.

More audit coverage could result in bigger savings

The large sums involved in commodity payments make strong internal controls essential to prevent substantial loss through inappropriate or erroneous payment. Questions have been raised in the past by GAO and AID's Inspector General regarding adequacy of internal controls over commodity payments. For example, in our June 2, 1982, report to the AID Administrator,[1] we brought to AID's attention a number of issues involving weak internal controls and accountability for host-country contracting activities.

AID has acknowledged the vulnerability of CIP to waste, fraud, and mismanagement in its assessment of internal controls made in December 1982 to satisfy the requirements of Office of Management and Budget Circular A-123. Without adequate internal controls, there is potential for improper expenditures due to errors, mismanagement, and noncompliance with regulations. Available evidence indicates that improper billings can reach millions of dollars annually.

For example, in addition to the $2 million in actual deductions and recoveries achieved annually during the past few years, an AID contractor performing post-audits of commodity payments had identified questionable payments of over $1 million in the first 10 months of this contract. Also, AID's Inspector General has reported improper payments of millions of dollars and pointed to other potential savings through elimination of bank charges.

AID did not have an estimate for further potential savings through increased audit coverage of commodity transactions and improved internal controls. AID officials told us, however, that several million dollars in additional improper billings are possible and that an increased level of audit coverage is likely to result in bigger savings.

AID actions to increase audit coverage

AID has recognized the need to improve voucher audit coverage. In 1979, AID's Inspector General recommended that Surveillance and Evaluation staff be augmented to implement that division's responsibilities, particularly to increase the number of transactions audited. Subsequent staff increase, however, eroded over the past years; by April 1983, the division had no more staff than it had in 1979 and efforts to add personnel were not successful.

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[1] Managing Host Country Contracting Activities (GAO/ID-82-42).

To achieve greater efficiency and expanded coverage in the voucher audit process within tight direct-hire personnel limits, the AID contract referred to earlier was entered into in November 1982 with a private firm to review a number of commodity voucher transactions financed under CIPs and project activities. This contract is expected to be cost effective, recovering more than the contract cost.

AID officials believe that by increasing the number of personnel performing voucher reviews, the Agency could identify more improper payments. During 1982, on the average, each voucher specialist in the Surveillance and Evaluation division was able to identify over $450,000 in savings, whereas an additional specialist would increase the cost to AID by about $45,000. On this basis, some AID officials believe it would be cost effective to increase the number of division staff.

AID's Inspector General believes that significant potential exists for further savings from commodity voucher audits and has suggested that AID increase the voucher audit coverage by its contractor and direct-hire staff in recognition of the fact that most bank letter of commitment transactions are not audited. In a May 1983 report, the Inspector General noted that AID has no effective system for auditing bank letter of commitment vouchers to assure that payments are proper. The prepayment review of the AID certifying officer in New York is limited to a quick check of documents and is made under great time pressure.

$25 MILLION PAID FOR COMMODITIES WITHOUT ASSURANCE OF ELIGIBILITY

Before reimbursement is made for purchases previously financed with the host-country's foreign exchange, AID must ascertain the eligibility of such commodities. Despite this requirement, AID reimbursed the government of Sudan $25 million for commodities which did not qualify for AID financing because it did not follow established procedures for reviewing supporting documentation before disbursing funds. It took AID 1 year after payment to obtain additional documents showing purchases of qualified commodities. The following discussion describes how inadequate review procedures resulted in AID's improper payment to Sudan.

During the first half of 1982, AID considered several options for quickly disbursing to the Sudan government $25 million of the $100 million CIP grant authorized for fiscal year 1982. The fastest disbursement method was being sought to meet the urgent need for funds to alleviate the country's balance-of-payments problems. Cash transfer--the fastest disbursing method--was not used. In March 1982, AID instructed the mission to identify eligible commodities that would qualify for direct reimbursement. This method permits reimbursement to a country for eligible transactions previously financed with the country's own foreign exchange and gives AID analysts an opportunity to fully review the transaction before AID funds are disbursed to assure that commodities meet the eligibility criteria prescribed by regulation pursuant to section 604(f) of the Foreign Assistance Act, as amended.

AID procedures make it clear that under the reimbursement method it is customary to perform a full review of supporting documents before reimbursement, with particular attention to eligibility of commodities, so that the grantee has an opportunity to substitute acceptable transactions for ones found defective. An AID handbook cautions that it is in the interest of all concerned to detect ineligible transactions before AID funds are paid out to avoid the necessity of filing refund claims.

In addition to these procedures, disbursements of AID funds are subject to financial controls which apply generally to U.S. government expenditures, such as measures to assure AID certifying officers that there has been a valid obligation of funds and that established internal controls have been observed to prevent duplicate or improper payments.

<u>Inadequate review of documents used as a basis for authorizing reimbursement</u>

Instead of performing the review of supporting documents in Washington where qualified AID commodity specialists were available, AID directed its mission in Sudan to review documents submitted by the host government. Mission personnel generally not familiar with such tasks made this review and did not recognize that none of the transactions qualified for AID financing.

In July 1982, AID advised the mission that it was prepared to reimburse the Sudan government for eligible transactions subject to the mission's certification that the documentation fully complied with AID rules.

In a July 20, 1982, cable, the mission stated that it had reviewed documentation for transactions in an amount in excess of $35 million. The mission certified that all such transactions met the requirements specified by headquarters: that is, they took place after October 1, 1981; involved only commodities, transportation costs, and other acceptable services eligible for financing under the subject grant; and the Sudanese government had certified that none of these transactions was financed by funds provided by an agency of the U.S. government. On the basis of this certification, a direct reimbursement authorization for $25 million was issued on July 23, 1982, and credited to the Bank of Sudan account in the Federal Reserve Bank of New York.

In directing the mission to review the supporting documents, AID deviated from its procedures. Moreover, it did not provide appropriate instructions on how this review was to be made or what documents had to be available to satisfy AID requirements for direct reimbursement. Although considerable correspondence was exchanged between headquarters and the mission in the months preceding the disbursement, there was no evidence that guidance was furnished to the mission.

AID officials said that direct reimbursement procedures were not followed because pre-disbursement review of documents was performed in the field rather than at headquarters. They believed that this delegation to the mission was acceptable at the time for several reasons. First, Sudan's inability to meet important multilateral financial commitments required prompt action by the United States. Second, they believed the mission had sufficient staff to handle the work. Finally, documentation supporting disbursements far in excess of $25 million was believed to be available.

As required, the mission sent all documentation reviewed to AID headquarters in July 1982 for further detailed review, as was customary when the direct reimbursement method of financing is used. In August 1982, AID determined that the documents were deficient and did not support the $25-million reimbursement. Cited reasons for documents not meeting the statutory and AID requirements included:

--Shipments were made on ineligible flag vessels.

--Contracts were subject to restrictive trade practice certifications, making the entire transaction ineligible for AID financing.

--Letters of credit were unsigned and not supported by bills of lading or carrier invoices.

Although AID determined that transactions were ineligible or that information for review purposes was incomplete, it did not notify the mission of this fact until October 1982. AID advised the mission that some transactions could be made eligible if the mission could obtain additional and legible documentation needed for determining eligibility and for obtaining necessary waivers.

From October 1982 to the time of our visit in March 1983, the mission had taken no further action to resolve the matter. Mission personnel who reviewed and certified the documents in

July 1982 had been transferred and no one at the mission could tell us why the review had not been more thorough. As a result of our inquiries, the mission's acting director told us that the matter would be given priority attention.

Also, AID headquarters was slow to take action on the improper payment. Despite regulations that authorize AID to initiate refund claims against the grantee when AID finds that funds were disbursed for ineligible transactions, the Office of Financial Management did not follow up on documents it had agreed to review until 3 months after disbursement. Moreover, having been informed in November 1982 that the documents did not support a direct reimbursement transaction, AID took no action to remedy the situation until we questioned the improper disbursement of $25 million in March 1983. Only in April 1983 did headquarters officials advise the mission that unless documentation for eligible transactions was received in a reasonable time period, it would be necessary to prepare a bill of collection to the government.

In July 1983, AID obtained documentation to substantiate the $25-million reimbursement to the government of Sudan. The documents consist of $9 million in freight payments for shipping grain products to Sudan, not included in the original submission, and $16 million worth of crude oil transported from Egypt to Sudan on foreign flag vessels. AID considers the crude oil purchases eligible for reimbursement on the basis of a retroactive determination that U.S. flag tankers were not available for these shipments.

CHANGES IN PROCEDURES COULD FURTHER IMPROVE INTERNAL CONTROLS

Although over the past few years AID has acted to review more commodity payment vouchers, procedural weaknesses preclude effective internal control over CIP transactions. Specifically, inappropriate placement of the voucher audit function and unclear communication of AID regulations to commodity suppliers weaken AID's ability to control the propriety of transactions.

The voucher audit function should be outside the Office of Commodity Management

The placement of the voucher audit function in AID's Office of Commodity Management conflicts with the generally accepted internal control standard of separation of duties. This standard requires that no one individual or separate entity controls all phases of an activity or transaction, which would create a situation that permits errors or irregularities to go undetected. In the Office of Commodity Management, however, the director controls the pre-procurement actions, actual procurement payment authorization, and review actions. Findings of overpricing and errors discovered in voucher reviews by the Office's Surveillance and Evaluation Division reflect unfavorably on the effectiveness of other functional units within the office. This can be embarrassing to the organization as a whole and does not foster the maintenance of a positive and supportive management attitude toward internal control.

The payment voucher audit function has been in the Office of Commodity Management since 1973. In a 1978 review of commodity procurement, AID's Inspector General concluded that in this office the function lacked the necessary degree of independence to be effective. The Inspector General repeated the same conclusion in 1979 but did not recommend that the voucher audit be established as an independent function because it was considered to be impractical and not cost effective. The Inspector General concluded, however, that the voucher audit function should be made more independent of other functions within the Office of Commodity Management.

AID's Office of the General Counsel has also commented on the commodity price review function, which is performed by the Surveillance and Evaluation Division. In 1981, the Office informed the Office of Commodity Management that AID should consider integrating the commodity price review and payment functions, the latter of which is now handled by the Banking and Finance Division.

On the basis of our review, we concur with the views of the Inspector General and General Counsel regarding the need to seek a different location for the voucher audit and price review function. Locating this function in the same organizational unit as the pre-procurement and actual procurement functions, contrary to the separation of duties standard, makes the internal control system vulnerable to procedural weaknesses. AID has considerable flexibility within the Bureau for Management to appropriately segregate the above functions and provide for an improved internal control.

Unclearly communicated requirements contribute to delayed or improper payment to commodity suppliers

Because AID does not always clearly advise commodity suppliers of AID procurement requirements, the necessary documentation is often incomplete when AID receives the suppliers' requests for payment. According to AID officials, most problems experienced in the process of reviewing and approving suppliers' vouchers stem from poorly communicating documentation requirements and not applying AID Regulation 1 procedures uniformly to commodity suppliers.

For example, some direct letters of commitment incorporate Regulation 1 only by reference rather than by specifically listing the documents and performance requirements the supplier is to provide. Thus, when reviewing vouchers for payment, AID voucher specialists find that required documents have not been included. This either necessitates additional communication with the supplier and delays payments or results in AID's paying for commodities or services without properly determining their eligibility or price.

AID's General Counsel has noted the problem of attempting to bind suppliers to statutory and AID requirements not set out in the letters of commitment and its effect on the internal control procedures. Since 1981, the General Counsel has opposed the practice of deducting amounts determined to be improper from payments because AID's letters of commitment fail to state the terms of Regulation 1 explicitly. The General Counsel states that if AID intends to pre-audit payment documents and deduct any overpricing, it should so advise the supplier expressly in the letter of commitment because a mere reference to a regulation is not sufficient notice. Unless the supplier is expressly notified, the General Counsel suggests that, instead of deducting the overbilled amount from the supplier's voucher, the Surveillance and Evaluation staff approve full payment and prepare a bill of collection for issuance after consultation with the General Counsel.

Some AID officials disagree with the suggested procedure. Officials in the Surveillance and Evaluation Division believe that the General Counsel's requirement to prepare a bill of collection and to provide additional proof before the bill of collection is issued has weakened the process of protecting the AID certifying officer who authorizes payment. They said AID has the authority for making an administrative determination to withhold amounts determined to be ineligible for AID financing. This deduction is made only after careful review of supplier's and resource documents, such as bills of lading, price lists, bid evaluations, and letters of commitment; and payment is usually made within time limits allowed by the Prompt Payment Act of 1982. Also, the AID Inspector General has noted that prepayment audit of suppliers' vouchers is needed to maintain sound internal controls and such procedure is allowed by an AID handbook.

Although the problem of not applying AID Regulation 1 procedures consistently has been discussed within AID and in December 1982 was identified as a particularly weak internal control procedure, no action had been taken to resolve it until June 1983. We were advised that the Bureau for Management has directed its financial management unit, which is responsible for issuing direct letters of commitment and bank letters of commitment, to take action on this matter.

CONCLUSIONS AND RECOMMENDATIONS

As a financer of commodities, AID has a management responsibility for assuring that funds are used effectively and that expenditures are in compliance with the Foreign Assistance Act and AID regulations. Although AID has procedures and internal controls for measuring compliance and monitoring eligibility and pricing of commodities, compliance with financing procedures has been inconsistent and financial controls do not meet acceptable internal control standards. Particularly serious was the case in which AID, contrary to established procedures, disbursed millions of dollars without assuring that commodities were eligible for AID financing and did not act promptly to correct unauthorized payment. We believe that placing the responsibility for performing the review of commodity eligibility on a mission without (1) determining whether mission personnel have the expertise to carry out these tasks and (2) providing timely support and guidance are deviations from established procedures for certifying the eligibility of transactions under the direct reimbursement mode.

To lessen risk and provide greater assurance that AID does not pay for unauthorized and excessively priced commodities, we recommend that the AID Administrator:

--Increase audit coverage of commodity transactions financed under bank letters of commitment.

--Strengthen established procedures for financing commodities under the direct reimbursement method by determining that personnel authorized to perform eligibility reviews are qualified.

--Study the need to transfer the commodity voucher audit function from the Office of Commodity Management to another organization within AID where its degree of independence would be enhanced.

--Require responsible officials to issue letters of commitment in appropriate standard language which would clearly inform and bind suppliers to AID requirements.

AGENCY COMMENTS AND OUR EVALUATION

AID agreed in principle with two of the four proposed recommendations in commenting on our draft report but believed one recommendation to be premature and another to be not sustained by the underlying narrative, as discussed below.

Audit coverage and standardized letters of commitment

AID agreed with our recommendations to increase audit coverage of commodity transactions and to revise the language of the letters of commitment. It said that actions are underway which will improve procedures in these areas. They include plans for renewing the contract for performing commodity voucher reviews to increase the level of coverage and forming a committee to study commodity procurement issues and recommend steps to strengthen internal controls where needed. As a first step, the committee intends to establish specific requirements for issuing standardized letters of commitment throughout AID.

AID expressed disagreement with specific statements describing its payment and review procedures and figures showing the total number of commodity transactions processed and reviewed and estimated potential recoveries. Based on more recent data furnished, we have made appropriate revisions in this chapter. The principal changes are on pages 10 through 12 involving clarification of payment and voucher review procedures, adjustments in the volume of commodity transactions, and estimated potential improper payments and recoveries.

We note, however, that the differences in estimates were primarily due to the fact that AID lacks accurate information on procurement and payment of AID-financed commodities. This problem has been brought out in our previous reports and recommendations for improving the reporting of commodity transactions.

For example, in our report to the Congress on project planning and implementation problems,[2] we identified the need to establish an accounting and reporting system that includes systematic collection and analysis of information on project commodities. Also, in our report to AID on host-country contracting,[3] we recommended that appropriate data on host-country contracts be promptly reported to Washington.

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[2]AID Slow in Dealing With Project Planning and Implementation Problems (ID-80-33) July 15, 1980.

[3]Managing Host Country Contracting Activities (GAO/ID-82-42) June 2, 1982.

AID agreed that commodity programs are vulnerable to abuse and said that the actions it is taking are evidence of its determination to deal with the issues raised. We note, however, that the steps initiated are in very preliminary stages and will require further effort before actual improvements in procedures and internal controls can be ascertained. For example, although a committee was formed in August 1983 to study procurement issues, in the 3 months since it was established the committee had not held its first meeting.

Also, we note that AID has identified problems with the work performed by the contractor reviewing commodity vouchers. An AID study shows that less than one-fourth of the targeted 2,000 commodity vouchers have been reviewed although the current contract period is nearly over and the costs have escalated from $372,000 to $465,000. AID has reviewed the quality of the contractor's work and found it to be largely unacceptable. AID's review disclosed that the contractor's identified questionable payments of about $1.6 million have not been supported; of this amount only $227,000 has been accepted as having potential for refund claims. The inadequate voucher reviews are attributed to turnover and inexperience of contractor personnel.

AID officials told us that in recognition of these problems, AID is making another evaluation of the contractor's performance. Pending the outcome of this second evaluation, AID plans to extend the current contract by 4 months rather than issuing a new 1-year contract, as indicated in the Agency's response. The above problems with the current contract raise questions regarding the feasibility of AID's approach to provide voucher reviews that would adequately protect U.S. government interests and at the same time be cost effective.

In its response, AID stated that AID-financed ocean transportation bills of lading are audited by the General Services Administration. Officials of the General Services Administration told us that they do not audit AID-financed commodity import program transportation vouchers; only food shipment transactions financed under Public Law 480, Title II programs are audited. AID officials said that consideration is being given to contracting for transportation rate audits.

Transfer of commodity voucher review function

AID believed our proposal to transfer the commodity voucher review function from the Office of Commodity Management was premature and doubted that the present organizational arrangement has compromised the integrity of operations. However, AID recognized that there might be arguments both for and against a relocation and supported a further study of this change.

In view of AID's recognition of commodity program vulnerability and actions taken and promised to strengthen internal controls, we concur with AID's suggestion that a further study be made of the most appropriate location of the commodity voucher and price review function. We have revised the recommendation accordingly.

Controls over direct reimbursement

The Agency stated that the narrative section of the report did not support our recommendation that the AID Administrator establish appropriate controls for preventing deviations from established procedures whenever commodities are financed under the direct reimbursement method. AID pointed out that for the Sudan reimbursement case, the procedure was authorized by the Assistant Administrator for Africa. No disagreement was expressed with the facts presented that described the payment of $25 million for commodities without assurance of their eligibility.

We were aware that the Assistant Administrator for Africa approved the cable authorizing the AID mission in Sudan to perform the review of commodity eligibility and compliance with other rules of AID. However, AID officials told us that in requesting approval for this procedure, the originating office did not fully inform the Assistant Administrator that the recommended action was a deviation from normal procedures. We believe that the report adequately presents evidence to show that AID has a responsibility to assure eligibility of commodities before a direct reimbursement is made.

In its 1982 vulnerability assessment, AID acknowledged that the lack of properly trained and experienced international trade specialists is a serious agencywide problem and continues to foster and support waste and mismanagement of commodity programs. Thus, authorizing unqualified personnel to perform the initial review of documents as a condition to reimbursement, in our view, was a serious internal control weakness. Our revised recommendation is intended to strengthen established procedures and to prevent recurrence of such problems.

CHAPTER 4

NEED TO STRENGTHEN THE MONITORING OF COMMODITY ARRIVAL AND DISPOSITION

Some AID missions are not effectively monitoring the arrival and disposition of AID-financed commodities. As a result, AID is unable to adequately account for the arrival, distribution, and end use of CIP commodities. Staff limitations and insufficient guidance from Washington are among the factors contributing to inadequate mission oversight during program implementation. Proper accounting for the arrival and disposition of CIP-financed commodities will take more concerted action by both AID headquarters and overseas missions.

MONITORING OF CIP IMPLEMENTATION IS INADEQUATE

Some AID missions have not complied with the policy for monitoring commodity arrival and disposition or exerted sufficient management control over program implementation. Our review of five commodity import programs showed that only one mission had established and operated its own system to account for commodity arrival and disposition. At the other missions, we found that:

--Contrary to AID policy, mission personnel had not conducted or documented the evaluation of the host governments' arrival accounting systems to determine their adequacy or the need for mission-operated systems.

--Personnel generally had little familiarity with the host governments' commodity importing systems and thus were not in a position to prepare descriptions of the arrival accounting systems or to develop the missions' procedures for monitoring the systems.

--Program personnel did not actively seek to identify and correct CIP implementation problems.

--The missions had not systematically followed up on the distribution and end use of CIP commodities.

More specifically, missions had not adhered to AID policy that (1) the host-governments' arrival accounting systems be evaluated and documented to determine whether AID needs to establish and operate its own system and (2) mission monitoring procedures be developed and documented for a composite description of those systems.

In Kenya, the mission had not made the evaluation, and program personnel said they were unaware this was necessary. In Zambia, where AID has provided CIP assistance since 1973, the mission had just completed part of the description and evaluation of the arrival system along with a brief summary of monitoring procedures. The document discussed principally the fertilizer arrival procedures at the ocean port in South Africa and transshipment to Zambia but did not describe the disposition of the fertilizer within Zambia.

Generally, AID's planning documents discussed arrival accounting and end-use monitoring, implying missions' familiarity with host-governments' systems. Yet in some missions AID personnel had very little knowledge of these matters. For example, at the Sudan mission no one knew whether the government had an arrival accounting system, let alone how it worked. Mission officials did not know whether AID procedures for port clearance within 90 days and commodity use within 1 year were being met or whether required commodity reports were received as required.

According to mission officials, some host governments did not have systems in place to adequately account for the arrival of commodities. Further, missions had little expectation that the governments could effectively perform these functions. Despite this knowledge, only the AID mission in Egypt assumed the task for arrival accounting of CIP commodities. In Zimbabwe, where the program was just getting started, the mission was preparing to establish its own arrival accounting system.

Commodity arrivals should be monitored

Except in Egypt, missions do not obtain timely and accurate information on commodity arrival necessary to identify and correct problems or assure that commodities arrive in proper condition and quantities being financed.

Monitoring the implementation of CIPs helps AID assure that U.S. funds are disbursed in accordance with statutory requirements and that the commodities financed with these funds are used effectively to produce intended benefits. AID has not insured that host governments have a system that can adequately account for the arrival and disposition of commodities; and except for Egypt, AID has not set up its own system. This means that the missions cannot determine whether CIP assistance has been properly accounted for and effectively used.

Agency procedures prescribe that missions stay abreast of program implementation chiefly by requesting host-government reports and making routine port visits. Missions often did not request specific reports, however, or did not follow up when requested reports were not received. AID officials told us that host governments are not responsive to requests for information on CIP activities. In some cases, AID missions are not certain that the host governments maintain the required records.

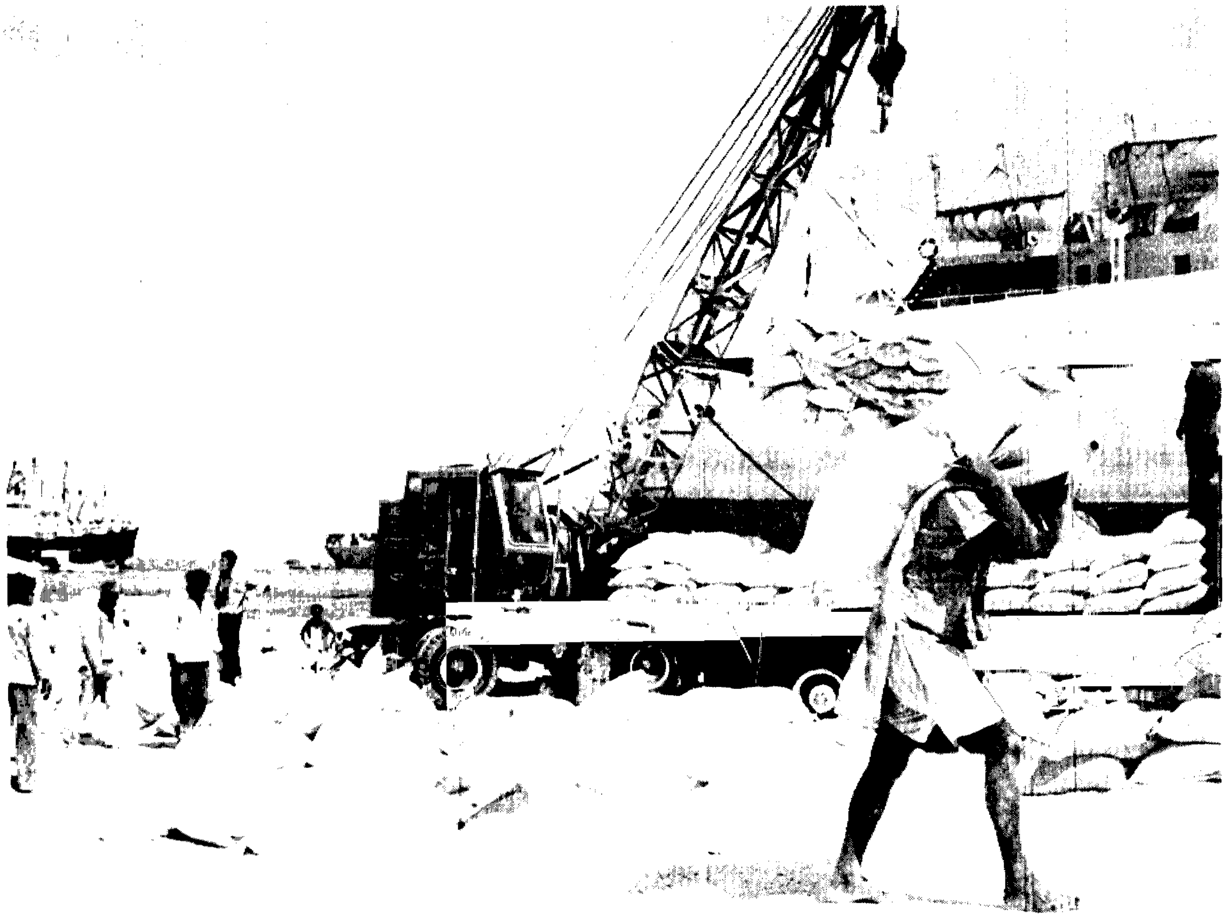
If periodic reports are not received on a timely basis and visits to CIP activities not made periodically, missions cannot verify that cargo has promptly cleared port facilities, that commodities have been sold or used within the prescribed time period, and that commodities imported under the CIP are not being re-exported or used for unauthorized purposes. In addition, absence of information on commodity arrival and disposition seriously hampers the effectiveness of the program, since necessary data is unavailable to facilitate program planning, implementation, and evaluation.

For example, missions in Zimbabwe and Zambia did not require arrival accounting reports from their respective governments on a continuing basis. In Egypt, Sudan, and Kenya, the missions required reports but the information was not being provided. The case in Kenya illustrates the problem of obtaining reports.

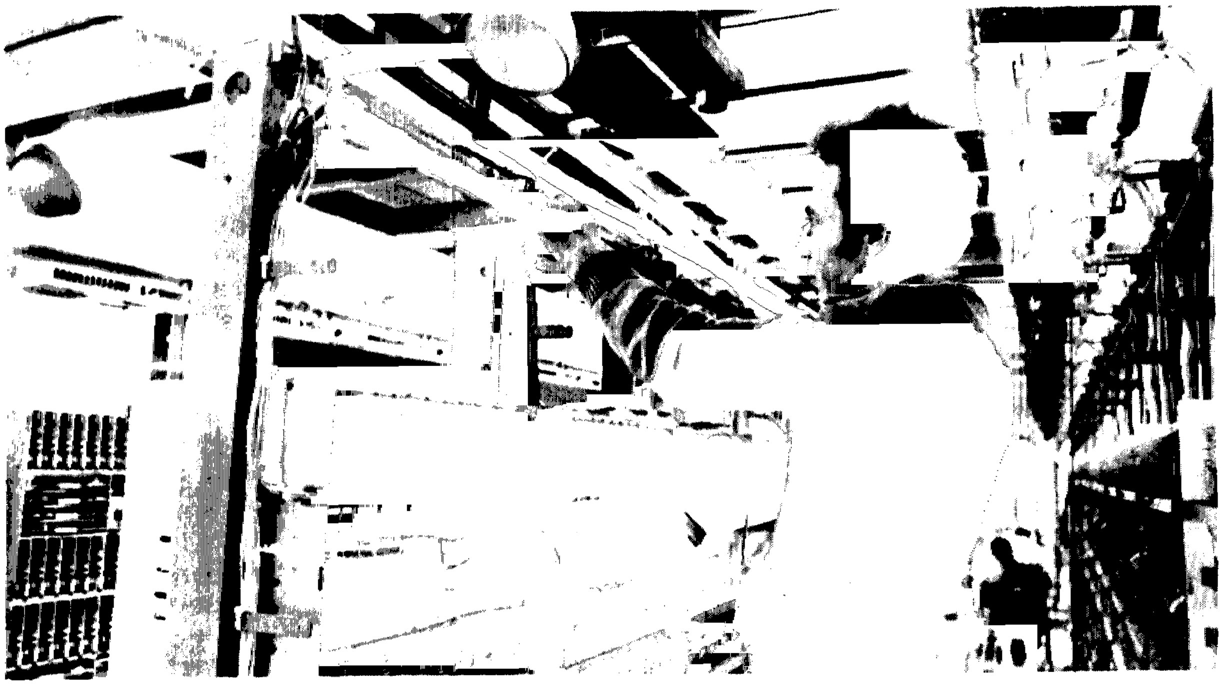
For the fiscal year 1980 CIP, AID requested a report from the government of Kenya that would show the type, quantity, and condition of the fertilizer received, noting damages, losses, and problems encountered as well as information on the movement, storage, and distribution. The government was reminded 4 months later that the report was overdue. The government's response a month later did not provide all of the requested information. The mission noted that the report was inadequate and planned to work with the government to obtain the correct information. However, a mission official told us that he had not been able to obtain the information.

AID did not formally require the host government to provide reports on fertilizer shipments for the fiscal year 1981 CIP. An official said that after several vain attempts to obtain formal reports from the government, the effort was abandoned. While the mission was able to obtain some unofficial reports, these were incomplete and not timely. Moreover, mission files did not contain complete records of the fiscal year 1980 and 1981 fertilizer shipped and off-loaded at the port. Thus, we could not reconstruct the arrival accounting of these commodities.

Another problem affecting program implementation is that some missions do not routinely perform port inspections to assure compliance with the procedure for prompt removal of commodities from customs and to identify problems of delayed shipments, losses, and damages. AID's experience on past



Unloading food staples at the Port of Alexandria in Egypt. In addition to agricultural commodities, AID has financed various raw materials, construction and transportation equipment, and industrial facilities such as the Cairo microwave telecommunications system (below). (Photo-courtesy of AID.)



programs has shown that physical checks of ports and warehouses is a good practice and often necessary to locate misplaced cargo.

AID personnel responsible for the Zambia CIPs had not inspected the ports in South Africa where most commodities for Zambia are unloaded. In January 1983, an AID supply management officer accompanied us on an inspection of port facilities and obtained valuable information for describing and evaluating the government's arrival and accounting system.

Despite knowledge of chronic congestion at Port Sudan, the Sudan mission had neither actively monitored the customs clearance process nor followed up with importers or port officials on the status of commodity arrivals. During our inspection of commodity arrival operations at Port Sudan, a shipping agent said that goods were now moving easily through the port but that unclaimed cargo was a problem. Sudanese port authorities consider cargo to be unclaimed after 30 days in port. We made a cursory inspection of a warehouse where unclaimed cargo was stored and located a consignment of AID-financed commodities which had been at the port for 8 months. We also observed several other AID-financed consignments which had been there for more than 1 month.

In May 1983, the mission director said that a contractor was hired to oversee arrival accounting and that the mission was negotiating a contract with a private firm to operate the arrival accounting system on a daily basis.

The mission in Egypt operates and monitors the commodity arrival accounting system. Mission staff stationed at the Port of Alexandria keep track of the quantity, date, and value of goods off-loaded, cleared through customs, and received by the importer. Short shipments, damages, and losses are recorded and followup action is taken to resolve any discrepancies. The mission also prepares a report which lists and gives the ages of shipments that remain in customs for more than 60 days and takes action to encourage importers to pick up their goods.

Lack of systematic procedures for monitoring commodity disposition impedes program effectiveness

Some missions do not adequately monitor the disposition of CIP commodities. With the exception of Egypt, none of the missions had developed procedures for either routinely checking commodity distribution within the prescribed one-year period or systematically verifying end use.

Mission officials in Sudan said that informal spot checks have been made and will continue to be made at selected activity sites. They told us that the mission plans to increase its efforts for monitoring commodity end use, particularly those transactions for public sector imports.

A mission official in Zimbabwe said that informal spot checks of the commodities that have already arrived in-country have been made. He said that, since much of the program is implemented through private importers, there was no need to formally monitor end use as the importers were interested in promptly selling these high-value items, such as tractors, earth moving equipment, and raw materials.

AID/Zambia could not track distribution and sale of all fertilizer within Zambia, as no attempt had been made to monitor commodity disposition beyond its receipt at the point of entry into Zambia. Even the host government could not track fertilizer movements to depots beyond the capital city.

In Zambia and Kenya, the policy to use or sell commodities within 1 year after arrival in-country was not being met. In Zambia, for example, substantial quantities of fertilizer were not used within the required 12 months. We found that 3,800 metric tons of AID-financed raw materials were at the Zambia fertilizer plant awaiting processing and an additional 9,000 metric tons of processed fertilizer, which included AID-financed inputs, were stored there awaiting bags for shipment to distribution depots in country. In fact, Zambian government officials told us that the only fertilizer materials at the plant in January 1983 were AID-financed, which had arrived in 1981.

In Kenya, because of higher U.S. flag shipping charges, a shipment of bagged fertilizer was priced higher than competing products and therefore remained unsold. Although the mission had raised the issue with the government in July 1982, suggesting the price be lowered, the government did not formally notify the mission that the price had been reduced until January 1983.

Egypt was the only mission which had performed extensive end-use checking of CIP commodities. As of March 1983, records showed that 70 percent of the value of goods received had been checked. Two staff members in the controller's office, assisted by mission staff in Alexandria, spend about 40 percent of their time on end-use reviews. These reviews are conducted using the mission's commodity arrival records as a base. Commodities are physically inspected or, in the case of resale or manufacture, importer records are examined. The controller's office coordinates with the Office of Commodity Management and Trade in selecting commodities to be checked and resolving problems.

In a December 1980 report, the AID regional Inspector General criticized the mission's end-use checking, noting that all or most of certain commodities were checked frequently while other commodities were seldom, if ever, checked. During that time, the mission's goal was to check 75 percent of the value of commodities received. Apparently this led to the practice of complete checking of some high-value and bulk shipments while ignoring others.

The acting controller said that he was changing the mission's selection procedures for end-use checks. Commodities checked frequently in the past with a record of no problems would not be scheduled. Instead, the mission would concentrate on importers and commodities which have received little coverage.

INSUFFICIENT STAFF AND GUIDANCE CONTRIBUTE TO INADEQUATE MONITORING

Staff limitations and insufficient guidance were often cited by mission officials as the major cause of inadequate program monitoring. Further, AID requirements' lack of specificity for implementing CIPs raised several issues which also appear to have contributed to the missions' difficulty in monitoring the program.

Lack of staff impedes effective monitoring

Insufficient staffing was primary among the various reasons cited by mission officials for not strictly adhering to AID regulations and aggressively monitoring CIPs. There were inequities in staffing levels in proportion to program size at certain missions.

For example, in Zambia, officials said they cannot monitor the disposition of CIP commodities very closely, primarily because of the small size of the total mission staff--only six AID personnel. They felt that with a single commodity--fertilizer--and one importer, arrival accounting was not as important and that once the commodities have been delivered to the importer, the disposition has been completed and the responsibility for monitoring fulfilled. It was their position that to track the disposition further would impose a serious drain on the mission's limited resources.

Similarly, mission officials in Sudan and Zimbabwe said that the need for extensive monitoring is not as great when the private sector is involved because private importers are expected to be "self-policing." According to these officials, the private importers' stake in ensuring prompt clearance and sale of commodities makes it unlikely that high-value items would remain unused or unsold longer than necessary. This may not always be true, however, since some of the unclaimed consignments that we observed at the port in Sudan were private-sector imports.

With regard to staffing, AID staff was not always assigned in proportion to the size of CIP activity. The shortage of experienced mission staff was particularly acute in Sudan, for example, where $190 million in CIP assistance was provided for fiscal years 1980 through 1982, and $48 million was approved for fiscal year 1983. Yet, for years, there was only one AID employee in the supply management office and two in the controller's office. In addition, from November 1982 until mid-February 1983, there was no permanent supply management officer at the mission. This contrasts with staffing in Zimbabwe, where one full-time supply management officer and the controller on a part-time basis monitor the $50-million CIP just getting underway.

The present supply management officer and the controller's staff in Sudan feel they are not adequately staffed to perform CIP monitoring. In July 1983, however, another direct-hire supply management officer was assigned to the mission. Also, as stated on page 27, an individual was hired and a private firm was to be engaged, using CIP-generated local currency proceeds, to assist with arrival accounting tasks. In this way, the mission had taken positive steps to improve the monitoring of commodities.

AID needs to issue clearer guidance on monitoring CIPs

During our review, missions brought out several issues involving unclear guidance which appeared to contribute to their problems in monitoring CIP implementation. First, there were no useful procedures for monitoring arrival and disposition of imports. Although an AID handbook describes the checking of commodity arrival and end use as one of the missions' monitoring responsibilities, it provides very few specifics on how this should be accomplished.

Second, monitoring commodity arrival and disposition was done differently. For example, in Zambia, where there is no supply management officer, monitoring was handled as an additional responsibility by other AID personnel. At the Sudan and Egypt missions, monitoring was assigned to the controller's office. In Zimbabwe, the responsibility was assigned to the supply management officer who worked full time on the CIP, while the mission controller was responsible for monitoring the generation and programming of local currency from the sale of commodities.

Third, the concepts of disposition and end-use checking were perceived differently by the various missions. For example, they were not clear on the definition of end use as it pertains to large bulk shipments, such as fertilizer. The most common interpretation entailed tracking the commodities to the first distribution point; however, the missions were not certain that this met the spirit of AID guidance. For some commodities, such as fertilizer raw materials, mission officials could do no more than track the materials to the fertilizer plant.

CONCLUSIONS AND RECOMMENDATIONS

Only one of the five AID missions reviewed was adequately monitoring the arrival accounting and disposition of AID-financed commodities. At the other four missions, successful program monitoring was impeded by non-compliance with applicable AID handbooks and by insufficient staff and guidance from Washington.

Despite requirements for host-government reports and visits to CIP activity sites, missions did not aggressively use these tools to obtain timely and adequate information on the status of the programs necessary for successful monitoring. Missions did not always place reporting requirements on the host governments or follow up when the required reports were not submitted on a timely basis. In addition, missions did not perform routine port visits or systematic end-use inspections to assure that commodities were promptly removed from customs and properly used.

In general, AID officials at the missions we visited believe that after funds have been approved and commodities procured, the objectives of the CIP assistance have been achieved. Attention then shifts to the preparation of the next year's CIP, with less emphasis on subsequent monitoring activities.

While we recognize that making AID's monitoring guidelines more explicit might require additional mission effort and reporting, missions need to account satisfactorily for CIP commodities on a uniform basis. The countries we visited, however, probably do not have the records or procedures necessary for a detailed accounting of their programs as provided for in AID Regulation 1.

We believe that AID needs to strengthen the monitoring of CIP implementation and issue instructions to the missions to comply with the Agency's stated policies. However, AID also needs to establish and issue specific guidance to the missions on how to perform and document the monitoring of commodity arrival and disposition. Particular attention is needed for monitoring the private-sector importers and the end-use checks for both public and private sectors.

To the extent that AID cannot provide missions with sufficient staff for carrying out monitoring responsibilities, we believe it has an option to use CIP-generated local currency proceeds to hire contractor assistance, as has been done in Sudan. We believe a concerted action by both AID headquarters and missions is required before there can be reasonable assurance that AID-financed commodities are being properly accounted for and used. Accordingly, we recommend that the AID Administrator:

--Issue specific guidance to AID missions on monitoring the implementation of commodity import programs, including the arrival accounting and disposition of commodities.

--Ensure that missions comply with established monitoring procedures.

AGENCY COMMENTS AND OUR EVALUATION

AID has agreed to amend its handbooks to indicate minimum standards and examples of arrival and end-use accounting systems. AID will require each mission with a commodity import program to provide a detailed description of the monitoring systems to be used. They will be reviewed by Washington and suggestions for improvements forwarded to the missions.

In response to our suggested option to help alleviate the limited availability of AID staff for complying with arrival and end-use accounting procedures, AID agreed to supplement these capabilities when necessary by hiring contractor assistance.

Based on information provided in the Agency's response, we have revised the report language to reflect AID/Zambia's monitoring of commodity arrival.

CHAPTER 5

BASIC QUESTIONS NEED TO BE ANSWERED CONCERNING

ACCOUNTABILITY FOR LOCAL CURRENCY PROCEEDS

Most AID missions do not systematically monitor the proceeds from CIP sales. Although the law and AID regulations require that the proceeds be deposited in a special account and used according to mutually agreed arrangements, AID monitoring does not assure that the expected amounts are generated, deposited, and reconciled with actual deposits; that host countries provide required status reports; or that the disposition of proceeds is in accordance with prescribed uses. As a result, missions do not know the status of special accounts, some of which had not even been established, and are unable to account for the amounts generated and used.

AID missions do not have adequate instructions on monitoring local currency generation and uses. AID needs to examine several key issues dealing with local currency in establishing guidance to its missions.

AID DOES NOT ADEQUATELY MONITOR LOCAL CURRENCY GENERATION AND ITS USES

Most AID missions we reviewed do not adequately monitor the host-government's accounting and use of proceeds generated from the sale of commodities, as required. AID regulations implement the statutory requirement of section 609 of the Foreign Assistance Act, which provides that local currency generated by CIP transactions be deposited in a special account and made available to the United States and cooperating country. While loan-funded commodity import programs, such as Zambia's, are not specifically subject to this legislation, AID can and does negotiate local currency generation and use provisions with recipient countries.

The disposition of local currencies generated is specified in the Commodity Import Agreement. The mission notifies the host government of the amount of local currency to be deposited and the basis of such computation. In four of the five missions reviewed, we observed insufficient management attention to the requirements of these agreements.

Inadequate monitoring of local currency generation

AID missions had numerous problems in monitoring local currency generation. The Sudan mission initially did not comply with the requirement to establish a special account and was unable to determine the status of the local currency generated from commodity sales. In Kenya and Egypt, the missions did not receive the required reports to satisfy the requirement that local currency proceeds be deposited. The Zimbabwe mission was an exception, however, and local currency generated by the sale of imported commodities was closely monitored.

Inadequate attention to the generation of local currency noted at the Sudan and Egypt missions illustrates problems attributable to the missions' poor monitoring of host-government records and reporting, as described below.

In Sudan, a special account was not established for fiscal year 1980. The CIP grant agreement required the government of Sudan to establish a special account and deposit therein the local currency generated from the sale of commodities. The Sudan mission, however, had no knowledge of the generation of sales proceeds and therefore could not ascertain the amount, if any, of local currency generated. A mission official said that any funds generated were deposited directly into the Sudanese treasury.

In 1980 and 1981, the mission requested the government of Sudan to provide information on whether a special account had been established and the amount of deposits and withdrawals. The government did not respond to these inquiries.

In May 1982, the mission informed the Sudanese government that $26.2 million should have been deposited in the special account as of March 31, 1982. The mission director said another request for a status report on these deposits was made in May 1983.

At the Egypt mission, corrective action had not been taken as promised on recommendations prescribed by two 1980 AID Inspector General reports. These reports had recommended that AID improve its monitoring of local currency by enforcing the requirement of the grant agreement for obtaining monthly bank statements on the special account, coordinating with the government of Egypt in implementing procedures for ensuring adequate internal controls over the special accounts, and designing a computer sub-system to monitor local currency generation and deposit.

As of March 1983

--although the mission had begun receiving monthly bank statements as requested, the deposits were not correlated to the specific AID payment documents;

- --the government of Egypt had not complied fully with the requirement to establish a consolidated special account; and

- --the local currency monitoring sub-system was not included in the final computer system design.

Mission officials acknowledged that they have not properly accounted for the generation of funds in accordance with grant agreements because the government has not provided essential information. We were told the mission is planning to use conditions precedent before obligating or disbursing the 1983 CIP funds as a means to make the government of Egypt furnish information on the past programs.

Agreements for programming local currency not monitored

Like the situation for monitoring the generation of currency, AID missions have not adequately monitored the programming of local currency to ensure that funds are used according to CIP assistance agreements. AID missions are responsible for monitoring host-governments' compliance with the terms of these agreements and often require in the agreements that host governments maintain records and make reports on the agreed uses of the proceeds. Because the missions, with the exception of Zimbabwe and Sudan, did not monitor host-governments' compliance with these requirements, they were unable to account for the use of deposited funds. The Egypt mission was unable to account for the use of funds which had been deposited since fiscal year 1979. The Kenya mission did not have adequate controls over whether funds were being used for the agreed upon projects. AID/Zambia did not receive complete and timely reports from the government and did not hold the required meeting on the uses of local currency proceeds. These missions' monitoring problems are presented below in detail.

As of March 1983, the Egypt mission was unable to account for the use of about $82 million in CIP-generated funds which had been deposited in a special account since fiscal year 1979.

The government of Egypt and AID had agreed to use local currencies generated with the fiscal year 1979 and 1980 CIPs for trust fund activities, local currency support for AID-financed projects, and other support activities. In March 1981, the parties agreed on the allocation of these funds to the various categories. Withdrawals from the account for specific uses within the broad categories were to be mutually agreed to on a case-by-case basis.

As of December 31, 1982, $120 million had been deposited to the special account and $112 million withdrawn. The government of Egypt transferred $22 million to the AID trust fund account, and an additional $8 million had been withdrawn for three mutually agreed upon activities. The remaining $82 million was withdrawn without prior mission approval or knowledge. The procedures for implementing the agreement also required the government to submit quarterly reports on the status of disbursements made to the various activities. No report was received.

Mission officials acknowledge that they had not properly accounted for the use of local currency proceeds in accordance with grant agreements, and they have initiated discussions with host-government officials to resolve the matter.

In March 1981, AID and the government of Kenya agreed on a list of development projects eligible for CIP-generated local currency financing. As of January 1983, the mission did not have information on the use of these funds although the projects on the list were already included in the government's 1982-83 budget for funding.

According to a mission official, the mission had not ascertained whether any withdrawals had been made from the special account or whether the host government had provided information to assure AID that the funds used were for the agreed upon projects. The official believed the government would have difficulty supplying the information because the funds in the special account were transferred to the government's general account and were not traceable. The official explained that the mission does not consider that its monitoring responsibility extends beyond identifying eligible development projects.

AID/Zambia's monitoring of local currency programming involves ensuring that the government of Zambia has attributed the local currency equivalent of the CIP loans to its development support measures jointly agreed to by AID and the government. CIP loan agreements establish deadlines for the government to take certain steps toward implementing the support measures. They also require periodic meetings between AID and the government and progress reports showing how local currency use implements the support measures. Our review showed that required meetings had not been held and the reports were incomplete and not provided on a timely basis.

GUIDANCE ON LOCAL CURRENCY PROCEEDS IS NEEDED

The incomplete guidance on monitoring local currency proceeds seriously hampers AID's efforts to carry out statutory and Agency objectives. Consequently, AID missions struggle with questions on practically every aspect of implementing the requirements for the generation and programming of local currency proceeds that accrue from the sale of AID-financed commodities.[1] AID needs to issue guidance on the following questions to help ensure effective monitoring of local currency proceeds.

<u>What type of procurements should generate local currency?</u>

The Foreign Assistance Act states that when the sale of a commodity furnished by the United States results in the accrual of proceeds to the recipient country, local currency equal to such proceeds is to be deposited into a special account. The difficulty in applying this requirement is in determining which CIP transactions ultimately result in sales. The CIP is used by different types of importers to procure a variety of commodities for various uses.

Mission officials expressed a view that the law is not intended to apply to host-government procurement of commodities for its own use, but they are not certain whether the law applies to a variety of other types of procurement, such as government procurement of fertilizer, wheat, and other commodities that are resold to both private and public-sector users; private-sector procurement of machinery used for production; or procurements by quasi-government entities.

<u>What basis should be used for determining the amount of local currency to be generated?</u>

The stipulation that the special account contain local currency equal to the proceeds from commodity sales is problematic, since AID has not issued guidance on how to determine sales proceeds. Missions require importers to generate local currency equal to the value of CIP funds disbursed and rely on the AID disbursements report as the basis for the calculations.

CIP disbursements do not necessarily equal sales proceeds, however, particularly when private importers procure commodities for resale. The commodities are generally sold at a price sufficiently high to cover the foreign exchange cost of the commodity plus custom duties, taxes, profit, and other fees.

On the other hand, commodities imported for use, such as machinery, do not result in direct sales but are used to produce

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[1]The AID mission in Egypt has been consulting with AID legal advisors on the applicability of section 609 of the Foreign Assistance Act.

commodities for eventual sale. Guidance is needed as to what basis should be used for computing local currency for this type of procurement. If disbursements are used to calculate the amount of local currency to be generated, this issue may raise broader questions about the intent of the law. If Congress intended the law to apply only to commodities that are imported for resale, the size of the special accounts may significantly diminish in Sudan, Egypt, and Zimbabwe, because in these countries the majority of the funds were allocated to procurements of commodities for use by either the government or private manufacturers rather than for resale.

What are appropriate uses for local currency?

The law is not specific on the uses of local currency. It states that a portion of the funds may be allocated for use by the U.S. government and the remainder is to be used for mutually agreed upon programs. As discussed previously, missions use these funds in a variety of ways but primarily for general budgetary support, which essentially returns the funds to the host governments. In some countries, such as Zambia, missions require the governments to show attribution of the local currency in their agricultural development budgets. Mission officials admit this is merely a paper transfer and does not influence the government budgeting process.

While some AID officials seem to view local currency as a valuable resource available for funding development projects, others regard local currency funds as a reallocation of government revenues between the special account and other budget categories. These officials believe in the value of requiring local currency to be generated as a means for (1) insuring that AID grant funds do not result in windfall profits to private importers and (2) providing the host government with reason for insuring that the commodities are properly used. However, they also believe that once the local currencies are properly accounted for and AID program needs are met, the funds should be returned to the government.

What are AID's responsibilities for monitoring the use of local currency?

Overseeing the use of local currency was a particularly sensitive issue for the missions visited. Mission officials said that their responsibilities for monitoring appropriated funds are overwhelming due to the shortage of staff. They are concerned that Congress may expect the same extent of monitoring on the use of local currency, which they believe would not be possible. To date, AID has issued no specific guidance on what is expected. Accordingly, with the exception of Zimbabwe and Sudan, missions have done little monitoring.

In Zimbabwe, the mission has required the government to provide periodic reports on the projects being financed with CIP-generated proceeds. Mission officials said they intend to make some site inspections as well. In Sudan, since the generated funds are used also to finance the local currency costs of AID projects, the local currency and appropriated funds are monitored jointly, and the monitoring workload is not therefore significantly increased.

CONCLUSIONS AND RECOMMENDATIONS

AID is not adequately monitoring host-government compliance with the requirement of the bilateral agreements that special accounts be established for all grant-funded commodity import programs when proceeds accrue from the sale of commodities. AID monitoring of the generation and programming of local currency is inadequate because AID has not issued detailed guidance on how to implement section 609 requirements for establishing special accounts. As a result, mission officials are struggling with questions regarding local currency proceeds. Moreover, host governments do not always provide the necessary information to permit AID monitoring of local currency generation and use, as required by bilateral agreements.

We believe a major reason for the inadequate management attention to local currency monitoring is that this aspect of the CIP does not affect program obligation and disbursement. As we noted in chapter 2, the missions appear to devote their efforts to tasks that directly affect program obligations and disbursements rather than to program implementation planning.

AID also needs to answer certain basic questions regarding local currency generation and use and to determine the extent to which missions should monitor local currency activities. In our opinion, good accounting for a CIP from the time goods arrive and are sold to when local currency is generated and programmed is difficult under existing conditions. Important decisions therefore must be made if AID expects missions to become more active in effectively monitoring local currency generation and use.

We believe AID should consult with appropriate congressional committees about the difficulties missions experience in monitoring local currency generation and programming. It may be unrealistic to expect missions to maintain the same type of control over local currencies as is required over appropriated funds. Meanwhile, AID needs to provide appropriate guidance to the missions on how to monitor establishment of special accounts. Accordingly, we recommend that the AID Administrator:

--Issue guidelines on accounting for the generation of local currency proceeds resulting from the sale of AID-financed commodities.

--Issue appropriate guidance on monitoring the use of local currency generated from the sale of commodities.

AGENCY COMMENTS AND OUR EVALUATION

AID reported that guidance is being drafted concerning the preparation and submission of mission plans for the use of CIP and Public Law 480 local currency generations. It said that this message might be an appropriate vehicle for providing guidance to missions in response to our recommendations. Also, the Agency acknowledged the need to advise missions that special accounts must be established for grant-financed CIPs. Finally, missions are being requested to report annually on how local currency generated from the sale of Public Law 480 Title I food aid and CIPs has been allocated.

AID acknowledges the incompleteness of its existing guidance, particularly for CIPs, and states that its 1976 guidance does not provide answers to the important questions on local currency accountability discussed in this chapter. Millions of dollars continue to be committed to CIPs without adequate accountability for the local currencies generated. AID missions need specific guidance and timely direction from AID Washington on what is expected of them in complying with the law and AID regulations which seek to maximize the development impact of CIP assistance. The 1983 policy statement on local currency proceeds from Title I food aid cited in AID's comments can be usefully applied to CIP generations, according to AID. To our knowledge, it has not been made applicable to CIPs.

With regard to the requirement for depositing local currency proceeds, we have deleted Zambia from countries mentioned on page 34 in recognition that the Zambia CIP is loan-funded and thus not subject to the requirement. However, it may be useful to note that requirements for the generation and use of local currency proceeds from loan-funded CIPs can be (and are in Zambia) subject to the agreement between AID and the recipient countries.

CHAPTER 6

AID NEEDS TO STRENGTHEN EVALUATION

OF COMMODITY IMPORT PROGRAM ASSISTANCE

Despite legislative requirements that AID improve the assessment of its programs, AID has not developed evaluation procedures for CIP assistance. As a result, AID does not formally evaluate commodity import programs and does not have information on program performance which is needed for operating future programs. AID should require that CIP assistance be evaluated.

PROCEDURES FOR EVALUATING PROGRAM ASSISTANCE HAVE NOT BEEN ISSUED

Although AID has issued a policy statement that both non-project and project assistance programs are to be evaluated, it has not developed instructions on evaluating non-project assistance. The issuance of these instructions has been pending since 1975. In the absence of guidance, CIP evaluations have been limited to only brief statements in the planning documents for the previous year's program.

Evaluation is a clearly stated element in AID's management process. Also, a mandate for evaluation comes from the Office of Management and Budget regulations directing all agencies to assess program efficiency and effectiveness. Despite this requirement and AID policy pronouncements, AID has not developed specific procedures for evaluating program assistance and AID's geographic bureaus have not assured that commodity import programs are adequately evaluated.

It is AID policy to use information obtained through evaluations as a basis for designing programs and projects. Evaluation is a key element in the accountability to the Congress and the executive branch and an integral element of AID's policy and program management processes. However, AID's Office of Evaluation has not issued formal procedures for evaluating CIPs, although, since September 1975, it has included space for a chapter on evaluations in the handbook dealing with non-project assistance.

Generally, AID evaluation officials agree that CIPs should be evaluated and procedures should be developed and issued. This has not been done because the primary focus has been on evaluations of project assistance. Some officials acknowledged the need for guidelines that would address how well AID and the host country have managed the programs. As discussed in chapter 2, we found that in planning CIP assistance, AID apparently does not incorporate or adequately consider evaluative information on past and current performance.

In a July 1982 directive, the AID Administrator reasserted the need for evaluating economic assistance programs, including CIPs, by expressing concern over the effectiveness with which such resources or commodities are employed. To help ensure that resource transfers have the greatest possible developmental impact, the directive required that country performance be closely monitored and evaluated to determine whether such assistance should be continued.

Although the geographic bureaus are responsible for guidance to the missions, they have not provided procedures for evaluating CIPs. AID officials told us that evaluation of CIP assistance is made each year when the following year's program document is prepared. We found, however, that the brief statements in AID's planning documents fall short of providing information for comparison of the actual results of CIP assistance with those anticipated when the program was undertaken. Moreover, they do not show required actions that would increase the likelihood of achieving program objectives.

Mission officials told us that in the absence of established, uniform, agencywide procedures for conducting formal evaluations of CIPs, the missions employ a variety of approaches to evaluations and hold various attitudes and beliefs on this subject. Some officials said that CIPs should not be evaluated in the same manner as project assistance, since the infusion of foreign exchange accomplishes the primary objective of the CIP aid and that actions occurring after the commodities arrive are incidental. Others stated that CIP evaluations are difficult to design and that a brief description of the past year CIP performance suffices for an evaluation.

Generally, mission assessments of past performance have been cursory and, in some cases, unsubstantiated or based on incomplete and inaccurate information. We were told that three missions planned to conduct evaluations of their CIPs.

Concern over not evaluating CIP assistance was evidenced in an October 1982 AID report to the Administrator. It recommended that AID give more attention to evaluating program-type assistance and auditing commodity import programs. The report noted a paucity of evaluation materials on the Agency's recent program assistance experience and that relatively few audits of CIPs, except for Egypt, had been made in the past 5 years. Apart from the Inspector General reports on Egypt's CIP, the Inspector General has reviewed only Kenya's CIP. Its review of the Zambia CIP planned for March 1983 was canceled after the regional Inspector General received the results of our Zambia review.

CONCLUSIONS AND RECOMMENDATION

AID is aware of the value derived from evaluations and has performed many evaluations of project assistance which have provided information needed by managers and designers in planning new and recurring projects. However, AID has not given the same attention to non-project assistance, including CIPs.

Although CIP assistance may not lend itself to the same evaluation methodologies used in project assistance, we believe AID should develop and formalize evaluation procedures for CIP assistance in compliance with the Foreign Assistance Act and AID directives. We believe that by placing appropriate emphasis on evaluating CIP assistance, the management of current programs would be improved and the effectiveness of future programs enhanced.

Accordingly, we recommend that the AID Administrator direct the Office of Evaluation to establish a requirement for evaluating CIP assistance and develop specific guidance for those performing such evaluations.

AGENCY COMMENTS AND OUR EVALUATION

AID agreed with our recommendation and said that a report is expected soon identifying the array of non-project assistance activities and how they are being evaluated. Promised actions include a review of the adequacy and relevance of AID's non-project assistance handbook and an evaluation of several CIPs to gain experience that would help shape evaluation guidelines for CIPs.

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

ASSISTANT TO THE ADMINISTRATOR
FOR MANAGEMENT

18 NOV 1983

Mr. Frank C. Conahan
Director
National Security and International
Affairs Division
United States General Accounting
Office
Washington, D.C. 20548

Dear Mr. Conahan:

Thank you for giving us the opportunity to comment on your draft report, entitled "Agency for International Development Needs to Strengthen Its Management of Commodity Import Programs" (GAO assignment code 472014) which was forwarded with your letter dated October 4, 1983.

Our comments are appended. They are arranged and identified by chapter number to coincide with the chapters of your report. We have no comments on Chapter 1.

We would be pleased to meet with you or members of your staff to clarify any question about our comments.

Again, thank you for the opportunity to review and comment on your report.

Sincerely,

R. T. Rollis, Jr.

R. T. Rollis. Jr.

Enclosure:
Comments on Draft Audit Report

CHAPTER 2

The GAO draft report is correct in stating that schedule slippage has occurred in the procurement of A.I.D.-financed fertilizer, notably in the case of Zambia. However, a number of critical factors outside the control of A.I.D. have contributed to this slippage. In accordance with your emphasis on Zambia in the draft report, the following comments apply to commodity programs in that country.

First and foremost, problems related to the procurement of fertilizer for Zambia have been recognized at last by the Government of the Republic of Zambia (GRZ). This is most important because a major difficulty encountered in A.I.D. program development and implementation with less-developed countries is the critical need for a country to first recognize its own restraints. Once this is accomplished and the problems mutually agreed upon, knowledgeable remedial action can then be undertaken. This recognition has been evidenced with the issuance by the GRZ of a comprehensive report, dated July 1983, entitled "Fertilizer Supply and Distribution - Issues and Constraints", conducted by the Planning Division, Ministry of Agriculture and Water Development, Lusaka, Zambia. The report's study team included appropriate GRZ officials assisted by U.S. fertilizer specialists from the International Fertilizer Development Center, Iowa State University and A.I.D. The study was initiated by A.I.D. as part of the Agriculture Training and Planning Project administered by the University of Iowa with A.I.D. project funding provided where appropriate. We believe the study findings address the many complex problems inherent in the procurement of fertilizer for Zambia, specifically those resulting from GRZ inefficiencies in the procurement process, which is further complicated by Zambia's physical location as a landlocked nation. In the report, the GRZ recognizes in-depth the problems resulting from its procedures and from its limited physical resources, which adversely affect fertilizer procurement. These problems include GRZ shipping arrangements which often result in problems such as: (a) thirty separate transfers from port of discharge to the consumer in Zambia, (b) inadequate storage facilities, (c) acceptance by the GRZ of title at the port of discharge, which fragments subsequent responsibility, because neither the forwarding agent nor the railroad will then accept full forwarding responsibility. This procedure results in a principal disincentive to efficient movement of the fertilizer. The GRZ report also addresses the need to improve its processes for appropriate fertilizer selection and for forecasting demand. Currently, some eighteen months expire between the beginning of the GRZ forecast and the actual need for the fertilizer. This practice provides no procedure for the updating of a forecast on the part of the GRZ and therefore could adversely affect the tendering process.

Space does not allow us to address in full detail how the above restraints affect A.I.D. implementation schedules. We believe, however, that these adverse factors contribute to the type of problems indicated in the GAO draft report, e.g., additional foreign exchange costs to the Government of Zambia and failure to have the right type of fertilizer arrive in Zambia at the appropriate time.

Zambia, without qualification, is a less-developed country in the full sense, A good understanding of the many problems affecting the procurement of fertilizer for Zambia, including those which are outside any donor's control to remedy, will be gained from a reading of the Zambia Fertilizer Supply and Distribution report. It is apparent that many of these problems will require a long time for the GRZ to remedy. We feel the issuance of the GRZ report and its inclusion of a scope of work for a recommended follow-up in-depth study is an important step forward. A.I.D. will encourage this follow-up effort. In the interim, the report is clearly a new and valuable management tool for all donors with respect to both pre-implementation and implementation planning.

Inasmuch as this report was not available at the time of its audit, we request that the GAO now review the report and recognize in their final report the many complexities which lie outside of a donor's direct control and which adversely affect the procurement of fertilizer for Zambia.

In addition to the above, other factors have contributed to schedule slippages of A.I.D.-financed fertilizer for Zambia and other less developed countries. Certain of these delays, at times protracted, have occurred in our USG apportionment process for the economic support funds used to finance fertilizer procurement. In this respect, apportionments are made country-by-country on a priority basis and are controlled by OMB, State and Treasury. Until the apportionment action is finalized, procurement on A.I.D.'s part cannot proceed.

Further, by agreement reached with the U.S. fertilizer industry, A.I.D. does not usually allow the shipment of fertilizer procured by less-developed countries to take place during the period from February through May. If such shipment were generally allowed, the procurement of relatively large quantities of fertilizer during the February - May period could increase prices to the disadvantage of American farmers. This is yet another restraint that can influence the timing of the procurement cycle.

Traditionally, the Government of Zambia has accepted title for fertilizer cargo at ports of discharge located in South Africa, Mozambique and Tanzania with arrangements made with freight forwarders for transport to various sites within Zambia. In recent years, A.I.D. has been willing to reserve foreign exchange loan funds for the costs associated with such inland transportation. Each year, with one exception, the Government of Zambia has preferred not to use A.I.D. funds for such a purpose. Instead, the GRZ has elected to buy additional quantities of fertilizer justifying this decision on the basis of need and noting that the loan agreements allow them to exercise the right to determine the amount of fertilizer to be purchased. However, when freight forwarders have demanded payment for inland transportation, usually in advance, the Government of Zambia has been hard-pressed to make such funds readily available. At this point, A.I.D. cannot furnish additional funds, because the GRZ has already used the A.I.D. loan funds available to it. A.I.D., however, will reinforce its efforts to prevail upon the Government of Zambia to set aside sufficient loan funds for inland transportation.

As the GRZ accepts title to fertilizer cargo at the port of discharge, any shipping losses from the port to the destination within Zambia are its responsibility. This procedure, as indicated in the Fertilizer Study and Distribution report, complicates the above situation by providing another disincentive for freight forwarders to efficiently transport the fertilizer to Zambia. The GRZ report recommends that a Zambia entity responsible for importing fertilizer take title after shipment arrives in Zambia rather than at the discharge port. This procedure would place the burden of transportation losses and delays on the transporters and provide an incentive needed for efficient movement of the product. In this respect, A.I.D. will continue its efforts to obtain the cooperation needed from U.S. shipping companies and the GRZ to provide through bills of lading from U.S. ports to designated locations within Zambia.

The comments made in the GAO draft report indicating that A.I.D. has financed the movement of an entire year's supply of fertilizer at one time are not accurate. A.I.D.-financed fertilizer shipments to Zambia usually move over at least a two month period and are structured in quantities sufficient enough for full shiploads. Manufacturing costs are understandably less when large quantities are involved. Shipping costs are lower and ship availability is greater when full shipload quantities are used.

We agree that fertilizer shipments spaced more evenly throughout a full year would be ideal. However, the Government of Zambia logistic capabilities are extremely limited with the fertilizer procurement also subject to our USG restraints resulting from the aforementioned apportionment process and preference given to the U.S. domestic market. Most importantly, what is now needed is a single organization within the GRZ structure charged with management of the procurement, transport, marketing and supply of fertilizer as recommended in the Fertilizer Supply and Distribution report. A.I.D. will work with the Government of Zambia and other donors to facilitate the establishment of such an entity as a critical part of our continuing efforts to improve the supply of fertilizer to Zambia.

Specific comments on the draft report were provided by our Mission in Zambia: (1) In the fall of 1981, an FSN was assigned to prepare detailed monthly reports from input provided by the GRZ and relevant freight forwarders on the arrival of CIP commodities in East London and Livingstone. These reports were made available to the GAO team in Zambia but were not mentioned in the draft report, (2) It is not correct that the USAID staff was unaware that fertilizer raw materials were stored at Nitrogen Chemicals of Zambia (NCZ) for more than one year; this awareness is reflected in an internal Mission memo on this subject. The Mission notes an inspection trip to the storage site would have been scheduled with or without the GAO's team presence. Further, the Mission had understood that the justification given by NCZ for the material storage was considered satisfactory by the GAO team leader, (3) A prime problem in effective monitoring is the dilemma of inadequate Mission staff and, (4) The Mission has requested that in the future the NCZ provide evidence of a contract for inland freight before the Mission will agree to finance the ocean freight.

In sum, we agree in principle with the report's recommendation requiring more specific pre-implementation planning for CIPs which would also provide for modifying plans when established milestones can no longer be reasonably met. As previously stated, in the case of Zambia, the GRZ Fertilizer Supply and Distribution report will be a valuable management tool in this effort. We emphasize our request that the GRZ report be reviewed by the GAO and the complexities inherent in fertilizer procurement for Zambia be recognized in the final report. These complexities will limit our efforts to improve pre-implementation planning and subsequent modification of planning until relevant improvements are made by the Government of Zambia in their procurement of fertilizer.

CHAPTER 3

Inadequate Internal Controls over Commodity Transactions Lead to Waste and Improper Expenditures

Chapter 3 of the draft audit report contains four recommendations. We agree in principle with two of the recommendations, those which relate to increasing audit coverage and revising letter of commitment language. Actions are well underway which will improve procedures in these areas. We believe one of the other recommendations, calling for a change in the office location of the audit function, is premature, but we support a further study of this change by the A.I.D. Administrator. We do not believe another recommendation, designed to prevent deviations from procedures under direct reimbursement, is sustained by the underlying narrative. We request that the report be revised in a number of important specific respects where facts or language do not correctly or fully explain the internal controls over commodity transactions which are in place..

Insufficient Reviews Contribute to Improper Payments

Commodity transactions are vulnerable to waste, loss and unauthorized expenditures

We disagree with:

- On page 16, the statement, summarizing the voucher review procedure, that A.I.D.'s Surveillance and Evaluation Division approves in advance payments requested for commodities under direct letters of commitment and issues bills for collection for ineligible payments made by A.I.D. under the bank letter of commitment system.

  The statement implies that under direct letter of commitment procedures, a full and complete review is accomplished thus obviating any possible need later for issuing bills of collection for ineligible payments. In practice, to effect prompt payment, our Surveillance and Evaluation Division quickly reviews supplier vouchers and supporting documents and approves payment by our Office of Financial Management. Such a document review

GAO note: Page references in this appendix refer to our draft report and may not correspond to page numbers in the final report.

may largely suffice for certain high value bulk shipments formally competed where the documents include independent inspection certificates of chemical analyses, weight surveys, etc., but it is not sufficient for many other, more complicated transactions. While payment in these cases is approved, AID does not and could not complete its audit. If irregularities are discovered later, bills of collection are necessary. The GAO statement also implies that, under bank letter of commitment, A.I.D.'s only protection against ineligible payments is the issuance of bills for collection after the fact. This is not entirely correct since the Form 11 review discussed below provides A.I.D. an opportunity for reviewing transactions for commodity eligibility before payment.

Revision requested: That the footnote descriptions of A.I.D.'s payment procedures on page 16 be substituted for the statement noted above with which we disagree.

We also disagree with:

- On page 16, the statement, "However, only a small part of commodity vouchers /presumably commodity program vouchers/ are reviewed by A.I.D.'s Surveillance and Evaluation Division either before or after payment to suppliers," and

- On page 17, the subsequent more precise statement that our Surveillance and Evaluation Division" reviews a total of only about 12 percent of all commodity transactions."

  The estimate is based on numbers of vouchers. The next two paragraphs of the report acknowledge that the value of transactions reviewed in 1982 was $252 million under Direct Letters of Commitment plus some unrecorded amount under bank Letters of Commitment. The value of transactions reviewed should be compared to the total of disbursements for CIP programs in 1982 which, according to reports by our Office of Financial Management, was $364 million. Thus, while we may have reviewed only 12% of the vouchers received, those we reviewed represented as much as 70%, perhaps more, of the value of all CIP transactions.

Revision requested: That the report acknowledge this higher level of CIP coverage measured on a value basis.

We disagree with:

- On page 17, the statement, "Particularly susceptible to errors are commodity ocean freight transactions which amount to an estimated $175 million annually, and transactions under bank letters of commitment -- A.I.D.'s most often used method of financing."

  We do not know the source of this statement and question its validity. According to data compiled by our Transportation Support Division from reports by our Office of Financial Management, A.I.D. financed ocean freight payments totalling $74 million in FY 1981, $59 million in FY 1982 and $84 million in FY 1983. These amounts include project as well as CIP assistance.

  The report does not acknowledge that under present procedures (as required by law) A.I.D.-financed ocean transportation bills of lading are audited by the General Services Administration for conformance with tariffs on file with the Federal Maritime Administration. Also it is doubtful, in view of statistics discussed above, that bank letters of commitment are our most often used method of financing - at least for CIP. We discuss later the relative susceptibility to errors of bank letters of commitment versus direct letter of commitment transactions.

Revision requested: That the report delete the statement which is not supported and, we believe, incorrect.

We disagree with:

- On page 18, the statement that, in FY 82, A.I.D. certifying officers processed over $1.6 billion in bank letter of commitment vouchers for commodities and related services.

  This information is not correct. It is attributed to A.I.D. IG and likely comes from a statement on page 2 of A.I.D. IG Memorandum Report No. 0-000-83-66 (either the draft of March 1983 or the final version dated May 27, 1983), "Savings In Bank Charges Possible If A.I.D. Enforces Its Payment Procedures". The quoted figure, $1.6 billion, covers more than just commodities and related services; for example, it includes payments for technical assistance services totally unrelated to commodities and payments to private voluntary organizations for freight costs incurred under PL 480 Title II programs.

Our records don't divide the payments made under bank letter of commitment procedures into categories of assistance, but we estimate that not more than half could have been for commodities and commodity-related services other than under PL 480. Moreover, not all of the payments which were for commodities and commodity-related services applied to CIP; a substantial portion applied to projects.

Revision requested: That the report delete the statement.

More audit coverage could result in bigger savings

A.I.D. actions to increase audit coverage

Several statements in the report imply criticism of A.I.D.'s using bank letters of commitment (and post audit) as opposed to direct letters of commitment (and preaudit) or otherwise suggest dissatisfaction with bank letter of commitment procedure.

We disagree with:

- On page 18 - the statement, "None of these ($1.6 billion in) transactions was subject to audit by A.I.D. prior to payment, and post audit is done on a test basis only. In contrast, the direct letter of commitment method permits A.I.D. to review the documentation for compliance with statutory and A.I.D. regulation before making payment," and
- On page 19 - the statement, "Also, A.I.D. IG has reported improper payments in millions of dollars and pointed to other potential savings through elimination of bank charges," and
- On page 20 - the statement, "In a May 1983 report, the IG noted that A.I.D. has no effective system for auditing bank letter of commitment vouchers to assure that payments are proper. The prepayment review of the A.I.D. certifying officer in New York is limited to a

quick check of documents and is made under great time pressure," and

- On page 18 and 19 - Several references to the inadequacy of internal controls which also suggest dissatisfaction with bank letter of commitment procedures.

The basis for the report's statements or attitude appears to follow from the draft of A.I.D. IG Memorandum Report No. 0-000-83-66 of March 1983, Savings In Bank Charges Possible If A.I.D. Enforces Its Payment Procedures."

We would first point out that management comments to the draft of that report dissuaded A.I.D. IG in its final version of the report dated May 27, 1983 from including the three recommendations for changes in procedures which it initially intended. We do not believe that our present procedures are so flawed or inadequate as your report implies.

A.I.D. reviews all CIP transactions for commodity eligibility before making payment. We require that commodity suppliers submit information about the commodities they intend to furnish on an Application for Approval of Commodity Eligibility (AID Form 11). The approved form must be submitted along with other required documentation for payment under either direct letter of commitment or bank letter of commitment procedures. This prior review of all transactions is done in the Commodity Procurement and Support Division, a sister division to the Surveillance and Evaluation Division. It is an important and effective control in managing CIPs. Disallowances occur not only as a result of preaudit by our Surveillance and Evaluation Division. Form 11 reviews and document reviews by banks also result in disallowances, but we do not record their number or value.

We believe that balanced use of both direct letters of commitment and bank letters of commitment, as appropriate, makes the most effective use of available resources and best protects the interests of the USG. Bank letter of commitment procedures transfer to the banking community some of the paperwork burden that would be required to issue individual letters of credit and amendments for a multitude of transactions. This represents contracting work out to the commercial banking community, work for which it must be paid but which permits A.I.D. to operate with fewer federal employees.

Timely payment considerations and legal considerations do not permit a fully adequate audit of direct letter of commitment transactions before payment. A review of documents is all that is possible. But a more careful and thorough review, which is possible only on a post audit basis, is necessary to reveal many kinds of irregularities. In this respect, direct letters of commitment and bank letters of commitment are subject to the same limitations.

Revision requested: That the report more accurately describe A.I.D.'s review system (including the Form 11 review) and that it recognize the advantages of balanced use of the different methods of payment.

We also disagree with certain general statements in this section:

- On page 18 - "Serious questions have been raised in the past by GAO and A.I.D. IG regarding adequacy of internal controls over commodity payments." - If there are specific questions not covered in the report and not answered previously we would like to know what they are so we can respond and take action if necessary.

- On page 18 - "Available evidence indicates that improper billings can reach into millions of dollars annually." - If this is a general statement covering the last paragraph in the section, we would point out, as discussed above, that the $1.6 billion estimated universe is not accurate. Moreover, we do not believe that extrapolation of a 0.7 percent error rate is a valid basis to estimate additional recoveries. Among other things, the law of diminishing returns will come into play.

- On page 19 - "Also, A.I.D. IG has reported improper payments in millions of dollars..." This may be referring to the case mentioned in A.I.D. IG Audit Report 83-34 dated December 30, 1982. "Irregularities in the Financial Management of the Ashuganj Fertilizer Plant Project in Bangladesh". If so, we believe it is significant that these irregularities were uncovered not as a result of preaudit of vouchers under direct letter of commitment procedures but rather in post audit reviews by our Surveillance and Evaluation Division under bank letter of commitment procedures. Bills for collection were held up pending resolution of criminal proceedings, but they have now been issued.

As the report indicates (on pages 18 and 19), we are aware that CIP programs are vulnerable to abuse and stated our concern in the assessment called for by Office of Management and Budget Circular A-123. The actions we are taking as a result of our assessment are discussed later; they evidence our determination to deal with the issues raised.

Revision requested: That the provocative or inadequately supported comments be deleted and the text suggested below be substituted on pages 19 and 20.

We appreciate the report's acknowledgement (on pages 19 and 20) of our efforts to increase the number of transactions we audit. Nevertheless, we believe the report should more accurately indicate what we are doing and our expectations. The draft text does not fully or correctly describe the emphasis placed on increasing audit coverage by our Office of Commodity Management including the progress which has been made and plans well underway for reaching, during next year, an appropriate level of coverage.

Revision requested: Substitute the following text for the paragraphs on page 19 and 20 of the report.

"To achieve greater efficiency and expanded coverage in the voucher audit process within tight direct-hire personnel limits, A.I.D. contracted in November 1982 with a private firm to provide voucher review services. While the major reason for the contract was to expand audit coverage, A.I.D. also anticipated that the contractor's work would result in the issuance of bills for collection and some greater recovery of A.I.D. funds improperly claimed by suppliers. Initially the firm was given a target of reviewing on a post audit basis 2,000 commodity vouchers which had been paid during fiscal years 1980, 1981 and 1982 for both CIP and project activities and under both direct letter of commitment and bank letter of commitment procedures. The firm has questioned payments of about $1.6 million. However, in reviewing a sample of these questioned payments, A.I.D.'s Surveillance and Evaluation Division has found that most of the questioned payments were automatically put in that category not because they were found to be improper but because the firm was not able to obtain all the documents and information to confirm the validity of the payment. Other payments, though questioned, have proven to be proper. Thus, the value of any refund claims will likely be small.

"A.I.D. is now planning a new one year contract with the same firm under approved noncompetitive selection procedures for minority-owned firms including an option to extend for another year. Funding in the first year will be at a level 30% higher than the contract which ends in December 1983. A.I.D. believes that this will permit a substantial increase in the firm's level of effort and, with the experience vested in the firm from the prior contract, will enable 2,000 vouchers to be reviewed in CY 1984. The vouchers reviewed will be those paid in fiscal year 1983 for both CIP and project activities and under both direct letter of commitment and bank letter of commitment procedures. A.I.D.'s Office of Commodity Management estimates that the review of these vouchers will bring voucher review coverage to 35% or more of the estimated 5,500 commodity vouchers paid during the fiscal year. Moreover, the Office of Commodity Management expects that the value of vouchers audited, combining the contractor review and the Surveillance and Evaluation Division in-house voucher review, will be well over 60% of the estimated FY 83 transaction value of about $700 million. This will be achieved by using sampling techniques which will maximize review of high value transactions (e.g. grains, fertilizer and transportation equipment). A.I.D. believes these targets are feasible and, if reached, will provide an appropriate level of audit coverage and likely result in bigger savings."

Change in procedures could further improve internal controls

The voucher audit function should be outside the Office of Commodity Management

On pages 28-30, the report puts forward a rationale for relocating the voucher audit function outside the Office of Commodity Management but acknowledges that questions of practicality and cost effectiveness dissuaded A.I.D. IG several years ago from making specific recommendations for relocation.

We believe other arguments can be made from keeping the function in its present location, e.g. closer cooperation between Form 11 reviews and voucher reviews. Contrary to the implication in the report, neither the director, nor any employee of the Office of Commodity Management controls the preprocurement actions or procurement itself. These actions are the responsibility of host country importers with A.I.D., in various locations and at various stages depending on the nature of the procurement, reviewing and approving those actions. All of the Office of Commodity Management and other organizations in A.I.D., not just the Surveillance and Evaluation Division, assume a responsibility to assure that improper transactions are not financed.

The Office of General Counsel comment mentioned in the last paragraph on page 29 was given as the last of a series of four "thoughts on Agency price review procedures" in a memo dated December 14, 1981 from Kenneth E. Fries to Stan Nevin (copy attached). It reads "Perhaps the Agency should consider the integration of commodity price review and payment functions which are now handled separately by SER/COM/SE and FM/BFD." It makes no mention, much less recommendation, as to the location (in SER/COM, in FM or elsewhere) of any such integrated operation. Although we doubt that the present organizational arrangement compromises the integrity of our operations, we nevertheless do recognize that there may be arguments both for and against a relocation.

<u>Revision requested</u>: That the report acknowledge that there are pro and con arguments and propose further study to analyze the various options and recommend action.

<u>Unclearly communicated requirements contribute to delayed or improper payment to Commodity Suppliers</u>

We disagree with the entire discussion under this heading because it is not entirely accurate and does not, as we believe it should, acknowledge the work we are doing as follow-up to our vulnerability assessment which was called for by Office of Management and Budget Circular A-123.

Revision requested: That this entire section be replaced by language essentially as follows:

"Incomplete documentation submitted by commodity suppliers impedes prompt and efficient processing of payments and auditing by A.I.D. In its vulnerability assessment called for by Office of Management and Budget Circular A-123, A.I.D. identified inadequacies and inconsistencies in its own financing documents as contributing to this problem. In August 1983, it chartered a committee chaired by its General Counsel with members from the Office of Financial Management and the Office of Commodity Management to deal with the problem. As a first step, the committee intends to establish specific requirements for the issuance of standardized financing documents (letters of commitment) throughout A.I.D. The committee will also study other commodity procurement issues and recommend steps to strengthen internal controls where needed."

"A.I.D. IG noted (in its Memorandum Audit Report No. 0-000-83-66 dated May 27, 1983) that prepayment audit of suppliers' vouchers is needed to maintain sound internal controls, and such procedure is allowed by A.I.D. regulations. Management comments, noted in the report, stated: "The idea that, under any system, this Agency could perform a full audit prior to each payment and do so within any acceptable time frame--under either the Prompt Payment Act or good commercial practice--is not within the realm of practical reality".

Supplementary Revision requested: For similar reasons, correcttion is necessary of the unqualified statement on page 18 that the direct letter of commitment method permits A.I.D. to review documentation for compliance before payment.

We have the following comments to the four recommendations in this chapter:

Recommendation: that the A.I.D. Administrator increase coverage of commodity transactions financed under bank letters of commitment.

Comment: As described in our comments above on the narrative of the report, we are well along in accomplishing a major increase in audit coverage of all CIP transactions, under both bank and direct letters of commitment.

Recommendation: that the A.I.D. Administrator establish appropriate controls, such as review and approval at the Assistant Administrator level, for preventing deviations from procedures whenever commodities are financed under the direct reimbursement method.

Comment: We do not believe that the narrative section of the report supports such a recommendation. In the Sudan case, the only direct reimbursement situation discussed in the report, the procedure was authorized by the then Assistant Administrator for Africa, F. S. Ruddy. Please see copy of cable, State 190791 dated 10 July 1982, attached.

Recommendation: that the A.I.D. Administrator transfer the commodity voucher audit function from Office of Commodity Management where its degree of independence would be enhanced.

Comment: As discussed in our comments on the narrative of the report, we urge that the recommendation be recast to provide that A.I.D. study this question.

Recommendation: that the A.I.D. Administrator require responsible officials to issue letters of commitment in appropriate standard language which would inform and bind suppliers to A.I.D. requirements.

Comment: As described in our comments above on the narrative of the report, we are already taking action in the context of our work under Office of Management and Budget Circular A-123 to improve language in our letters of commitment.

CHAPTER 4

Chapter 4 of the draft report concerns commodity arrival and disposition accounting.

USAID/Zambia commented on the statement on page 39 of the report that it did not require arrival accounting reports from the Zambian government. USAID/Zambia acknowledges that it had not required these reports on a continuing basis. However, starting in the fall of 1981 with the hiring of a foreign service national, USAID/Zambia has prepared monthly reports, based on information supplied by Namboard, Nitrogen Chemicals of Zambia, and the relevant freight forwarder, of the arrival of CIP commodities in East London and Livingstone. These reports include information on shortlandings, damages, and losses enroute. USAID/Zambia believes that it is well informed on the status of commodity arrivals from the fall of 1981 onwards. It advises that this information and supporting materials were made available to the GAO team. We request that the report acknowledge this.

The GAO recommends that the A.I.D. Administrator:

- issue specific guidance to A.I.D. Missions on monitoring the implementation of commodity import programs, including the arrival accounting and disposition of commodities, and

- ensure that missions comply with established monitoring requirements.

The current Agency Handbook guidance on CIP monitoring, arrival accounting and end-use checks is written in general terms because the various systems of host country governments differ widely - as do their laws, procedures, and mechanisms for commodity imports. The Agency believed that the general Handbook guidelines would provide the necessary flexibility for each mission to determine the most appropriate monitoring systems for its special set of circumstances. However, as the draft report points out, the general guidance has proven insufficient in many cases. We, therefore, will amend the Handbooks to indicate minimum standards and suggested examples of arrival and end-use accounting systems.

Some guidance concerning CIP arrival accounting is included in our Payment Verification Policy Guidance which was sent to the field this month. In addition, we are requiring each mission with a CIP program to report to A.I.D./W a detailed description of the systems to be used. This report will be reviewed in A.I.D./W and suggestions for improvement (if any) will be forwarded to each mission.

A.I.D. staffing limitations, which in part led us to emphasize host country responsibility for arrival accounting in the first place, have continued to handicap our monitoring efforts. We agree with the suggestion that we supplement our own capabilities when necessary by hiring contractor assistance. In fact the Payment Verification Policy Guidance mentioned above encourages USAID's to make greater use of local CPAs and contract personnel.

CHAPTER 5

Chapter 5 of the draft report concerns local currency.

We question the mention (bottom of page 53) of Zambia as one of the places where the mission did not receive required reports on local currency deposits. The Zambia CIP is loan funded and therefore the FAA Section 609(a) requirement that local currency proceeds be deposited in a special account does not apply. We request that Zambia be deleted from the countries named in that sentence.

The GAO recommends "that the A.I.D. Administrator:

- issue guidelines to the geographic bureaus on the accounting for the generation of local currency proceeds resulting from the sale of A.I.D.-financed commodities, consistent with the intent of Section 609 of the Foreign Assistance Act and A.I.D. bilateral agreements and

- issue appropriate guidance on monitoring the use of local currency generated from the sale of commodities."

AIDTO Circular A 222 of 6/23/76 is the most recent policy statement on A.I.D. participation in the programming of local currency proceeds generated from both A.I.D.-financed commodity imports (CIPs) and PL 480-financed commodity imports (food aid). While this policy statement provides guidance on monitoring the use of local currency generated from the sale of commodities, it contains no guidance about establishing special accounts in compliance with Section 609 of the FAA. Also, it does not discuss in detail: (a) what types of procurements (and associated local currency generations) are covered; (b) what basis should be used for determining the amount of local currency generated; (c) what the local currency should be used for; or (d) what A.I.D.'s responsibilities are for monitoring the use of the local currency. Essentially, it states that A.I.D. requires Mission examination of the merits of more active A.I.D. participation in the programming of local currencies and encourages its use as another aid tool in those countries where it promises to be effective.

Policy Determination No. 5 (PD-5) of 2/22/83 is a more recent policy statement on this subject. Although it specifically covers only the local currency proceeds generated from PL 480 Title I food aid, much of its guidance can be usefully applied to CIP generations. PD-5 reinforces the 1976 guidance by stating that Agency policy explicitly encourage A.I.D. participation in the programming of country-owned local currency generated by the sale of PL 480 Title I commodities when such involvement promises to help in achieving developmental objectives. It provides guidance on accounting for Title I local currency generations as well as on programming these generations.

Specifically, it summarizes the salient elements of Article II-F of Part I of all Title I agreements which indicates the amount of local currency that must be used to support economic development objectives; the appropriate exchange rate to be used to determine the amount of local currency available; that an annual or more frequent report must be submitted to the U.S. indicating how the local currency was used; etc. The Food for Peace Office in the FVA Bureau is responsible for monitoring compliance with Article II-F.

PD-5 also provides programming and monitoring guidance with respect to Title I local currency generations. For example, it states, inter alia, that "Missions and the host government should agree on the specific uses of the sales proceeds as well as on appropriate policy reforms as must as possible before the Title I agreement is signed;" that "The specific activities which will be funded with the local currency and the specific amount of funding available for each activity -- as well as specific activities that will not be eligible for funding -- should be explicitly stated;" that "The Mission should systematically monitor the recipient government's overall budget allocation decisions;" that "Missions should consider using the sales proceeds to support activities implemented by private voluntary organizations. . .and should also encourage expansion of the private sector."

However, we would need to advise Missions that special accounts must be established in the case of CIPs that are grant financed, while special accounts are not required under loan-financed PL 480 Title I agreements.

PPC is currently drafting guidance concerning the preparation and submission of Mission plans for the use of CIP and PL 480 local currency generations. This guidance message might be an appropriate vehicle for providing guidance to Missions in response to the GAO recommendations.

Finally, PPC and FVA prepared a questionnaire in 1983 asking Missions to report on how local currency generated from the sale of Title I food aid and CIPs had been allocated. We intend to update this information annually.

CHAPTER 6

Chpater 6 of the draft report concerns evaluation. The GAO recommends "that the A.I.D. Administrator:

- direct the Office of Evaluation to establish a requirement for evaluating CIP assistance and develop specific guidance to those performing such evaluations."

The GAO is correct that A.I.D. has not issued guidance for evaluating nonproject assistance, of which CIPs are one instrument. We expect to have a report by the end of calendar year 1983 identifying the array of non-project assistance activities of the Agency and how they are being evaluated.

A.I.D. Handbook 4 on Nonproject Assistance was completed in 1975. The Chapter on evaluation (Chapter 9) remains "reserved". Before we proceed with preparing evaluation guidance, a review will be undertaken by our Bureau for Program and Policy Coordination as to the adequacy and relevance of Handbook 4 to present circumstances. During fiscal year 1984, the Africa and Near East Bureaus plan to evaluate several CIPs. The experience so gained will help shape Agency evaluation guidelines for CIPs.

(472014)

*U.S. GOVERNMENT PRINTING OFFICE : 1984 0-421-843/215

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