



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

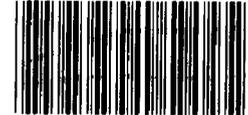
~~25092~~  
~~#8573~~  
118602

INTERNATIONAL DIVISION

June 2, 1982

B-206204

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



118602

Dear Mr. McPherson:

Subject: Managing Host Country Contracting  
Activities (GAO/ID-82-42)

We have examined aspects of Agency for International Development-financed project activities implemented under contracts awarded by the host countries. We identified issues which we believe should be brought to your attention. We found that

- a centralized inventory of host country contracts, as directed by AID management in 1977 and again in 1979, has not been developed;
- the idea of a centralized inventory has all but been abandoned and a substitute data system has not been established; and
- AID overseas missions have continually ignored the requirement to provide certain data on host country contracts to AID/Washington.

We believe that certain actions are needed to correct identified management weaknesses and improve AID's operational capabilities. Information on host country contracts would (1) assist AID managers in general oversight and policy examination, (2) enable AID to readily inform the Congress and the general public on foreign aid contract expenditures and how they benefit the United States, (3) assist auditors in obtaining more complete audit coverage, and (4) provide a basis for exchanging contract cost information and serve to alert AID officials on problem contractors. When you complete the study of host country contracting problems requested by the Senate Appropriations Committee in its November 1981 report, you may determine that further actions are needed to improve internal control and oversight of these activities. (See enc. I.)

(471991)

022 323

This letter contains recommendations to you on page 11. We have discussed these matters with AID officials who have responded to us with indications of positive actions that are to be taken on our recommendations. (See enc. II.)

As you know, Section 236 of the Legislative Reorganization Act of 1970 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 this report to the Chairmen of the four above-mentioned committees; to interested House and Senate authorization committees, and to the Director, Office of Management and Budget.

Sincerely yours,

  
Frank C. Conahan  
Director

Enclosures - 2

MANAGING HOST COUNTRY CONTRACTING  
ACTIVITIES

BACKGROUND

In 1976, the Agency for International Development (AID) instituted a policy that developing countries will, to the extent they have the capability to do so, implement AID-financed projects. The majority of project activity is carried out under contracts, entered into either directly by AID or by the host country implementing agencies. The latter are generally referred to as "host country contracts."

Since its inception, the host country contracting policy has been modified to allow AID more flexibility in choosing whether or not, in given circumstances, it is appropriate to implement projects under the host country contracting mode. The latest change occurred in February 1982, allowing overseas missions to increasingly use the AID-direct contracting approach.

Presently, AID does not collect data on host country contracts and, therefore, does not know how many host country contracts exist or how much of the foreign assistance dollar is spent in this manner. AID estimates that it funded about \$1 billion in host country contracts in each of fiscal years 1980 and 1981.

Although a host country contract is a contractual obligation between a host country agency and a contractor, AID retains certain managerial responsibilities even though it is not a party to the contract. AID procedures clearly state that greater reliance on host country implementation of projects does not relieve AID from the responsibility to approve contract transactions and to monitor the progress of the contracted work. This responsibility has been assigned to AID's four regional bureaus and, in turn, delegated to overseas missions. Thus, any information on these contracts usually originates and is available only at these missions.

OBJECTIVES, SCOPE, AND METHODOLOGY

We examined AID accountability processes and procedures for providing reasonable assurances to the Congress and within AID that host country implemented project activities are carried out economically and efficiently. We selected this area for examination because of the significant expenditures and problems observed by AID auditors in reviewing host country contracting activities.

Our work was performed principally by reviewing AID procedures and practices, examining records, and by interviewing AID officials in Washington, D.C., and at AID missions in the Philippines and Bangladesh during January and February 1982.

Information developed by the AID Inspector General (IG) on host country contracting activities was also used in identifying areas of concern.

WHY AID NEEDS INFORMATION  
ON HOST COUNTRY CONTRACTS

In 1977, AID established a requirement to collect data on host country contracts. This requirement was never implemented and, AID management, acting on its Procurement Policy Advisory Panel's recommendation, no longer supports the idea of a central inventory for host country contract information.

AID regional bureaus, which were subsequently given the responsibility for establishing their own contract reporting requirements, have not implemented a substitute reporting system to ensure that missions report all host country contracts. AID still does not have ready access to information on host country contractors implementing economic assistance projects and does not know how much money (estimated at about \$1 billion annually) is expended for these activities, principally because there is no centralized inventory of host country contract information in Washington.

Longstanding requirement to collect  
data on host country contracts

In March 1977, the AID Administrator directed that regional bureaus and missions establish procedures to ensure that copies of all direct- and AID-financed project contracts and grant agreements be submitted to the Bureau for Management, Office of Contract Management, where a centralized file and data bank would be established and maintained. The purpose of establishing a central point for recording and keeping track of all AID-financed contracts was to overcome AID's recurring problems in reporting such activities to the Congress and within AID. In December 1977 and in January 1979, AID reminded the missions of the requirement to provide data on host country contracts for input into a computerized contract information system in the Office of Contract Management.

In May 1979, the AID IG reported that a centralized control system of host country contracts had not been established and that the missions do not have a readily available record of such contracts. The IG recommended that a uniform numbering system and an inventory of all host country contracts be established so that information on contractor overhead rates can be disseminated to missions, host country agencies, and auditors. Again, in August 1979, AID acknowledged a need for a centralized inventory of host country contracts and directed the missions to provide copies of host country contracts to the Office of Contract Management.

A centralized inventory has  
not been established

AID has not developed a centralized inventory of host country contracts and still lacks data on such contracts. In fact, the requirement has been abandoned in the process of revising AID's procedures for host country contracting. As a result of this change, AID regional bureaus in October 1981 were given the responsibility for establishing their own host country contract reporting requirements. This system had not been established by April 1982.

We found in February 1982 that AID missions in the Philippines and Bangladesh did not report host country contracts to AID Washington because they were not aware of the requirement. Mission officials said they manage activities on the basis of projects and had no need for data on contracts. Furthermore, there was confusion at the missions on whether contracts for commodities and construction would be considered as host country contracts. AID regional bureau management had not taken steps to ensure that missions provide contract information to AID Washington.

Office of Contract Management personnel told us there was insufficient staff to handle the extra workload required to establish and maintain a centralized inventory of host country contracts. Furthermore, many of the contracts sent to Washington by the missions were in foreign languages, making it impossible for AID personnel to extract the necessary data. Some missions have sent copies of host country contracts to the Office of Contract Management but the contracts have been merely accumulating.

Bureau for Management personnel felt that missions would continue to ignore the reporting requirements unless the regional bureaus find a means for ensuring compliance. For this reason, the AID Procurement Policy Advisory Panel approved a change in procedures in 1980 allowing the regional bureaus to establish their own reporting requirements for host country contracts. This position is reflected in the revised Handbook 11, which states:

"The Mission will inform the Contracting Agency how many copies of the final executed contract and amendments are to be submitted to AID. The Regional Bureau shall advise the Mission of AID/W distribution requirements."

The revised Handbook 11 was approved by the AID Administrator effective October 1, 1981.

Benefits of having contract information

Information on host country contracts--a significant segment of AID's foreign assistance expenditures--could improve AID's operational capabilities. It would

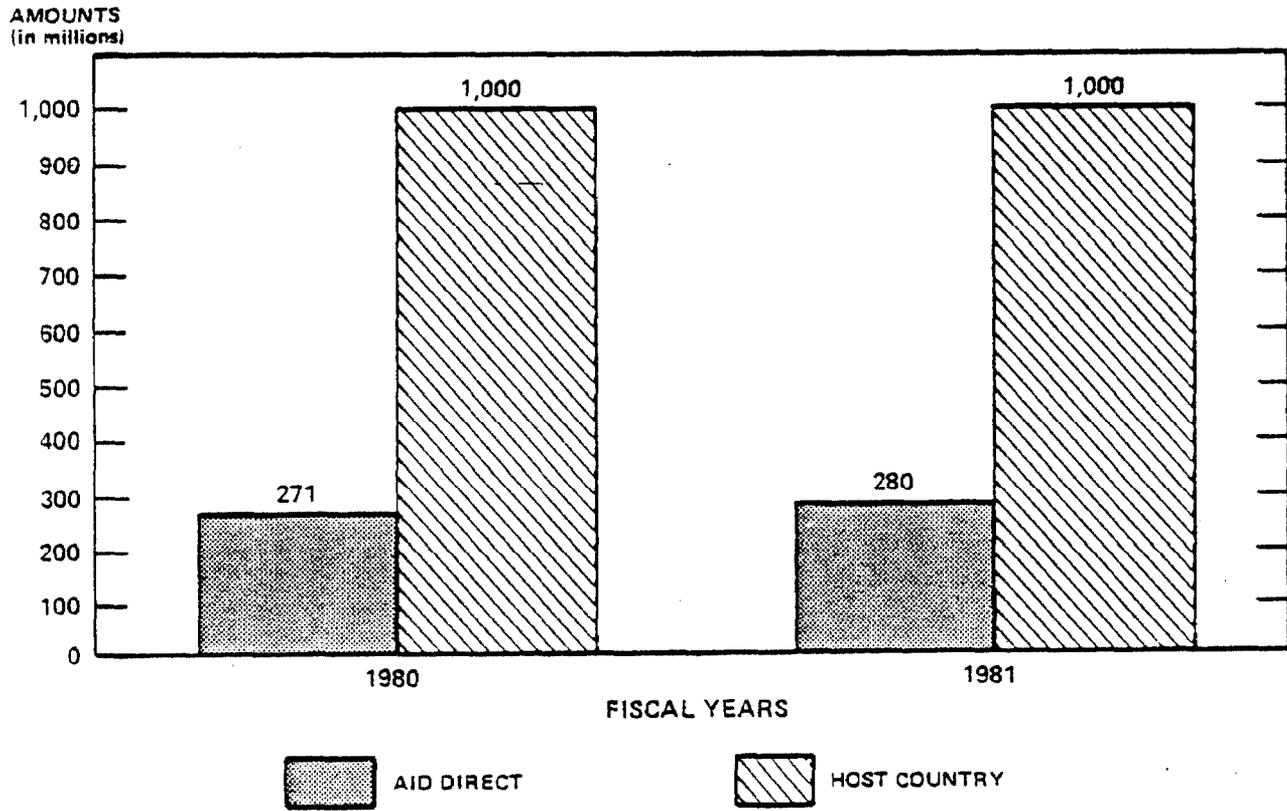
- enable AID to readily inform the Congress, AID managers, and auditors on contract activities;
- assist in evaluating the impact of host country contracting policy;
- assist in obtaining more economical and efficient audit coverage; and
- provide a basis for exchanging contract cost information and serve to alert AID officials on problem contractors.

The Congress needs information on AID expenditures

Considerable interest has been expressed by congressional committees and individual Members of Congress on AID funds expended for host country contracts. For example, in October 1981, the House Government Operations Subcommittee on Legislation and National Security and, in March 1982, the Senate Committee on Appropriations asked AID to provide information on host country contracts. AID's reply was it does not collect such information because it would not assist in project management responsibilities.

Similarly, Members of Congress often express interest in foreign aid expenditures benefiting their districts and States. AID accumulates this information on most AID-direct contracts but generally not on host country contracts. As the following chart shows, funding for host country contracts is estimated to be more than three times the funding for AID-direct contracts. Together, AID-direct and host country contract funding in fiscal year 1981 was estimated at \$1.3 billion. This is over one-third of the \$3.6 billion total AID economic assistance appropriation for that fiscal year.

### VALUE OF CONTRACTS AWARDED BY AID AND HOST COUNTRIES



Host countries award contracts to local, third-country, as well as U.S. contractors. Because AID could not estimate the amount of host country contracts awarded to U.S. contractors, information on a major segment of its foreign aid expenditures was not available. The effect of this is illustrated by the following example.

In fiscal year 1980, a host country agency awarded a contract for \$5.2 million to a U.S. contractor based in New Jersey. AID's news release on foreign aid expenditures for that fiscal year showed that AID negotiated technical service contracts totaling \$11.3 million with New Jersey universities and other private institutions. The contract for \$5.2 million was not included in this total, thus understating the amount of U.S. foreign aid accruing to U.S. firms in New Jersey by 46 percent in this instance.

We were told that in recent months AID has been under increasing pressure from Members of Congress to provide information on contract awards and expenditures. Because AID lacks a system or a single point for recording and keeping track of all AID-financed contracts and grants, AID has had recurring problems in responding to these inquiries.

For example, in July 1981, AID directed all missions to report promptly all AID-financed direct and host country contract, grant, and cooperative agreement awards over \$100,000 for congressional notification and public relations purposes. In March 1982, AID notified the missions that relatively few notifications have been received and, those that were sent, came too late to carry out public relations objectives.

To illustrate further, in February 1982, we asked AID to provide an estimate of the number and dollar value of current host country contracts financed by AID. We were told this information could be obtained from AID missions. However, AID missions in the Philippines and Bangladesh did not have a list of all host country contracts and could not readily provide such information. Moreover, as of May 1982, AID had not responded to our request for information on host country contracts.

AID officials told us in May 1982 that efforts are underway to improve the reporting of grant and contract awards. This action is being taken at the suggestion of the Senate Foreign Relations Committee staff on the belief that more complete information on foreign assistance expenditures would result in greater support for these programs by the American public.

#### Evaluation of host country contracting policy

Lack of data on host country contracts also affects AID's ability to evaluate the success of its host-country contracting

policy. Since its inception in 1976, the policy has been modified to allow missions more flexibility in deciding whether or not host country contracting is appropriate in given circumstances. These modifications had been made primarily based on complaints by missions and university contractors and IG findings, rather than on the basis of statistical information, such as trends in the number of contracts and the amount of expenditures. Such information simply has not been available for determining whether the policy has a desirable impact on the implementation of foreign assistance programs.

#### Scheduling of audits

Although AID is not a party to host country contracts, it has the right to audit and examine records of such contractors. However, the AID IG has noted that lack of information hampers AID auditors in carrying out their responsibilities and, in recent years, has attempted to improve audit coverage of host country contracts. For example, in September 1980, the IG informed AID management that without a listing of host country contracts it is extremely difficult to prepare an audit plan and develop an efficient and economical means for ensuring adequate audit coverage. He said that sound management and good internal controls make it imperative that AID has knowledge of the number and value of contracts it finances under loans and grants. AID management has ignored this need for information.

Other Government agencies, such as the Department of Health and Human Services and the Defense Contract Audit Agency, have audit responsibility over many AID-financed host country contractors. Lack of information on all contracts with an organization prevents AID from providing these agencies with appropriate information so that AID-financed contracts can be included in their audits. This is particularly important since many of the contracts contain provisional overhead rates that need to be finalized at the conclusion of the contracts. Moreover, results of audits of contractors need to be provided to all missions where contractors operate so that adjustments can be made worldwide on overhead rates based on one audit.

Our work at the missions disclosed difficulties in scheduling audits and finalizing rates. For example, in March 1980, the Bangladesh mission requested AID Washington advice on whether to accept a contractor's proposed overhead rate for 1979 which was needed for approving a contract amendment. In May 1980, Washington advised the mission that an audit of the contractor's overhead rate had been requested.

In July 1981--1 year later--Washington informed the mission that the Defense Contract Audit Agency would audit the contractor's 1979 rates. In April 1982, IG personnel told us that the audit of the contract was scheduled for that month. In

May 1982, the audit report had not been received by AID. Thus, 2 years after the initial request for the contractor's overhead rate audit, the information was not yet available, and payments under the contract continued on the basis of provisional overhead rates.

#### Need for contractor cost and performance data

AID officers are responsible for approving host country contracts and contract amendments. Project officers can ensure that contractor cost proposals are reasonable by checking and comparing files at other missions. Presently, AID is not in a position to advise missions of other host country contracts with the same firm because it does not maintain a list of such contractors.

AID project officers in Bangladesh told us that it is difficult and time consuming to obtain contractor cost data. AID's Office of Contract Management has responsibility for providing information to the missions on overhead rates for individual contractors. We found, however, it cannot always assist the missions with information requested.

For example, project officers in Bangladesh needed comparison of cost data for completing contract extension negotiations. In September 1980, the mission requested AID Washington to supply information on a contractor's indirect cost and compensation levels. Nearly 3 months later, the Office of Contract Management advised the mission that it had no information to provide and suggested that the mission contact another AID mission that has an ongoing contract with the contractor.

Also, AID needs information on contractor performance so that missions could be alerted of contractors with poor performance records. A list of contractors would allow notification of other missions having contracts with the problem contractors. Presently, AID does not have a readily available record of all contractors and locations where they perform services and has to obtain information on contractor performance from each mission.

#### Automation in AID offers choices for developing contract inventory

Currently, AID offices in Washington and in overseas missions are being automated to improve productivity and methods of handling information. This offers AID several choices for capturing data on host country contracts with relative ease and little additional cost.

Our analysis of AID's effort to develop an inventory of host country contracts indicated that previous attempts did not adequately consider several factors dealing with AID's organizational

structure and management attitudes. This experience should be useful now in designing an appropriate system for collecting and maintaining information on host country contracts.

Because the host country contracting activities are carried out at AID overseas missions, the key to the success in implementing a reporting system is the AID mission project officer who can provide the necessary contract data. Our discussions with mission officials and AID personnel in Washington indicated, however, that the project officers have not been convinced that information on host country contracts could contribute to better operations or serve public relations purposes. This belief has been reinforced by the lack of mission, regional bureau, as well as AID followup to ensure appropriate reporting on host contracts. Evidence suggests that this attitude has been the single most important cause for AID losing oversight in the host country contracting area.

Several technical aspects also added to the past difficulties in implementing a system of reporting. The requirement that copies of contracts be provided to Washington created problems in handling the often bulky documents and extracting necessary information from contracts in foreign languages. AID management did not advise the missions that selected data, rather than copies of contracts, are needed--although this was suggested by the AID IG in September 1980.

Also, the directives did not provide adequate guidance to the missions on what types of contracts and contractors should be included. We found that mission personnel had differing views on what constitutes a host country contract for purposes of reporting. Several officials told us they did not feel host country contracts for construction and commodities should be included. Others thought only contracts above a certain dollar limit awarded to U.S. firms should be reported. AID may decide that not all host country contracts need to be reported.

Assigning responsibility to the Bureau for Management for maintaining the host country contract inventory, placed the function outside the line-of-responsibility. The Bureau for Management personnel did not believe they could enforce compliance unless the regional bureaus were willing to lend full support. Subsequently, the responsibility for reporting contract data was placed in the regional bureaus.

Presently, several AID offices collect information on contracts and contractors. Copies of some host country contracts have been accumulating in the Office of Contract Management where information on AID-direct contracts is also maintained. The Office of Engineering in the Bureau for Science and Technology independently collects information from the missions and prepares periodic reports on architect-engineer and construction contracts,

including many host country contracts. AID auditors maintain lists of certain contractors for audit planning purposes. The Office of Financial Management has automated information systems on financial data.

Data on contract awards is being sought by the Office of Legislative Affairs. Thus, AID has several options for placing the function of collecting and maintaining data on host country contracts.

The additional cost of recording, transmitting, and maintaining basic contract data should be modest. Generally, an AID officer approves each host country contract or contract modification above \$100,000 prior to its award. Little time should be required for the project officer to prepare a brief data sheet of pertinent information when contract approval is given. To do it at any other time would be time consuming and inefficient. AID project officers are responsible for monitoring host country implemented project activities. It is a reasonable requirement that such officers would record and transmit contract data as a basic monitoring tool.

Similarly, once contract data is captured, duplication of effort in obtaining and maintaining this information could be avoided. For example, the collection of data on contract awards by the Office of Legislative Affairs may provide an excellent start for an inventory of key host country contracts. The regional bureaus in Washington are receiving computers to meet their management information needs. This automation may offer opportunities to capture and transmit contract data with ease and speed.

#### CONCLUSIONS

AID does not have adequate information on the number and value of host country contracts--a significant part of its foreign assistance expenditures. Even though a requirement was established in 1977, a central inventory of all AID-financed contracts and grants was not developed. AID overseas missions have continually ignored the requirement to provide necessary information, and AID management has not followed up on its directives. With the issuance of recently revised AID host country contracting procedures, the requirement is left up to the regional bureaus.

The lack of information on key AID-financed contracts and grants has created recurring problems in providing information to the Congress, as well as to AID managers, auditors, and project officers. We believe that by not having information available on a significant segment of AID-funded contract expenditures, AID places itself at a severe disadvantage, particularly in terms of efficient and effective management.

First, AID management is missing opportunities for informing the Congress and the general public on benefits accruing to the United States from the foreign assistance programs. Moreover, the information on host country contracts is needed by AID managers for general oversight and policy examination purposes. Also, AID and other auditors need this information for carrying out their auditing responsibilities more efficiently, and project officers need information on contract costs and contractor performance. This is particularly important in view of the serious management weaknesses resulting in the potential waste of millions of dollars that have been reported by the AID IG.

In our view, the potential benefits of having basic host country contract data readily available would greatly outweigh the cost of collecting this information and transmitting it to Washington.

#### RECOMMENDATIONS

We recommend that the AID Administrator require that appropriate data on host country contracts be promptly reported to Washington and maintained in an automated data bank. This information should contain those data elements needed to satisfy the various user requirements including managers, auditors, project officers, and the Congress.

Also, we recommend that the AID Administrator direct the regional bureaus to ensure that missions comply with this requirement, and institute appropriate measures for evaluating compliance.

#### WEAK INTERNAL CONTROL AND ACCOUNTABILITY OVER HOST COUNTRY CONTRACTS

During our survey we noted other management weaknesses associated with host country contracting activities, many of which had been reported by AID IG. Although we did not fully review these issues, we believe they should be brought to your attention. In November 1981, the Senate Appropriations Committee requested AID to study problems with host country contracting. We believe these issues, presented below, should be considered in responding to this requirement.

#### Need for more audit coverage

The primary responsibility for auditing host country contracting activities rests with the host governments. However, AID has determined that host countries have limited capacity to adequately audit these contracts and that host country contracts go largely unaudited. In 1979, the AID IG recommended that Assistant Administrators, in concert with the IG, decide on the

most economical and efficient means for ensuring audit coverage of host country contracts.

AID has recognized satisfactory audit coverage as an important part of management assurance that funds are spent properly and economically and, over the past few years, has been discussing approaches for increasing audits of host country contracts. As stated on page 7, IG efforts have been hampered by the lack of the host country contract inventory. The use of private accounting firms operating under an AID-financed contract is being explored as an alternative.

In our view, it is essential that AID decide, as soon as possible, on appropriate means for ensuring adequate audit coverage of host country contracts.

Inadequate internal controls  
contribute to waste

An area where serious shortcomings have been noted is the system of internal controls for payment for goods and services. Our limited testing of host country contractors' vouchers approved for payment in AID mission in Bangladesh indicated that improper and questionable payments had been made. We noted limited AID staff attention on verification of documents submitted with contractors' vouchers. For example, several mission employees are assigned to check a mission's travel vouchers, which amount to a few thousand dollars, while less staff is available for verifying host country contractor vouchers involving millions of dollars.

AID IG reports issued during the past 3 years show a potential for waste of AID funds resulting from inadequate internal controls in approving contractors' vouchers for payment. Questionable expenditures were found in all geographic regions and recur from mission to mission. A January 1982 IG report identified \$6.5 million in improper or questionable payments out of \$40.4 million worth of vouchers examined. The IG's critical findings included payments for ineligible items, payments of unauthorized expenses, freight overpayments, and unsupported payrolls.

The IG noted that the risk of questionable payment is particularly great when payment is made under the bank letter of commitment method because generally no AID official reviews the voucher and supporting documentation prior to payment. Currently, AID leans heavily on the bank letter of commitment for voucher reimbursement. In March 1981, 40 bank letters of commitment were outstanding with a total value of \$2.3 billion.

Because of the potential for waste due to poor or non-existent internal controls, AID management should give priority

attention to corrective action, such as that found in the Office of Management and Budget Circular A-123.

Poor project commodity procurement procedures costing AID millions

In our 1980 report on project planning and implementation problems <sup>1/</sup> we noted that AID, as a financier of projects, needs to take a more aggressive role in managing project commodity acquisition. We identified wasteful expenditure of foreign assistance funds because the services of a procurement agent were used to purchase commodities for a host country.

In September 1981 the AID IG reported similar findings and noted that at least 15 percent of the project procurement dollar could be saved by implementing more economical procurement practices. These savings could amount to about \$30 million of the \$200 million project commodity purchases for 1980. The IG's sample was taken from AID-financed project procurements under host country contracts exclusive of commodity import program expenditures, commodity procurements contained in contracts for technical services, and overseas mission procurements. These procurements amount to an additional \$800 million in 1980. Thus, the potential savings could be greater if applied to total AID-financed commodity procurements. The IG stated that AID has started a re-evaluation of its procurement methodology.

Difficulty in monitoring host country contracts

During our survey in Bangladesh we noted that AID personnel had difficulty in monitoring host country compliance with AID regulations because information on project activities was not readily available at the mission. An area of particular concern was the compliance with purchasing project materials and equipment from eligible sources--an area in which direct AID monitoring seems essential. This situation is illustrated by the following example.

During a visit to a major construction project site, the mission engineer found that the steel being used to construct the facility was from an ineligible source and origin. In this case, the host country contractor had failed to comply with contract terms. The contract price was amended to eliminate the purchase of ineligible steel amounting to about \$700,000. If AID personnel had not visited the site, then the noncompliance would not have

---

<sup>1/</sup>"AID Slow in Dealing With Project Planning And Implementation Problems" (ID-80-33, July 15, 1980).

been detected. We were told that information on project activities was not always available at the mission.

Adverse findings have been made by AID IG, such as the case where \$900,000 in freight charges was paid to ineligible foreign carriers making \$2.2 million in project commodities ineligible for AID financing. These improper or questionable payments are often attributed to the fact that AID project officers do not have enough information available for verifying contractor compliance.

In view of the significant amount of AID funding for host country contract activities and the substantial rate of error disclosed by IG audits, AID management should place particular emphasis on this area.

#### AGENCY COMMENTS AND OUR EVALUATION

AID acknowledged that it shared the basic objectives underlying our recommendations and that it has pursued a combination of administrative means of accomplishing the process of providing information to the Congress and assisting AID managers and auditors. The agency said it (1) intends to collect and maintain centrally basic summary information on existing host country contracts and (2) will establish a system of notifying the Congress of AID approved host country contracts over \$100,000. Also, a task force has been established to address the issues of weak internal control and accountability over host country contracts and the poor project commodity procurement procedures. (See enc. II.)

We believe that these indicated actions are positive steps in the right direction. When implemented and consistently applied, these actions should improve AID's ability to systematically collect and utilize information on host country contracts. However, we consider these initiatives to be modifications of AID's existing procedures that are described on pages 6 through 13. Without specific AID responses on the coordination and control provisions it would institute, we cannot further evaluate whether agency actions will result in readily available, complete, timely, and specific data on host country contracts. We intend to follow up on AID actions in this area and monitor closely the actions promised.

UNITED STATES INTERNATIONAL DEVELOPMENT COOPERATION AGENCY  
AGENCY FOR INTERNATIONAL DEVELOPMENT  
WASHINGTON, D. C. 20523



OFFICE OF  
THE ADMINISTRATOR

May 26, 1982

Mr. Victor Zangla  
Group Director  
United States General Accounting Office  
Washington, D. C. 20548

Dear Mr. Zangla:

We have reviewed the draft report entitled "Managing Host Country Contracting Activities", submitted with your letter dated May 19, 1982.

The Agency has shared for some time the basic objectives that underly your recommendations--information on host country contracts to:

- "(1) enable AID to readily inform the Congress and the general public on foreign aid contract expenditures and how they benefit the United States;
- (2) assist AID managers in general oversight and policy examination;
- (3) assist auditors in obtaining more complete audit coverage; and,
- (4) provide a basis for exchanging contract cost information and serve to alert AID officials on problem contractors."

The major issue has not been over those objectives, but the most effective and economical means by which the Agency can fulfill its responsibilities in the context of its world-wide operations. To that end, since 1976, as your draft report notes, the Agency has pursued a combination of administrative means - both centralized and decentralized - of accomplishing the objectives you cited: to inform the Congress, the Agency now has had for some time operated a system of post-award notification of AID approval of host country contracts of \$100,000 or more. To assist AID managers in the field, policy guidance has been provided regularly in regard to host country contracts. While obligation and expenditure levels for host

- 2 -

country contracts are not maintained specifically in Washington, they are available in the missions, and AID's Office of Financial Management does periodically collect overall information on project and non-project activities generally for oversight. Additionally, in respect to AID managerial oversight, mission plans are reviewed by the Washington Bureaus annually as a part of the budget submission process. To assist auditors in obtaining more complete coverage and provide a basis for exchanging contract costs information, at one time, AID required the missions to forward to AID's Office of Contract Compliance actual copies of host country contracts.

We have reviewed our experience with these efforts and your recommendations, and believe that the objectives we share may be furthered through the following initiatives, which we are now instituting.

First, as may be necessary for the audit and other purposes you cited, the Agency intends, in the coming months, to collect and maintain centrally (as it now does through the bureaus and missions), basic information on existing host country contracts. Rather than require submission to Washington of a copy of each contract--which is cumbersome and of limited usefulness--we will be collecting summary information essential to the purposes you identified. Through appropriate means, we will periodically up-date the information.

Second, under a Congressional pre-award notification system that will be established shortly, more complete information regarding host country contracts will be provided than before. The new procedures are designed to ensure advance notice to AID's Office of Legislative Affairs, and to the Congress, of AID approval of host country contracts of \$100,000 or more, as well as of awards of direct contracts, grants and cooperative agreements in that amount. New coordination and control provisions should ensure that ongoing information on host country contracts is timely and useful.

These means of addressing the overall objectives are consistent with your recommendation that the new legislative notification process serve initially as a basis for host country contract data, as we develop a more centralized base of information over the longer term.

Your report addresses collaterally two related concerns--alleged weak internal control and accountability over host

- 3 -

country contracts and difficulty in monitoring host country contracts. A separate issue--alleged poor project commodity procurement procedures, is also covered.

With respect to the former, we believe that the steps we have outlined will provide a solid base for the continuing exercise of audit reviews. Moreover, as a general matter, AID has recognized the problems associated with verification of documentation submitted with contractor's invoices. The differing levels of supporting details required for direct contracts, host country contracts, grants under OMB circular A-102 and other documents leads to some of the problems suggested in your report. On April 1, 1982, the Administrator established a special task force to address these overall issues through definition of the appropriate level of Agency responsibility and oversight by category of expenditure. In addition, this task force is following closely the provisions of OMB circular A-123, as the Agency conducts vulnerability assessments and internal control reviews. Notwithstanding our continuing general concern and the steps we are taking through the task force and otherwise, we note that the IG review of voucher practices cited as a basis for your findings did not utilize random sampling techniques; furthermore, it is unclear whether your own limited testing of vouchers, employed such techniques. Without the utilization of such random sampling, it would not seem appropriate to reach general conclusions about the very extensive total universe of AID's verification procedures. Of course, as to the specific instances cited, we are taking corrective actions.

The findings of the 1981 IG report regarding commodity procurements have been subject to a substantial internal review by the Agency in response to concerns regarding methodology and other issues. When the Agency completes its reviews, it will advise the GAO of its findings and any necessary corrective action that will be taken.

We trust that this letter will meet your concerns regarding host country contracts and related issues.

Sincerely,



R. T. Rollis, Jr.  
Assistant to the Administrator  
for Management