



MEMORANDUM

DATE: September 17, 2018

TO: USAID/Pakistan Mission Director, Jerry Bisson

FROM: Acting Regional Inspector General/Manila, Emily Gardiner /s/

SUBJECT: Financial Audit of the Malakand Reconstruction and Recovery Program Assistance in Pakistan Managed by the Provincial Reconstruction Rehabilitation & Settlement Authority, Government of Khyber Pakhtunkhwa, Grant No. 47, July 1, 2012, to June 30, 2013 (5-391-18-030-R)

This memorandum transmits the final audit report on the Malakand Reconstruction and Recovery Program Assistance in Pakistan managed by the Provincial Reconstruction Rehabilitation & Settlement Authority (PaRRSA), Government of Khyber Pakhtunkhwa. The audit was conducted by the Auditor General of Pakistan (Auditor General). The “Memorandum of Understanding Between the United States Agency for International Development and the Auditor General of Pakistan” requires that the audit be conducted in accordance with U.S. generally accepted government auditing standards (GAGAS) or the financial audit manual and the guidelines developed by the Auditor General.

The Auditor General stated that it performed its audit in accordance with GAGAS. It did not disclose the scope limitations that it did not fully comply with GAGAS pertaining to having a continuing professional education program and external quality control reviews. However, the mission confirmed that the Auditor General is not in full compliance with GAGAS requirements to have a continuing professional education program and external quality control reviews.¹ The Auditor General also stated that it performed its audit in accordance with international standards of supreme audit institutions issued by the International Organization of Supreme Audit Institutions (INTOSAI).² The Auditor General is responsible for the enclosed auditor’s report and the conclusions expressed in it. We do not express an opinion on the PaRRSA’s

¹ Issues which the Auditor General should address in future audit reports to more fully comply with GAGAS 3.83-3.85, which required the auditors to institute internal quality control procedures.

² GAGAS 2.19 allows auditors to use GAGAS in conjunction with professional standards issued by other authoritative bodies.

fund accountability statement; the effectiveness of its internal control; or its compliance with grant terms and applicable laws and regulations.³

The audit objectives were to (1) express an opinion on whether the grantee's fund accountability statement for the period audited was presented fairly, in all material respects; (2) evaluate the grantee's internal controls; and (3) determine whether the grantee complied with grant terms and applicable laws and regulations. To answer the audit objectives, the Auditor General reviewed program documents and procedures; examined the fund accountability statement including revenues received from USAID and costs incurred during the period; reviewed the internal control systems; and tested compliance with grant terms and applicable laws and regulations. The audit covered program revenues and costs of \$9,389,046 and \$18,879,017, respectively from July 1, 2012, to June 30, 2013.

The Auditor General concluded that the fund accountability statement presented fairly, in all material respects, program revenues and costs incurred under the agreement for the period audited. However, the Auditor General reported questioned costs totaling \$691,000 (\$86,000 ineligible and \$605,000 unsupported) in the fund accountability statement.¹ On page 15 of the report, the Auditor General provided a breakdown of the \$691,000 in questioned costs consisting of 16 items. Each item had an amount and a finding number but no description of the finding.³

In the report on internal control, the Auditor General did not identify any significant deficiencies or material weaknesses in internal control. In the report on compliance, the Auditor General indicated that it identified certain matters involving noncompliance; however, it did not provide a description or summary of these noncompliance issues nor did it state whether these noncompliance issues were considered material instances of noncompliance.¹

In its management letter, the Auditor General identified 30 issues. Based on the description of these issues, we consider all of the issues to be material instances of noncompliance;¹ hence we are making a recommendation for corrective action. Further, the effects of these material noncompliance issues totaling \$3,642,191 should have been identified as questioned costs in the fund accountability statement.¹ Accordingly, we are making a recommendation to the mission to determine the allowability of and recover, as appropriate, these questioned costs.⁴ The details of the material instances of noncompliance and the associated questioned costs are summarized in the following table.

³ We reviewed the Auditor General's report for conformity with professional reporting standards. Our desk reviews are typically performed to identify any items needing clarification or issues requiring management attention. Desk reviews are limited to review of the audit report itself and excludes review of the auditor's supporting working papers; they are not designed to enable us to directly evaluate the quality of the audit performed.

⁴ Some questioned costs are covered by fixed amount reimbursement agreements (FARA) wherein USAID's reimbursement to PaRRSA is fixed in advance based upon cost estimates reviewed and approved by USAID, and made upon the physical completion of an activity, a subactivity, or a quantifiable element within an activity. The emphasis is upon reimbursement based on outputs rather than inputs or costs. However, the audit report did not indicate which of the findings are covered by FARA, and whether or not the questioned costs covered by FARA had been billed to and paid by USAID. Therefore, we are making a recommendation to determine allowability of all questioned costs.

Table I

	Description of Findings	Ineligible Costs		Unsupported Costs		Reference-Finding No.
		PKR ^a	USD	PKR	USD	
1.	Payment for deployed security guards but the deployment was not verified by the authorized officers			372,500	3,884	4.1.1 Page 27
2.	Payment for utility charges of the Defense Office but the user and the relation to the project is not known			182,007	1,898	4.1.2 Page 28
3.	Payment of petroleum, oil, and lubricants for unauthorized vehicles	1,058,850	11,040			4.1.3 Page 29
4.	Difference in the opening balances between the bank statement and the cash book (\$10,875,838 or PKR1,043,151,605)	-	-	-	-	4.2.1 Page 30
5.	Funds deducted from the cash book without support			1,933,939	20,163	4.2.2 Pages 30-31
6.	Funds released without immediate requirement	1,144,989	11,938			4.2.3 Page 31
7.	Funds released with the work estimates not technically sanctioned by a competent authority			177,000,000	1,845,392	4.2.4 Page 32
8.	Funds deposited to a bank account which was not an exclusive bank account for the project activities	-	-	-	-	4.2.5 Page 32-33 ^b
9.	Incorporation of unsubstantiated cost estimate in the project implementation letter	-	-	-	-	4.2.6 Page 33-34 ^b
10.	Incorporation of unsubstantiated cost estimate in the project implementation letter	-	-	-	-	4.2.7 Page 34 ^b
11.	Expenditures incurred in excess of the amount authorized (PKR42.230 million + PKR8.108 million)	50,338,000	524,821			4.2.8 Page 35
12.	Unspent balances of deposit for completed projects not surrendered to the project authority	16,184,000	168,733			4.2.9 Page 35-36
13.	Funds released with the estimates of the relevant work not technically sanctioned by a competent authority			10,395,000	108,378	4.2.10 Page 36
14.	Funds released without immediate need	7,114,000	74,170			4.2.11 Page 37
15.	Payment of advance rental without prior approval of the Finance Department			360,000	3,753	4.3.1 Page 37-38

	Description of Findings	Ineligible Costs		Unsupported Costs		Reference-Finding No.
		PKR ^a	USD	PKR	USD	
16.	Replacement of batteries for 96 hand held sets without justification			758,400	7,907	4.3.2 Page 38
17.	Contract award not approved by authorized official	-	-	-	-	4.3.3 Page 39 ^b
18.	Contract award on the basis of open bill of quantities to the contractor instead of as prescribed in the PC-I Form of the project ^c	-	-	-	-	4.4.1 Page 39-40 ^b
19.	Outstanding secured advance to a contractor not recovered	3,363,000	35,062			4.4.2 Page 40
20.	Sales tax not deducted from payments to a contractor	-	-	-	-	4.4.3 Page 41 ^b
21.	Excess payment to a contractor due to a higher billing rates	2,421,000	25,241			4.4.4 Page 41
22.	Payment to a contractor for work not supported			11,135,000	116,093	4.4.5 Page 42
23.	Payment to a contractor for work not supported			3,852,000	40,161	4.4.6 Page 42-43
24.	Payment on the bill for dismantling work that showed no details about the dismantled materials and the costs of the dismantled materials not recovered	3,500,000	36,491	1,284,000	13,387	4.4.7 Page 43
25.	Payments to contractors of unallowable escalation charges	25,168,000	262,400			4.4.8 Page 44-45
26.	Payments to contractors without supporting documents			5,860,479	61,101	4.4.9 Page 45
27.	Penalty was not imposed on contractors for late completion	24,256,000	252,892			4.4.10 Page 46
28.	Payment to a contractor for work not identified in the bill of quantities nor possible to be executed	45,657	476			4.4.11 Page 46-47
29.	Payment to contractors for work not identified in the bill of quantities	1,526,000	15,910			4.4.12 Page 47
30.	Payment to a contractor for excess quantity of work claimed	86,345	900			4.4.13 Page 48
TOTAL		136,205,841	1,420,074	213,133,325	2,222,117	
TOTAL QUESTIONED COSTS		PKR349,339,166 or \$3,642,191				

^a PKR stands for Pakistani Rupee. All PKR figures have been converted at USD 1 = PKR95.9146 (computed average exchange rate per fund accountability statement on page 15) for the purposes of this memo. In future audit reports, the Auditor General should have stated all currency amounts in the audit report, including the report findings, in U.S. dollars. The audit report must include a note to the fund accountability statement that states the exchange rate during the audit period.

^b The finding was not related to disbursements in the fund accountability statement; thus, not questioned.

^c The PC-I Form certifies that the project proposal was prepared by a grantee based on the instructions provided by the Planning Commission.

For the 16 items comprising the \$691,000 in questioned costs reported in the fund accountability statement (discussed on page 2 of this memorandum), 2 items matched with the amount and finding number in the management letter (Items 22 and 23 in Table I on pages 3–4), and 5 items matched with the amount but with a different finding number in the management letter (Items 2, 14, 25, 26, and 30 in Table I on pages 3–4). The remaining 9 items (16 less 2 and 5) could not be matched with any of the findings in the management letter. To ensure that proper corrective actions are taken on the \$691,000 in questioned costs, we are making a procedural recommendation for the mission to determine (1) the descriptions of the 16 items comprising the \$691,000 in questioned costs reported in the fund accountability statement;

(2) the questioned costs in the fund accountability statement that did not pertain to the questioned costs summarized in Table I on pages 3–4; and (3) the allowability and recovery, if appropriate, of these questioned costs.

Further, for Finding 4.2.1 (Item 4 on page 3 of Table I), the difference in the opening balances between the bank statement and the cash book of \$10,875,838 or PKR1,043,151,605 should be further verified. Thus, we are making a procedural recommendation for the mission to determine if there was improper use of funds, and determine the allowability and recovery, if appropriate.

In response to our inquiry, the mission confirmed that the grantee does not have a cost-sharing contribution requirement and a USAID-authorized provisional indirect cost rate. However, the Auditor General improperly included a report on indirect cost rate on page 10.¹ Also, several findings in Table I on pages 3–4 were prior audit recommendations that had not been satisfactorily addressed; thus, were again reported in the current period management letter, and are covered by Recommendation 4 below.

To address the issues identified in the report and discussed in this memorandum, we recommend that USAID/Pakistan:

Recommendation 1. Determine the allowability of \$3,642,191 in questioned costs (\$1,420,074 ineligible and \$2,222,117 unsupported) as detailed in Table I on pages 3–4 of this memorandum, and recover any amount that is unallowable.

Recommendation 2. Determine (1) the descriptions of the 16 items comprising the \$691,000 in questioned costs reported in the fund accountability statement; (2) the questioned costs in the fund accountability statement that did not pertain to the questioned costs summarized in Table I on pages 3–4 of this memorandum; and (3) the allowability and recovery, if appropriate, of these questioned costs.

Recommendation 3. Determine if there was improper use of funds related to the difference in the opening balances between the bank statement and the cash book of \$10,875,838 or PKR1,043,151,605, as detailed in Finding 4.2.1 on page 30 of the management letter, and determine the allowability and recovery, if appropriate, of any misappropriated funds.

Recommendation 4. Verify that the Provincial Reconstruction Rehabilitation & Settlement Authority, Government of Khyber Pakhtunkhwa corrects the 30 material instances of noncompliance detailed in Table I on pages 3–4 of this memorandum.

We ask that you provide written notification of actions planned or taken to reach management decisions. We appreciate the assistance extended during the engagement.

The OIG does not routinely distribute independent public accounting reports beyond the immediate addressees because a high percentage of these reports contain information restricted from release under the Trade Secrets Act, 18 U.S.C. 1905 and Freedom of Information Act Exemption Four, 5 U.S.C. 552(b)(4) (“commercial or financial information obtained from a person that is privileged or confidential”).

Attachment: a/s