

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

Ramon Magsaysay Center
1680 Roxas Boulevard
Ermita 1000, Manila
Philippines



Fax Nos.: 6324214241
632-521-4811
Tel. No. 632-522-4411

May 29, 1998

MEMORANDUM

TO: Director USAID/Philippines, Kenneth G. Schofield

FROM: RIG/^{Manila}~~Bangkok~~, Bruce M. Watts *Bruce M. Watts*

SUBJECT: Audit of USAID/Philippines' Management of Technical Assistance Contracts, Audit Report No. 5-492-98-003-P

This memorandum is the final report on the subject audit. We considered your comments on the draft report and have included them at Appendix II. The report contains one recommendation. Actions taken by management as described in the comments are responsive to Recommendation No. 1 contained in the report. We therefore consider final management action on Recommendation No. 1 to be complete.

I appreciate the cooperation and courtesies extended to my staff during the audit.

BACKGROUND

USAID/Philippines uses technical assistance contracts to support USAID-funded programs in the Philippines. For these contracts, USAID/Philippines is responsible for ensuring that the technical assistance is performed efficiently and effectively.

A 1992 joint Office of Management and Budget (OMB)-USAID review team (SWAT) identified Agency-wide problems in USAID's management of contractors. The SWAT Team found that USAID did not know whether its contractors were working in an efficient or effective manner because, among other things, USAID did not (1) effectively evaluate contractor performance and (2) hold contractors accountable for specific results.

An October 1992 audit report issued by USAID's Office of the Inspector General identified similar situations related to USAID/Philippines' management of technical assistance contractors. The audit found that (1) statements of work contained in Mission contracts did not always include performance indicators to measure contractors' progress in accomplishing contract objectives and (2) contractors did not prepare adequate work plans and progress reports which would enable objective measurement of contractor

performance (Audit Report No. 5-492-93-01, Audit of USAID/Philippines' Direct A.I.D. Contracting for Technical Assistance).

As of February 25, 1997, USAID/Philippines was administering 14 active contracts for technical assistance with estimated costs totaling \$99.6 million, of which \$85.1 million and \$38.1 million had been obligated and spent, respectively.

AUDIT OBJECTIVE

The Office of the Regional Inspector General/Bangkok audited USAID/Philippines' management of technical assistance contracts to answer the following objective:

Did USAID/Philippines have the information necessary to ensure that the work under technical assistance contracts was on track toward achieving the contract objectives?

Appendix I includes a discussion of the scope and methodology for this audit.

USAID/Philippines did not always have the information necessary to ensure that work performed under technical assistance contracts was on track toward achieving contract objectives. Statements of work and work plans for two of three technical assistance contracts reviewed did not specify objectively verifiable progress indicators and targets. As a result, for the two contracts USAID/Philippines could not readily assess contractor progress and measure results.

The three contracts reviewed during the audit included the contract for the Growth with Equity in Mindanao (GEM) Program. As of February 25, 1977, \$15.1 million in obligations and \$4.9 million in expenditures had been incurred under the contract. The GEM contract and work plans contained **objectively** verifiable progress indicators and targets such as:

the identification of new market opportunities for and facilitation of 2 - 3 significant sales agreements (i.e. with a value of at least .5 million pesos) each year for products produced by farmer groups in each of the targeted areas.

This indicator and target are well defined and would permit the mission to assess progress on a periodic basis. However, unlike the GEM contract, the other two contracts and supporting work plans did not contain objectively verifiable progress indicators and targets. The results of our review of these contracts follows.

Progress Indicators and Targets Are Needed

OMB Policy Letter 91-2 (dated April 9, 1991) stipulates that performance-based contracting should include formal, measurable (i.e., in terms of quality, timeliness, and quantity) performance standards and surveillance plans to facilitate the assessment of contractor performance. In addition, USAID's "Managing for Results" directives-Automated Directives Systems (ADS) Section E203 .5.5(1)-state that operating units shall define performance, indicators for which quality data (reliable) are available at intervals consistent with management needs. For further clarification, the directives refer to Performance Monitoring and Evaluation TIPS No. 6, Selecting Performance Indicators, issued by USAID's Center for Development Information and Evaluation.

According to TIPS No. 6 :

“Performance indicators are at the heart of a performance monitoring system -- they define the data to be collected to measure progress and enable results achieved over time to be compared with planned results. Thus, they are an indispensable management tool for making performance-based decisions about program strategies and activities.”

TIPS No. 6 also identifies criteria for assessing the appropriateness and utility of performance indicators, including the following:

- Indicators should be direct. They should measure as closely as possible the result they are intended to measure.
- Indicators should be objective. They should be unidimensional (i.e., measure only one phenomenon at a time) and operationally precise (i.e., no ambiguity as to the kinds of data to be collected).
- Indicators should be quantitative, if possible.
- Indicators should be reliable. They should be selected based on whether data of sufficient quality for confident decision-making can be obtained.

In addition to performance indicators, ADS Section E202.5.5 stipulates that performance targets be established for USAID-financed contracts. According to ADS Section 203.4.52, performance targets are the specific and intended results to be achieved within an explicit time frame and against which actual results are compared and assessed. Such targets should be defined for each performance indicator.

Further, a General Notice issued by USAID's Assistant Administrator for Management in November 1994 instructed all missions to modify cost reimbursement and requirements contracts to require quarterly progress reports that focus on actual accomplishments in relation to goals and objectives for the quarter. In October 1994, the Director of USAID's Office Procurement issued a unilateral amendment to each cost-type and requirements contract. The amendment directs contractors to state whether activities are on target, compare actual accomplishments with objectives, deliverables, or requirements established for the period, and explain why objectives, deliverables or requirements were not met.

In addition to the contract under the Growth and Equity in Mindanao Project, we reviewed contracts under the Governance and Local Democracy Project and the Natural Resources Management Program. We found that the contracts for the later two programs did not include indicators and targets that meet the criteria identified above.

The \$13.6 million contract under the Natural Resource Management Program identifies two outputs; but, it does not specify objectively verifiable indicators and targets to measure progress in achieving the outputs. For example, one output was for establishment of a policy environment that promotes the management of forests on a sustainable basis and encourages long-term investment in forest-based industries. One of the performance indicators for measuring progress in achieving this output was: "The GOP [Government of the Philippines] develops and implements a system for assessing fees and charges for access to public forest resources that stimulates investment in, and a long-term commitment to sustainable management of forest lands by both communities and private corporations accessing public forest lands." However, no targets and time frames were established for the amount of fees and charges expected to be accessed and investments to be stimulated, nor were precise criteria identified to objectively determine when the anticipated long-term commitment would be achieved.

The \$14.1 million contract under the Governance and Local Democracy Project states that the contractor will provide assistance to selected local governments and communities to achieve effective systems for local governance and attain self-reliance. The contract identifies seven service objectives, but does not include indicators and targets to measure progress in achieving those objectives. For example, two of the objectives are: to increase private sector investments and participation, and to assist local governments to strengthen their financial positions. However, the statement of work does not specify targets and time frames for assessing changes in private sector investment or strengthening local government financial positions.

To supplement the work statements, contracts under the Governance and Local Democracy Project and the Natural Resources Management Program require contractors to provide work plans describing activities to be undertaken and how the activities contribute toward achieving the project and/or contract objectives. However, work plans prepared by the contractors do not consistently include objectively verifiable indicators and targets to

measure the contractors' progress toward achieving objectives. Instead most work plans describe activities to be performed by the contractors, such as holding meetings, training people, and preparing reports.

The contract under the Governance and Local Democracy Project requires the contractor to submit a life-of-contact work plan that reflects the expected achievement of project and contract objectives. The project objectives are to (1) strengthen local governments' financial positions by significantly increasing net tax collections; (2) help local governments achieve replicable development and service delivery performance benchmarks in such areas as maintaining roads and water supply systems and implementing primary health care projects; and (3) increase private sector investments at the local government level. However, the life-of-contract work plan does not identify objectively verifiable indicators and targets. As a result, an effective assessment of the contractor's progress can not readily be made. As of February 1997, USAID had paid the contractor \$3 million.

The contract under the Natural Resources Management Program requires the contractor to prepare a life-of-contract work plan that reflects the expected achievement of program and contract objectives. The work plan prepared by the contractor identifies 508,615 hectares as priority areas to be covered under management plans. This relates to the contract objective of managing 500,000 hectares of residual forest land on an ecologic, economic and socially sustainable basis. However, the work plan does not identify specific criteria and related targets and time frames for measuring progress toward achieving specific outputs specified in the plan such as: "Develop a sound policy framework, guidelines, and procedures for sustainable forest management...;" and "Help communities develop and implement sound and sustainable forest management system.. ." Further, the work plan does not identify targets and time frames so that progress toward achieving the contract objective can be measured and a determination can be made as to when USAID-funded technical assistance is no longer needed. As of February 1997, USAID/Manila had paid the contractor nearly \$6.1 million.

USAID/Philippines officials generally agree that the contract statements of work and work plans can be improved. However, some officials believe that indicators as to the number of activities to be performed—such as people trained, plans developed, and agreements signed—are in some cases good indicators for measuring contractor performance. In addition, some officials stated that:

- it is not always possible, especially when preparing work statements, to clearly define specific performance indicators or benchmarks to measure the performance of contractors;
- contractors' performance is dependent to a large extent upon developments that occur during the implementation of the contracts and the priorities of the host country; and

- the selection of cost-effective indicators is difficult in a setting that places considerable emphasis on social interaction. Therefore, the officials believe that greater consideration should be given to the role and judgement of the program manager's assessment of a contractor's performance.

This report is not saying that statements of work and work plans should not include indicators as to the number of activities to be conducted. However, indicators and targets for measuring results must be established and reported on so that contractors' progress in achieving objectives can be assessed and measured. TIPS No. 6 states that:

"...number of service providers trained would not be a direct measure of the result improved service delivery because people trained does not necessarily mean they will deliver services better".

This would also apply to other activity-oriented indicators such as plans developed or agreements signed.

It may be difficult to develop objectively verifiable performance indicators and targets in the ever changing environment within which USAID operates. Nevertheless, without indicators to identify "what" the contractor is expected to achieve and targets to specify "when," USAID/Philippines and others cannot objectively measure contractors' progress toward anticipated results. In addition, the Mission can not effectively determine when contract objectives have been achieved and USAID funding should end.

USAID/Philippines can improve management of its technical assistance contracts by establishing objectively verifiable indicators and targets for measuring progress toward achieving contract objectives and requiring contractors to report on the indicators and targets in quarterly progress reports.

Recommendation No. 1: We recommend that USAID/Philippines take action to incorporate objectively verifiable performance indicators and targets into the technical assistance contracts under the Governance and Local Democracy Project and the Natural Resources Management Program and/or require the contractors to prepare work plans with such indicators and targets and require contractors to report on the indicators and targets in quarterly progress reports.

Management Comments and Our Evaluation

Management officials agree that contracts using performance-based contracting methods should include objectively verifiable performance indicators and targets, and that contractors should be required to prepare work plans which include such indicators and

targets. The officials state that the contract for the Growth with Equity in Mindanao Project has objectively verifiable performance indicators and targets.

The Mission has determined that it would not be cost beneficial to modify existing contracts to conform to performance-based contracting guidelines. Officials state that it is difficult to incorporate the elements of performance-based contracting after an activity has begun. They believe such elements should be applied at the design stage. However, Mission officials have taken action to change the contracts cited in this report to **cost-plus-fixed-fee** completion contracts because the expected benefits from the award fee arrangements were insufficient to warrant the additional administrative costs involved.

Mission officials agree that contracts using performance-based contracting methods as well as cost reimbursement completion contracts should require contractors to report periodically on progress in achieving targets. The officials indicate that the Mission has implemented a requirement that contractors report semi-annually on such progress. The semi-annual reports on targets will be included in two of the four quarterly reports contractors are required to submit.

Management officials indicate that the Mission has used the contracts cited in this report as prototypes for performance-based contracts. Lessons learned from implementation are being used to ensure, to the maximum extent practicable, that performance-based contracting methods are incorporated into future acquisitions. Officials cite four recent acquisitions as examples. According to the officials, contracts for the four acquisitions include the elements associated with performance-based contracting, i.e., performance work statements, performance monitoring plans, quality assurance plans, and periodic reporting on progress toward achieving indicators and targets.

Based on management comments, Mission officials have taken action to ensure that future performance-based technical assistance contracts contain the elements necessary for assessing contractor performance. These actions are responsive to Recommendation No. 1. Therefore, we consider final management action on Recommendation No. **1** to have been taken. Recommendation No. 1 is closed upon issuance of this report.

SCOPE AND METHODOLOGY

We audited USAID/Philippines' management of technical assistance contracts to determine whether the Mission had the information necessary to ensure that work under technical assistance contracts was on track toward achieving contract objectives. The audit was performed in accordance with generally accepted government auditing standards and was conducted at USAID/Philippines from October 1996 through May 1997.

To accomplish the audit objective we reviewed Federal Acquisition Regulations (FAR) and Office of Management and Budget policies and guidance for the use of performance-based contracts. We reviewed USAID's Automated Directives Systems Series 200 and 300 related to technical assistance contracts. We also contacted USAID/Washington Office of Procurement officials to clarify USAID's policy and procedures related to progress reporting by technical assistance contractors.

We selected three large technical assistance contracts with estimated costs totaling \$46.4 million, representing 47 percent of total estimated costs of \$99.6 million for all active technical assistance contracts administered by USAID/Philippines as of February 1997. The three contracts were under the following mission programs: the Growth with Equity in Mindanao Project, the Governance and Local Democracy Project, and the Natural Resources Management Program.

We reviewed the contracts and the work plans prepared by the contractors to determine if objectively verifiable indicators and targets to measure contractor progress have been established. We also held discussions with USAID/Philippines' project and contracting officials responsible for administering the three contracts.

USAID/Manila
FPO AP 96515



Fax Nos.: (632) 521-4811
(632) 521-5241
Tel. No. (632) 522-4411

JAN 27 1998

MEMORANDUM

TO: Mr. Bruce Watts
RIG/A/Bangkok

FROM: ^{KGS} Kenneth G. Schofield
Mission Director
USAID/Philippines

SUBJECT: Draft Report on the Audit of USAID/Philippines'
Management of Technical Assistance Contracts

REF: Watts-Redder e-mail dated November 28, 1997

USAID/Philippines appreciates RIG/A's efforts and cooperation in completing the subject report. We present the following comments for incorporation into the final audit report.

Recommendation No. 1: We recommend that USAID/Philippines take action to incorporate objectively verifiable performance indicators and targets into the four technical assistance contracts reviewed and/or require the contractors to prepare work plans with such indicators and targets, and require contractors to report on the indicators and targets in quarterly reports.

Mission Response:

a. The Mission agrees that contracts using performance-based contracting methods should include objectively verifiable performance indicators and targets, and that contractors should be required to prepare work plans with such indicators and targets. The GEM contract has objectively verifiable performance indicators and targets (see pages C-5 through C-9 of the contract which is included as Attachment A), and the audit report makes no assertions to the contrary.

b. The other three contracts addressed in the audit report -- the contracts for GOLD, CRM and the NRM -- were designed and advertised as completion contracts, and do not use performance-based contracting methods as described in recent guidelines for

- 2 -

using these methods. For the record, performance-based contracting methods employ performance work statements, quality assurance plans, performance standards, and clear definition of results to be achieved. On the other hand, completion contracts, per FAR 16.306(d)(1), are defined as "...stating a definite goal or target and specifying an end product". The three contracts identified above meet the test of completion contracts. As a result, the Mission has determined that it would not be cost effective or beneficial for USAID to amend the three contracts to conform to guidelines for using performance-based contracting methods, given the implementation status of the activities (performance-based contracting methods need to be applied at the design stage because it is extremely difficult to incorporate the different elements after implementation has begun). Note: The Mission has modified these contracts from cost-plus-award-fee completion contracts to cost-plus-fixed-fee completion contracts (Attachments B, C, & D, respectively) because the expected benefits were insufficient to warrant the additional administrations associated with award fee contracts, per FAR 16.405-2(c)(3).

c. The Mission agrees that not only contracts using performance-based contracting methods but also cost reimbursement completion contracts should require the contractors to report periodically on achieving their targets. We are implementing semi-annual reporting procedures that we believe are adequate for these purposes because it is a more efficient use of resources and results in substantial savings in administrative costs by contractors, USAID, and GOP counterparts. Semi-annual reporting conforms to the Mission's practice of conducting Mission-wide reviews of results for all SOs on a semi-annual basis. We acknowledge that the current AIDAR "Reports" clause requires quarterly performance monitoring reports; however, the AIDAR permits discretion as to what these quarterly performance monitoring reports contain. The quarterly performance monitoring reports described in the AIDAR "Reports" clause requires the contractor to discuss briefly issues, problems, and achievements, but not necessarily on specific targets specified in the contract. In order to comply with the AIDAR and efficiently utilize USAID resources, the Mission will require contractors to report on the progress of achieving their targets in two of the four quarterly reports or semi-annually each year.

d. When the four contracts addressed in the audit report were designed and awarded, the guidance on using performance-based contracting methods was neither well-developed nor understood. It continues to be less developed and less understood for technical assistance service contracts of the kind awarded most frequently by USAID. However, USAID/Philippines considers these four contracts as prototypes for performance-based contracts, and have used the "lessons learned" from their implementation in order to ensure that performance-based contracting methods are

- 3 -

incorporated into future acquisitions to the maximum extent practicable. This is shown by the Mission's most recent acquisition actions -- the issuance of RFPs for the following major activities in FY 98: Accelerating Growth Investment and Liberalization with Equity (AGILE); Municipal Coastal Environmental Initiative (MCEI); and the Build-Operate-Transfer (BOT) Program (Attachment E). Consistent with Recommendation No. 1, each of these contracts will have the various elements associated with performance-based contracting methods, i.e., performance work statements, performance monitoring plans, quality assurance plans, etc., and will require periodic reporting on progress in achieving indicators and targets.

Based on the considerations described above, including the actions taken by the Mission, the Mission requests that Recommendation No. 1 of the draft audit report be considered resolved and closed.

Mission Management's Representation Letter is shown under Attachment F.

Attachments: a/s