PROJECT PROCUREMENT- RELATED AUDIT REPORT

Loan No. 1909-INO (SF)
Poor Farmers’ Income Improvement through Innovation Project
EXECUTIVE SUMMARY

1. The Integrity Division (OAGI) conducted a project procurement-related audit (PPRA) on Asian Development Bank (ADB) Loan No. 1909-INO (SF): Poor Farmers’ Income Improvement through Innovation Project (the Project) carried out in Indonesia. The Indonesian Agency for Agricultural Research and Development (IAARD) is the executing agency (EA) of the Project. The Project’s overall objective is to benefit farmers of more than 1,000 villages in five districts of Indonesia, namely Temanggung and Blora in Central Java, East Lombok in West Nusa Tenggara, Ende in East Nusa Tenggara, and Donggala in Central Sulawesi. It comprises four components:
   - Part A: Poor Farmer Empowerment (which includes the provision of village investment funds for village-level public investments);
   - Part B: Development of National and Local Agricultural Information Resources;
   - Part C: Support for Agricultural Innovation, Development and Dissemination; and
   - Part D: Project Management

2. The project used existing decentralized government structures to deliver project objectives, as decentralization is a central economic and political reform instrument of the Government of Indonesia (GoI). Community empowerment and capacity building are enabled, in line with Indonesia’s strategy for long term poverty alleviation.\(^1\) It was designed in close coordination with other donors to ensure it is compatible, complementary, and avoids overlap with concurrent development projects.\(^2\) This approach is in line with ADB’s country operational strategy for Indonesia, which emphasizes participatory project design and implementation.\(^3\) Subsequently, the Paris Declaration on Aid Effectiveness was endorsed in 2005 to maximize aid effectiveness and management for development results.\(^4\)

Major Recommendations

3. The Audit Team acknowledges the challenges inherent in the Project design. Greater collaboration between SERD (jointly with IRM) and GoI/IAARD is crucial to establish an effective monitoring mechanism for future decentralized projects in Indonesia to ensure transparent procurement and financial management capacity at all levels.

4. Bidding integrity and transparency should be established at project commencement, as this is when material, large contracts are often awarded, and the opportunity to maximize development effectiveness and results is greatest. IAARD should ensure financial management and internal controls over project funds and assets are strengthened across all levels of project implementation.

5. Strong procurement and financial management controls mitigate the risk of improper use of Project funds and assets, maximize development effectiveness\(^5\) and deter fraud and corruption. GoI must take the lead in addressing this promptly, and collaborate with ADB to strengthen Indonesia’s capacity to manage for development results.

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\(^2\) Paragraph 6, *RRP:INO 34112 Report & Recommendation of the President to the Board of Directors on a Proposed Loan to the Republic of Indonesia for the Poor Farmers’ Income Improvement through Innovation Project.*


\(^4\) Alignment with national structures and strategies, coordination with other donors, strategies, capacity building are some of the principle commitments of the Declaration. Both ADB and Indonesia are signatories to the Declaration

\(^5\) Note that comments on development effectiveness throughout this report are limited to audit observations as to how recommendations made here - with respect to anticorruption measures, strong internal controls and compliance with applicable guidelines - can increase development effectiveness, and are not intended as comments on the overall development effectiveness of the project.
Key Findings & Recommendations

Project’s Procurement Process

6. Observations were made during the PPRA indicating that there is probable cause for concern that ADB’s Procurement Guidelines and Anticorruption Policy may not have been closely followed. These were in relation to conflict of interest among bidders, potential misrepresentation in bid documents, irregularities in the tendering process, and possible overpricing of electronic goods. OAGI will further investigate these subsequent to issuance of the PPRA report in accordance with ADB’s Integrity Guidelines and Procedures. Not closely observing the Anticorruption Policy invariably results in ineffective and/or improper use of aid funds, thereby reducing development effectiveness.

7. Audit Team’s recommendations to ADB and the IAARD pertaining to the procurement process are highlighted below.

Recommendations for ADB:

8. To familiarize the key Project staff, especially the tendering committee members of the ADB Procurement Guidelines, the Audit Team recommends that the ADB’s Central Operations Service Office, in coordination with SERD and IRM’s Procurement unit, ensure that periodic training sessions are conducted in the DMCs with targeted participants from project officials who are responsible for procurement matters especially at project commencement in future seminars and provide support in addressing procurement concerns during the course of projects.

9. Decentralized projects such as community-based project like this one, may be better managed and administered by IRM whose Procurement Unit could review procurement activities systematically for all IRM-delegated projects and provide better support for the EA to ensure ADB’s Procurement Guidelines, Anticorruption Policy, and Project Administration Memorandum are strictly complied with.

Recommendations for IAARD

10. To provide the individuals involved in bid evaluation with adequate support and to ensure due diligence on their part, it is recommended that IAARD
   - consider setting up a procurement unit supported by a procurement consulting team initially, within IAARD to provide guidance to tendering committees in future projects;
   - ensure tendering committees exercise due diligence in evaluation of bid proposals, while strictly observing applicable bidding procedures;
   - identify and augment appropriate training on procurement matters directed toward key procurement staff, especially the tendering committee members at the project commencement in the future.

11. The Audit Team recommends IAARD strengthen control procedures to ensure that the tendering committees conduct procurement process transparently and in conformity with ADB’s Procurement Guidelines.

Financial Management System and Village Investments

12. The role expected at village level in relation to financial management and reporting is unclear. Documentation of bank reconciliations and financial progress reporting is weak at the village level. This erodes effective delivery of project development objectives. It is recommended that in future projects IAARD
clarify the role and responsibilities of participants at all levels – especially in the area of financial management; and

establish and/or strengthen required internal controls and financial management systems over project funds and assets across all levels of project implementation.

Final Comments

13. There were positive indications that the Project has delivered expected outputs to improve the incomes of Indonesian farmers, and should continue to do so. A case in point is that project assets were found to be generally used as intended by targeted beneficiaries. Implementation of recommendations made in this report can only augment results achieved to date.

14. The Audit Team thanks Project management and staff for their cooperation and responsiveness to audit requirements, especially in receiving OAGI’s follow-up Mission prior to issuance of this report. ADB values the courtesy and support that Project officials extended to the Audit Team, including the valuable participation of Badan Pemeriksa Keuangan (Audit Board of the Republic of Indonesia) who jointly conducted this PPRA, as well as SERD, and IRM.

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6 This is also the finding of the Regional Technical Assistance project (RETA) 6218 – Decentralization in Social Sectors, and RETA 6089 – Strengthening Results-Based Management for Social Sector Agencies, which were conducted in part to identify the interplay of decentralization and results-based management in the education and social sectors.