

5250110 (3)  
PD-AAF-991-C1



# Auditor General

REVIEW OF THE  
RURAL & MUNICIPAL DEVELOPMENT LOAN  
PROJECT NO. 525-0176  
USAID/PANAMA

Audit Report Number 1-525-80-14

Issue Date June 30, 1980

Area Auditor General Latin America  
Agency for International Development

## TABLE OF CONTENTS

	<u>Page No.</u>
EXECUTIVE SUMMARY	1
Introduction	1
Scope	1
Conclusions and Recommendations	1
BACKGROUND	1
Scope	2
AUDIT FINDINGS, CONCLUSIONS AND RECOMMENDATIONS	3
Implementation	3
Technical Assistance and Training	3
Project Evaluation	7
Contractor Evaluation Performance	9
Lack of Compliance with Audit Report Requirement	9
Lack of Signs and Markings	10
Delays in Processing Reimbursement Requests	11
Monitoring	14
APPENDIX A - Listing of Recommendations	17
LIST OF REPORT RECIPIENTS	18

**REVIEW OF THE  
RURAL AND MUNICIPAL DEVELOPMENT LOAN  
PROJECT NO. 525-0176  
USAID/PANAMA**

**EXECUTIVE SUMMARY**

**Introduction**

The United States made available to the Republic of Panama a loan of not more than \$4 million in November 1975. The loan funds provided were to assist in financing training, technical assistance and subloans for food, rural development and nutrition projects. Various agencies and municipalities in Panama were to contribute \$4.5 million to implement project activities.

The funds made available for training and technical assistance were to strengthen the institutional capacity of the Panamanian implementing agency as well as the administrative capacity of the various municipalities being assisted. The funds subloaned to the municipalities were to be for projects specifically designed to increase the productivity and income of the rural poor.

As of March 31, 1980, AID loan disbursements totaled \$1.3 million with an additional \$948,000 approved for disbursement in April 1980. Panamanian organizations have contributed their share of the funds for the implementation of activities.

**Scope**

The purpose of our interim audit was to review progress made in achieving objectives, identify problems, determine compliance with the loan agreement and AID regulations and observe the use of AID-financed goods and services. Our audit covered activities from inception of the loan agreement on November 28, 1975 through March 31, 1980. This project had not previously been audited by AID's Auditor General.

**Conclusions and Recommendations**

Forty-seven projects at total costs of \$5.2 million had been approved as of March 31, 1980. Of the \$5.2 million, \$3.1 million will come from AID loan funds and the remainder from Panamanian sources. Many of these projects have been completed and were for various types of activities including wholesale and retail markets, slaughterhouses, agro-businesses, transportation facilities, feeder roads, bridges, water supplies and working capital. An additional 14 projects for similar type activities with an estimated cost of \$828,000 were being considered. We believe this portion of the project has progressed satisfactorily and will contribute to the accomplishment of the project's goals and objectives (page 3).

Only a limited amount of technical assistance and training has been provided under the project, the Panamanian implementing agency officials have been reluctant to accept external technical assistance and needed assistance in critical areas has not been provided to municipalities. As a result, the institutional capacity

of the Panamanian implementing agency and the operating and managing capabilities of the municipalities have not been improved. Thus, progress in technical assistance and training has not been satisfactory and unless action is taken now AID should withdraw from further participation in the project (pages 3 to 6).

The 1979 annual evaluation of activities was not done because USAID/Panama did not believe that enough projects had been completed long enough to adequately measure the impact of the projects. We believe that an evaluation should be done annually to highlight shortcomings so that corrective action can be taken at the earliest possible time (pages 7 to 9).

USAID/Panama's management and monitoring should be improved. Some project sites we visited were not properly marked to show AID's participation in the activities. Also, some commodities financed with loan funds did not have AID emblems attached (page 9 ). There were significant delays in reimbursing the Panamanian implementing agency for project expenditures because of a lack of written procedures and coordinated follow-up (page 10 ). Our recommendations to USAID/Panama are: to notify the implementing agency that it should fully comply with marking requirements (page 11 ), to issue an implementation letter listing the supporting documentation to be submitted with reimbursement requests (page 14 ), to establish a schedule of field visits, and to require written reports of these visits (page 15 ).

## BACKGROUND

The United States, acting through the Agency for International Development, agreed to loan the Republic of Panama, acting through the National Bank of Panama (Bank), an amount not to exceed \$4 million. The loan agreement (no. 525-T-044) was signed on November 28, 1975 to finance activities under the Rural and Municipal Development project no. 525-0176.

The loan funds provided were to be used to assist the Bank in financing training, technical assistance and subloans to rural municipalities or associations of municipalities for food, rural development and nutrition projects. The Bank was to establish a Municipal Development Division to permit the timely and effective implementation of the project. The activities assisted by loan funds were to enable government units to play a more significant role in providing municipal public services and developing productive enterprises in response to local needs.

Training and technical assistance were to strengthen the institutional capacity of the Municipal Development Division of the Bank as well as the administrative capacity of various municipalities involved in the project. The medium and long term credit provided by the subloans were specifically designed to increase the productivity and income of the rural poor through such means as stimulation of small enterprises in rural towns.

The loan agreement required the establishment of an Advisory Council and Technical Coordinating Committee to assist in the implementation of loan activities. The Advisory Council was to make recommendations about policies and projects for funding and about technical assistance and training program. In addition, the Advisory Council was to review the implementing agency's operations and identify those areas needing technical assistance and where such technical assistance could be obtained. The Technical Coordination Committee was to help implement the provision of technical assistance.

Activities financed with loan funds were to be completed by March 31, 1979. However, delays were encountered and the current completion date is now March 31, 1981. As of March 31, 1980, disbursements totaled \$1.254 million and an additional \$948,000 was approved for disbursement in April 1980.

As of March 31, 1980, subloans for 47 projects involving about \$3.1 million of AID funds had been approved by the Bank. The remaining \$640,000 of funds allocated for subloans were set aside for 14 projects expected to be approved in 1980. Types of activities being financed include wholesale and retail markets, slaughterhouses, agro-businesses, transportation facilities, feeder roads, bridges and provision of water supplies. The remaining \$260,000 in loan funds were reserved for technical assistance and training of which \$113,000 had been expended as of March 31, 1980.

In addition to the \$4 million in AID loan funds, the Republic of Panama and the Bank were to provide \$3.5 million. Two and a half million dollars were to be used for subloans to municipalities and the remaining million was to pay training and operating costs of the Municipal Development Division of the Bank. The municipalities were to contribute a total of one million dollars as their participation in the projects within their respective areas.

The Bank is responsible for the project's execution. A Municipal Development Division was established within the Bank to implement the project. The Division was to be responsible for directing and coordinating subloan activities. The Division's responsibilities included accounting for the financial activities of the fund, providing technical assistance and training to the municipal governments, evaluating the financial, economic and technical feasibility of subloan proposals, preparing the subloan documentation, and monitoring subloan execution. An evaluation and research section was to design and implement a continuing evaluation system.

Responsibility for monitoring the implementation of the Rural and Municipal Development project is assigned to the Agriculture and Business Development Division of USAID/Panama.

### Scope

The purpose of our interim audit of the Rural and Municipal Development project was to review progress made in achieving objectives, to identify problems requiring management's attention, to determine if the provisions of the loan agreement and AID regulations were being complied with, and to observe the use of AID-financed goods and services. The period covered by our audit was from inception of the loan agreement on November 28, 1975 through March 31, 1980.

Files maintained by USAID/Panama, the National Bank of Panama, and selected project sites for the Rural and Municipal Development project were reviewed and discussions were held with individuals of these organizations. During our audit, we visited the sites of 18 projects in various parts of Panama.

## AUDIT FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

### Implementation

Implementation of the subloan portion of the project has been progressing satisfactorily. However, technical assistance and training have not moved as rapidly as expected.

Originally it was estimated that it would take 5 years to implement the Rural and Municipal Development project, the first year being used to basically build the institutional capability necessary for the project. While USAID/Panama believed that 5 years would be required to implement the project, AID/Washington policy required that all projects be designed so they could be completed within 3 years. Activities are now scheduled for completion by March 31, 1981, just over 5 years from the signing of the loan agreement. USAID/Panama officials believe that all activities will be completed by that date.

A Municipal Development Division has been established within the National Bank of Panama and it has provided some technical assistance and many subloans to municipalities. Some of the early subloans were not effective because the projects were not financially viable. However, this was a learning process and improvements have been made by moving more to service orientated and financially viable activities

A total of 47 projects had been approved as of March 31, 1980 for a total cost of \$5.2 million. Many of these projects have been completed and were for various types of activities, construction, purchase of commodities, and working capital. Of the \$5.2 million, \$3.1 million will come from AID loan funds, \$712,000 from the Republic of Panama and the National Bank of Panama, and \$1.3 million from municipalities. In addition, the Bank has contributed additional funds to pay necessary operating costs.

As of March 31, 1980, there were subloans for an additional 14 projects for estimated costs of \$828,000 being considered. About \$642,000 of the funds for these projects will come from AID funds, the remainder will come from Panamanian sources.

Only a limited amount of technical assistance and training has been provided. Panamanian implementing agency officials have been opposed to external technical assistance because of the cost and because they believed the Bank had the expertise. Recently, Panamanian officials have decided that some technical assistance is needed and should start by July 1, 1980.

While accomplishments have been made, we did note several areas where improvements should be made. These areas are discussed in the remaining sections of this report.

### Technical Assistance and Training

Technical assistance and training provided under the rural municipal development project have been very limited because the National Bank of Panama has been reluctant to accept external technical assistance. As a result, operating and managing capabilities of the municipalities have not been improved. Needed assistance has

not been provided in the critical areas of administration and management, finance and tax administration, and public services management, organization and methods.

The loan agreement allocated \$264,000 for technical assistance. These funds were to be used to finance short and long term consultants who would provide training and technical advice to personnel of the Panamanian implementing agency and through this agency to the various municipalities being assisted. The purpose being to strengthen the institutional capacity of the Bank and participating municipalities.

The loan agreement required as conditions precedent to initial disbursement for items other than technical assistance the establishment of an Advisory Council and a Technical Coordinating Committee and evidence that arrangements for technical assistance and training to be provided under the project had been made. The Advisory Council was to make recommendations about programs. In addition, the Advisory Council was to review the implementing agency's operations and identify those areas needing technical assistance and where such technical assistance could be obtained. The Technical Coordinating Committee was to help implement the provision of technical assistance and to coordinate assistance activities and prevent duplication.

The Advisory Council and Technical Coordinating Committee were established in 1976. However, USAID/Panama accepted letters between various Panamanian ministries where agreement in principle was reached to support the technical assistance and training needs of the project as being satisfactory evidence that firm arrangements had been made. A USAID/Panama memorandum of March 3, 1976 stated, in part, "These letters lay the ground work for more concrete future arrangements relating to the provision of specific technical assistance\*\*\*. \*\*\*Insisting on more definite or specific arrangements\*\*\* would be inadvisable at this time and might be counterproductive." "The costs, exact timing, and exact types or numbers of instructors have not been identified. For this reason neither funding nor training personnel requirements can be identified at this time." "The exchange of letters referred to in paragraph above, we believe, satisfies the CP (conditions precedent) even though agreement on the details under which agencies will make trainees available have not been delineated."

Implementation letter no. three dated March 12, 1976, advised the Panamanian agency that the conditions precedent to initial disbursement had been met. The implementation letter also advised that USAID/Panama expected the municipalities scheduled to receive the first subloans would have the highest priority in receiving appropriate technical assistance and training to maximize the prospects for a successful project.

The Advisory Council never met because its members were from a high level in the government, their time was at a premium, and were not able to devote the time necessary to implement activities. The Council was also not given the necessary logistic and staff support. The Technical Coordinating Committee has met sporadically at the technical level and put together a program. The Committee suffered from impotence and severe lack of logistical and moral support and it was not expected that the program developed would be carried out. In essence, the situation regarding technical assistance and training, that the Advisory Council and

Technical Coordinating Committee were to resolve, remains about the same as it was before the AID loan was signed, that is, each ministry has its own program and activities with the municipalities and no coordinated effort has been implemented.

As of March 31, 1980, loan funds of \$112,878 had been expended to finance the services of a municipal development consultant from Colombia and six mid-level advisors from Panama. Technical assistance provided consisted of diagnosis, programming, organizing and implementing services necessary to establish the organizational structure required to implement loan activities. The consultant from Colombia, developed operating and credit manuals as well as manuals for technical assistance, training, and analysis of information and evaluation. The six Panamanian mid-level advisors worked as counterparts to the consultant and helped the Bank in carrying out its municipal development program.

Bank officials advised us that these advisors' assistance was very effective in setting up the organizational structure and instituting implementation. However, technical assistance at the municipality level has been minimal, although the need for such assistance was evident in the projects we visited. For instance, the majority of the projects inspected were not maintaining sound accounting records and if maintained they were not up to date.

USAID/Panama commented in its reply to a draft of this report that the contributions of the Panamanian mid level technicians (advisors) to the tasks of organization and preparation of manuals were minimal and these technicians never worked as advisors but were utilized as part of the Bank's technical staff. When the situation came to the attention of USAID/Panama, the Bank was advised that the payments to the technicians constituted budget support, was in violation of the loan agreement, and unless the roles of the technicians were changed AID could not support an extension of their contracts. AID financing of the contracts was not continued.

USAID/Panama has tried to get the National Bank of Panama to initiate a program of technical assistance and training during the implementation of this project but in most cases has been met with a negative attitude by Bank officials. The reasons for this negative attitude toward accepting external technical assistance were twofold: First, Bank officials feel that external technical assistance is too expensive and they appear to resent an outside advisor or consultant making more money than the Bank's General Manager. Second, there is an apparent engrained resistance to the acceptance of technical assistance no matter the source of such assistance. It appears the Bank considers itself a prestigious organization with highly qualified professionals and feels that it is competent to implement a credit program for municipalities.

After 4 years of operations, the Bank now realizes it lacks the expertise to assist the municipalities in their development process. It appears this change in attitude toward technical assistance has been the result of USAID/Panama's continuing pressures to have the Bank use technical assistance. The provision of technical assistance services to municipalities was a condition for extending the loan's terminal commitment and disbursement dates to September 30, 1980 and March 31, 1981 respectively.

The Bank is now in the process of procuring a consulting firm contract to train its staff so that needed technical services can be provided to municipalities.

Loan funds of \$96,828 will be used for this purpose. The remaining technical assistance funds of \$54,294 will be used for training of Bank personnel (\$37,000) and for observation trips (\$17,294).

The services of four contract advisors were being procured by the Bank for a 6 month period at an estimated cost of \$96,828. The period of service of these advisors may be extended and, if so, will be financed with Panamanian funds. The areas of assistance include administration and management; finance and tax administration; and public services management, organization and method. During the period of the contracts, technical assistance will be provided to six selected municipalities as a pilot project. The Bank planned to finalize the contract negotiations in May or June so the advisors could start working by July 1, 1980.

The training program contemplates short courses in municipal administration and management, municipal finances, project design and development, and project evaluations for 10 participants. The observation trips are for key staff personnel of the Bank to municipal development institutions in other Latin American countries and the U.S. to learn about problem solving techniques, sources of funding, socioeconomic impact and target groups.

While USAID/Panama has made a number of attempts during the implementation of activities under the Rural and Municipal Development project to get the Bank to implement a program of technical assistance and training, we believe that once USAID/Panama agreed to release funds for subloans in March 1976 without a technical assistance and training program in place it lost the only effective lever it had. A second opportunity was made available when a recommendation was inserted in the evaluation of project activities for 1976 that disbursement of funds be suspended unless the Advisory Council formally convenes and decides on the strategy and an action plan to accomplish project activities. USAID/Panama failed to effectively follow-up on this recommendation since the Advisory Council has never met. The 1978 evaluation made a recommendation that another attempt be made to get an amended version of the Advisory Council and Technical Coordinating Committee operating. This latest recommendation has also not been implemented.

One of the major benefits to be derived from this project was to build the institutional capabilities of the Bank and various municipalities so they could provide better services. Without technical assistance and training this can not be done. The Bank now appears ready to implement a reduced version of a technical assistance and training program which build some institutional capabilities. Should the Bank fail to implement the revised technical assistance and training program, we believe USAID/Panama should withdraw from participation in any more subloan projects and deobligate any unutilized funds.

#### Recommendation No. 1

USAID/Panama should not participate in any subloan projects after August 1, 1980 if the National Bank of Panama has not implemented a technical assistance and training program by that date. Any unutilized funds should be deobligated.

## Project Evaluation

The annual project evaluation for 1979 was not made as required by Section 4.03 of the loan agreement. The evaluation review was to be held in September 1979 to evaluate the project's progress and continuing appropriateness of targets, sublending criteria and procedures and the impact of achieving project purposes. The reason for not conducting this evaluation was that not enough projects had been completed long enough to warrant an evaluation of basic aspects such as: employment generation, cost effectiveness in providing services, expanded coverage of services, and administrative and managerial improvements. Although this reason has some merit, we believe had the project been evaluated as scheduled USAID/Panama and the Bank should have benefitted from implementation experiences adversely affecting the progress of the project, i.e., the lack of technical assistance and training program.

The last project evaluation was made in 1978 by a contractor. The contractor submitted a draft report dated November 15, 1978. The draft report in English was submitted to the Bank on December 1, 1978 so that the report's contents could be evaluated. We were advised by USAID/Panama that the evaluation report was translated into Spanish and distributed to high level functionaries of the Bank and to representatives of the Technical Coordinating Committee. USAID/Panama's Director suggested that a meeting be held between USAID/Panama and Bank officials to begin action on the report's recommendations to improve the program. We found that the draft report was accepted by USAID/Panama as the final report and a meeting, as suggested by the USAID/Panama Director, was not held to take action on the report's recommendations. We found no evidence during our review that the Spanish version of the evaluation report was formally transmitted to Bank officials.

The draft evaluation report of November 15, 1978 compared actual accomplishments against the project's logical framework goals and objectives. The evaluator concluded the program, as designed, had been successful in establishing a municipal development fund, but that there were deficiencies in meeting objectives in technical assistance and training, institutional development of the Bank credit programs and coordination between GOP agencies. The contractor made four recommendations to improve the program. These recommendations, among other things, were:

- To develop a department of local development plans as well as department of municipal revenue improvement, with underlying one-year technical assistance from a full-time resident advisor.
- Create a new organization to provide technical assistance to municipalities.
- To establish a Board of Directors (Junta Directiva) to coordinate and guide GOP efforts in municipal development to replace the original advisory council and technical coordinating committee.
- To improve personnel stability and internal structure

Bank officials complained that the contractor did not discuss the draft report's recommendations with them and thus they were not given an opportunity to give

their opinion. USAID/Panama commented in its reply that it is highly unlikely that the contractor did not discuss his proposed recommendations with Bank officials. We found no record of any discussion of the report's recommendations with Bank officials during our review. We found that Bank officials had taken steps to implement one of the four recommendations but considered the other three recommendations as impractical and politically impossible to implement.

The first and second recommendation called for creating and expanding a new bureaucratic institution instead of strengthening an existing one. The third recommendation called for another try in establishing a new coordinating committee. Concerning the contractor's recommendation to create another institution, the USAID's Acting Chief of Development Resources said the evaluator became discouraged by the Bank's closed minded attitude on the matter of providing technical assistance to clients. The contractor was trying to find a way through which the Government of Panama could coordinate its services better.

USAID/Panama officials were apparently not in complete agreement with the contractor's recommendations and on December 1, 1978 indicated to the BNP's General Manager that the draft report's views were the contractor's and not necessarily AID's. However, USAID/Panama later reported that the Mission agreed in general with the evaluation report's recommendations.

The goal of the project is to strengthen the constitutional process by institutionalizing the participation of local government units to assure a larger role for identifying and meeting many of the socio-economic needs of their inhabitants in concert with national and regional development programs. The purpose of the project is to improve the quality and quantity of rural municipal administration, and productive activities (a) by concentrating on technical assistance and training in municipal administration, development planning and project preparation and implementation, and (b) by providing financial resources for food, rural development and nutrition projects.

The Bank has provided limited training and seminars to staff personnel of the municipalities and extended subloans to finance municipality projects in the service and production areas in efforts to accomplish the purpose and goals of the project. A minimum amount of technical assistance had been provided to the municipalities. Needed external technical assistance was not sought and the mechanism for advising and coordinating technical assistance was established but not implemented, mainly because of political reasons.

In our opinion many of the broad goals of the project have not been accomplished particularly an extension system to provide guidance and information to assist municipalities in planning, administration and implementation. We believe that an evaluation is needed to determine the extent that program goals and objectives have been achieved and what can be done in the time remaining to improve accomplishments. When we discussed this situation with USAID/Panama officials they agreed with our position but commented that an evaluation at a later date would be considerably more useful. They indicated a final evaluation of the project was scheduled for May 1980. However, it was doubtful if the project evaluation would be made because there would be other project evaluations underway at that time. On the other hand, it is expected the project will be evaluated during the second half of 1980.

## Recommendation No. 2

USAID/Panama, in conjunction with the National Bank of Panama, should evaluate the Rural and Municipal Development project.

### Contractor Evaluation Performance

Bank officials have not formally evaluated the performance of seven technical assistance contracts costing \$113,000 that were financed by the loan. The contracts called for the contractors to collaborate and participate with Bank personnel to provide technical assistance and training to municipalities in Panama. Bank officials informed us that while the contractors' performance had not been formally evaluated they consider the performance of all contractors satisfactory and had employed six of the contractors on a full-time basis. Two are still working for the Bank and the remaining four had resigned for various reasons.

We believe it may not be worthwhile now to evaluate the performance of the seven contractors as all services were provided prior to December 1978 and the services have been rated satisfactory by Bank officials. However, the Bank is planning to contract during 1980 for additional technical assistance costing about \$100,000. USAID/Panama should assure that the Bank evaluates each contractor's performance and that USAID/Panama's contract representative participates in all reviews and evaluations.

No recommendation is made because USAID/Panama's administrative procedures clearly list the contract representative's duties and responsibilities in monitoring a host government contract that is AID-financed.

### Lack of Compliance with Audit Report Requirement

The Bank had not submitted to USAID/Panama copies of the audit report that was prepared by the GOP's Controller General on the activities being financed with loan funds. We found no evidence that USAID/Panama had requested a copy of the audit report. USAID/Panama advised us that this was due to an oversight. Thus, no copy of the audit report had been received and reviewed by USAID/Panama.

Section 4.08 of the loan agreement, requires that the books and records of the Bank's implementing division be audited at least annually. Copies of the audit reports showing the results of the review were to be submitted to USAID/Panama. However, this was not done and USAID/Panama did not request copies of the audit reports.

We were advised by Bank officials that between November 28, 1975, (date the loan agreement was signed) and December 31, 1977, the activities of the implementing division were so small that they were audited along with the rest of the Bank's activities. A separate audit of only the implementing division's activities was prepared by the GOP's Controller General for calendar year 1978. We were advised by Bank officials that the GOP's Controller General had made a review of calendar year 1979 activities but they did not know when an audit report would be completed and submitted.

The GOP's Controller General audit report for calendar year 1978 focused on the financial activities and accounting for loan funds. We were advised that the 1979 report covered similar areas. The 1978 GOP Controller General audit report did not meet AID audit requirements. The report does not comment on whether the sub-loans financed from AID loan proceeds were used for the purposes authorized in the loan agreement. To satisfy this requirement the Controller General should have made some end-use checks of subborrowers. We were told that the GOP Controller General review was limited to the Bank's books and records.

USAID/Panama in commenting on a draft of this report stated, in part,

"Contrary to the assumptions in the Audit Report, the GOP Controller's reports are not similar to USG audits which focus on the financial and accounting aspects of specific projects. The GOP's controller's responsibility is of a fiscal nature and focuses on the financial activities of GOP agencies and control of public funds. The type of audit performed on this project is typical of most audits performed by the GOP Controller's Office both on GOP projects and other donor activities. To suggest that this process should be modified within the context of this \$4.0 million project is quite simply beyond the capabilities of AID and its Project Managers."

We agree that the "GOP Controller's reports are not similar to USG audits". Because the audits are different, we assume that is the reason the "A.I.D. Audit Requirements" were made a part of Implementation Letter No. 1 issued on November 28, 1975. The "A.I.D. Audit Requirements" set forth the type of audit and report required and provided for discussions of any questions that might arise or clarifications needed. From the results to date, it is clear that USAID/Panama did not take advantage of a management tool built into the loan agreement and implementing letters.

#### Recommendation No. 3

USAID/Panama should request the Bank to submit copies of audit reports prepared by the GOP Controller General on the review of loan funded activities.

#### Recommendation No. 4

USAID/Panama should meet with Bank officials to discuss its needs for audit coverage in future audits.

#### Lack of Signs and Markings

Signs have not always been displayed at construction sites to indicate participation by the United States in the financing of the project. Of the projects we visited which had completed buildings, only one of the buildings had a permanent sign attached. Vehicles were properly marked, but other commodities financed with loan funds did not have the required AID emblems affixed. We believe that more visits and follow-up action by USAID/Panama would have reduced the number of cases of insufficient signs and markings we noted during our site

visits. We found that people participating in the projects were aware of AID's assistance, but the general public has no way of knowing unless appropriate signs and markings are displayed.

Section 6.11 of the loan agreement and attachments to implementation letter number one call for the borrower to identify the project sites and mark goods with appropriate AID emblems for those items financed under the loan.

There were no signs at five of the ten project sites we visited. Two of the five sites without signs were farms which had been cleared and improved for raising crops. The other three were construction projects. All three buildings had been completed and one was ready for inauguration. Bank personnel were aware that signs should be maintained at the construction sites and signs were being constructed for installation. A Bank official informed us that permanent bronze plaques showing AID participation would be affixed to the buildings constructed under these projects.

AID emblems have not been affixed to commodities because Bank officials advised us they never instructed suppliers to comply with this AID requirement. While we found no evidence that USAID/Panama officials specifically instructed the Bank on the exact AID marking requirements, the loan agreement and certainly the data transmitted as an attachment to implementation letter number one clearly specified the markings and signs required. Therefore, we believe that the Bank was notified of the AID marking requirements and should have notified suppliers of the requirement.

USAID/Panama officials made infrequent visits to inspect project sites. We believe that USAID/Panama should have made more frequent visits to project sites and notified Bank officials when it found that sites and commodities were not properly marked.

We discussed the lack of signs and markings with USAID/Panama officials. We were advised that action would be taken to ensure that appropriate markings and signs are installed.

#### Recommendation No. 5

USAID/Panama should request the National Bank of Panama to fully comply with the marking requirements of loan agreement 525-T-044.

#### Delays in Processing Reimbursement Requests

Reimbursement requests for project expenditures have not been processed in a timely manner. Delays in processing the requests resulted from the lack of written reimbursement procedures and coordinated follow-up to obtain and review needed documentation. This situation prompted the Bank to finance project costs with its own resources. Had the Bank not done this, it would have delayed implementation of loan financed activities.

On March 31, 1980, the Bank informed us that six requests for reimbursement totaling \$1,220,468 had been submitted to USAID/Panama for which it had not been paid. We found the USAID/Panama Project Manager was holding four of these requests which totaled \$632,796. The requests had been held by the Project Manager from 14 to 108 days because verbally requested documentation had not been received from the Bank or had been received but not reviewed. One of the remaining two unpaid requests was being processed by the USAID/Panama Controller's office and the other request, reportedly sent to USAID/Panama, had not been recorded as being received.

To eliminate a possible obstacle to the successful implementation of loan funded activities, USAID/Panama made an advance of funds, \$460,000, to the Bank. During the early months of project activity, this advance was sufficient because activity was limited and because reimbursement requests were processed and paid in an average of 27 days from the date of receipt. However during the most recent period of activity, project expenditures have increased and it has taken USAID/Panama longer to process and pay the reimbursement requests. For example, reimbursement request no. 6 was submitted on September 28, 1978 and paid on June 27, 1979, 272 days after submission. Reimbursement request no. 7 took 184 days and no. 8 took 274 days. Although other reimbursement requests had been submitted, no. 8 was the last one paid at the time we initiated our review.

This delay in paying reimbursement requests had resulted in the Bank having to use its own funds to finance project activities. By April 1979, the Bank had expended about \$130,000 more than USAID/Panama had advanced. The Bank continued to expend funds and USAID/Panama paid some of the reimbursement requests but at no time between April 1979 and March 1980 was the Bank operating on AID advanced funds. As of March 31, 1980, the Bank claimed it had spent \$760,000 more than USAID/Panama had advanced (\$1,220,000 less \$460,000).

Our review of the records and discussions with USAID/Panama and Bank officials show that the lack of written reimbursement procedures and coordinated follow-up have resulted in the delayed payment of reimbursement requests. While we have no specific data to support the point that project activities have been delayed, we believe that a lack of AID funds on the part of the Bank may have delayed or prevented the approval of some projects.

The general procedures for the disbursement (payment of reimbursement requests) of funds are included in the basic loan agreement. Under Section 7.02 -- Disbursement for Local Costs -- the Bank may request disbursement (reimbursement) for the costs of goods and services procured for the project by submitting to USAID/Panama the supporting documentation prescribed in implementation letters. We found no specific supporting documentation prescribed in any of the implementation letters issued on this loan from inception through March 31, 1980.

In discussions with USAID/Panama officials, we were advised that initially (1976) it was agreed that the Bank would retain the supporting documentation for reimbursement requests, that is, invoices, receiving reports, source and origin certificates, construction engineering reports, and payrolls and submit to USAID/Panama a summary by subloan of the amounts paid out by the Bank as an attachment to a reimbursement voucher. The underlying premise being that the Bank was capable of carrying out AID's documentation requirements. USAID/Panama officials could then visit the Bank and make whatever checks were necessary to approve the

reimbursement request for payment. Correspondence between USAID/Panama and the Bank in 1976 confirm that the above procedures would be followed in processing reimbursement requests.

In 1978, USAID/Panama verbally requested that a detailed listing of disbursements be submitted along with the reimbursement voucher and summary statement. The additional information requested was needed to complete USAID/Panama disbursement records and to provide information for follow-up. The new procedures were oral and never communicated to the Bank in implementation letters as required by the loan agreement. We found no explanation why the new procedures were not transmitted to the Bank by an implementation letter. Of the six reimbursement requests submitted by the Bank since the change in procedures, we found no indication that the requested detailed listing was attached to the original voucher submitted. USAID/Panama advised us that delays in obtaining the detailed listings have contributed to the long periods of time required to process the reimbursement vouchers.

USAID/Panama stated in its comments on a draft of this report that the detailed listing of disbursements was requested in 1978 as a result of AID's new (at that time) requirement for project officers to administratively approve all payments based on the voucher, related invoices and supporting documentation. The changes made in 1978 were the minimum deemed necessary to allow the project officer to administratively approve reimbursement requests.

USAID/Panama's follow-up and review of reimbursement request have not always been well coordinated. For example, reimbursement request no. 8 for \$497,367 was received in June 1979 by USAID/Panama's Controller's office and transmitted to the Project Officer for administrative approval. Between June 1979 and February 1980, the Project Officer obtained from the Bank a detailed listing of expenditures and a corrected reimbursement request of \$496,767. The original request was in error due to a typographical mistake. The Project Officer disallowed expenditures of \$1,482 because equipment from an unallowable origin was purchased with these funds. He then administratively approved the voucher.

The reimbursement request was then forwarded to the Controller's Office where an additional 31 days passed before the request was certified for payment. During this period, the Controller's office did not request additional documentation from the Bank nor visit the Bank to review any documentation, but decided to make disallowances of \$426,679 and pay only \$70,088 of the amount requested. While there were some discussions between the Controller's Office and the Project Officer regarding the reimbursement request, the significance of the disallowances being made was not discussed. The Controller's Office did not discuss the disallowances with Bank officials.

In replying to a draft of this report, the USAID/Panama's Controller advised us that disallowances are not discussed with the claimants prior to processing vouchers. The claimants are provided a written statement of the reason for disallowances and the statement is given to the payee, with a copy of the voucher, at the time the check is delivered.

The disallowances on reimbursement request no. 8 were primarily due to the lack of information in the detailed listing submitted by the Bank as to the source and

origin of vehicles and equipment being financed. The source and origin certifications for vehicles and equipment purchased had not been required to be submitted to USAID/Panama for prior reimbursement requests. In replying to a draft of this report, the Controller advised us that the requirement for source and origin certifications was implemented because of an audit recommendation made on another USAID/Panama project. We found no evidence that this requirement had been formally communicated to the Bank.

The delays in getting requests processed was brought to the attention of USAID/Panama management on April 3, 1980. On April 15, 1980 a USAID/Panama financial analyst, the Project Officer and a USAID/Panama Finance Officer visited the Bank to review documentation supporting the pending reimbursement requests. After the documentation review, which was completed in one day, the USAID/Panama Controller approved for payment \$948,334 from reimbursement requests nos. 8 thru 12 which totaled \$1,210,234. Reimbursement request no. 6, (\$10,234) which was being reviewed by the Project Officer, was not included in the review. The difference between the amounts requested and approved of \$261,900 were for unexpended funds on a letter of credit (\$91,981), the value of a construction contract which was not readily available for review (\$60,000), the value of a used tractor (\$17,818), the cost for a releasing mortgage on a subproject lot (\$9,419), downward revision by the Bank of a reimbursement request (\$65,235) and other items including Panamanian taxes levied on local procurement (\$17,447). Thus, most of the expenditures requested for reimbursement have now been made.

In our draft report, we recommended that procedures be established for clarifying reimbursement instructions, coordinating reviews of documentation, and following up on requests to assure they are processed within a reasonable period of time. USAID/Panama advised us in its comments on the draft report that procedures have been established to ensure timely processing of reimbursement requests. The procedures include the recording of reimbursement requests in a "Date-Log" by loan agreement and preparing a weekly report showing the aging of vouchers on hand. In addition, as a result of meetings between Bank and USAID personnel, an implementation letter is in draft which confirms the procedures. Since the implementation letter has not been issued, we recommend:

#### Recommendation No. 6

USAID/Panama issue an implementation letter under loan no. 525-T-044 that describes the supporting documentation to be submitted with reimbursement requests.

#### Monitoring

Monitoring of project activities needs to be improved. We found that USAID/Panama officials were making infrequent visits to inspect subloan projects and were not preparing field trip reports.

USAID/Panama has relied on the Bank's management capability to monitor subloan activities. The majority of the projects being financed with subloans that we visited were experiencing problems requiring management's attention. To illustrate, accounting records at the project level were not properly maintained or

not maintained at all as was the case at the bean production project at the Municipio de Renacimiento. Vehicle maintenance problems were being experienced on the garbage collection project at the Municipio de David. Spare parts were not readily available. Trucks remained idle for 2 or 3 days or were cannibalized. Construction design problems (water pipe connections) were being experienced in the slaughterhouse project at the Municipio of Gualaca. These are a few examples of problems that could have been detected with effective monitoring.

Periodic field visits to selected projects should be made to identify problem areas, determine projects progress and evaluate the impact the project has on the rural poor. The field trip reports are needed to show the results of the inspection and as a basis for follow-up action when problem areas are identified.

In our field inspections of projects, we were informed that USAID/Panama officers seldom visit project sites. One Bank field representative advised us that over a 3 year period only one visit to the project had been made by USAID/Panama officers. We found only one field trip report in the files that reported visits to a project that was being inaugurated, two on-going projects and five proposed projects.

USAID/Panama's Project Officer said that projects were visited while inspecting other loan or grant activities. However, no field trip reports were prepared showing the results of the inspections. The Project Officer and USAID/Panama's Chief of Agriculture and Business Development Division said they were more concerned with assuring the Bank becomes a viable institution capable of implementing the project, including making loans to municipalities and disbursing loan funds. They advised us that it was their understanding that the Bank, as an intermediate credit institution, would implement and monitor all field projects. Therefore, it was not necessary for USAID/Panama officials to visit project sites to determine progress, problems and accomplishments.

We believe that USAID/Panama officials need to make selective visits to field projects to assure themselves that AID regulations and loan conditions are being complied with and to evaluate the impact the project is having. In other sections of this report, we comment on the lack of signs at construction sites identifying projects as AID financed and commodities purchased with AID funds that do not have affixed AID labels as well as other problems because of the lack of technical assistance to municipalities.

In its comments on a draft of this report, USAID/Panama stated, in part,:

"While 'monitoring' may be an end in itself to some observers, we feel that all the monitoring in the world can serve no useful purpose unless there exists a capacity on the part of the implementing agency to do something about the noted deficiencies. We simply do not understand how improved monitoring will in any way assist in resolving sub project problems unless we first establish an effective capability within the BNP (Bank) to address these problems. For these very reasons we have been focusing most of our attention on BNP/FODEM (Bank) issues so that the many problems identified by the auditors can be addressed."

We agree that 'monitoring' just for the sake of 'monitoring' should not be done. We also agree that the host country implementing agency must have the capacity to do something about the noted deficiencies. We believe that improved monitoring can and will materially help resolve problems. In our opinion, the first steps in solving any problem are realizing there is a problem and identifying the causes. By improved monitoring, the obstacles (causes) preventing the accomplishment of goals and objectives can be identified.

Recommendation No. 7

USAID/Panama should establish a schedule of field visits to project sites and require that trip reports be prepared on the results of the field visits.

LISTING OF RECOMMENDATIONS

Recommendation No. 1

USAID/Panama should not participate in any subloan projects after August 1, 1980 if the National Bank of Panama has not implemented a technical assistance and training program by that date. Any unutilized funds should be deobligated.

Recommendation No. 2

USAID/Panama, in conjunction with the National Bank of Panama, should evaluate the Rural and Municipal Development project.

Recommendation No. 3

USAID/Panama should request the Bank to submit copies of audit reports prepared by the GOP Controller General on the review of loan funded activities.

Recommendation No. 4

USAID/Panama should meet with Bank officials to discuss its needs for audit coverage in future audits.

Recommendation No. 5

USAID/Panama should request the National Bank of Panama to fully comply with the marking requirements of loan agreement 525-T-044.

Recommendation No. 6

USAID/Panama issue an implementation letter under loan no. 525-T-044 that describes the supporting documentation to be submitted with reimbursement requests.

Recommendation No. 7

USAID/Panama should establish a schedule of field visits to project sites and require that trip reports be prepared on the results of the field visits.

LIST OF REPORT RECIPIENTS

	<u>Copies</u>
Deputy Administrator, AID/W	1
Assistant Administrator - Bureau for Latin America and the Caribbean (LAC), AID/W	5
Assistant Administrator, Office of Legislative Affairs (LEG), AID/W	1
Controller, Office of Financial Management (OFM). AID/W	1
Mission Director, USAID/Panama	5
Country Officer	1
General Counsel, GC, AID/W	1
Director, LAC/DP/PO, AID/W	3
Director, OPA, AID/W	1
DS/DIU/DI, AID/W	4
Auditor General	1
AG/PPP, AID/W	1
AG/EMS/C&R, AID/W	12
PPC/E, AID/W	1
DS/RAD, AID/W	1
AAG/Africa (West) AID/W	1
AAG/Africa (East) Nairobi, Kenya	1
AAG/E, Cairo, Egypt	1
AAG/W, AID/W	1
AG/IIS, AID/W	1
IIC/IIS/Panama	1
AAG/LA Bolivia Residency	1
AAG/EA New Dehli Residency	1