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Auditor General

AUDIT REPORT

AID ORGANIZATION

USAID/URUGUAY

Audit Report Number 1-528-80-3

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Area Auditor General Latin America
Agency for International Development

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EXECUTIVE SUMMARY

Introduction

The Agency for International Development (AID) began to phase out economic assistance to Uruguay in FY 1978. No new programs have been initiated since then. All existing projects are scheduled to be completed by December 5, 1981, but USAID/Uruguay phaseout plans called for the turnover of residual AID activities to the U.S. Embassy by December 31, 1979. In order to ensure that all matters relative to close-out were taken into consideration, a final audit was done prior to close-out. This will allow the Agency to take corrective action on reported deficiencies before USAID/Uruguay personnel are terminated.

Scope

This final review was made to determine the effectiveness of the steps taken by USAID/Uruguay to phase out Mission operations and turn over residual AID activities to the U.S. Embassy. We reviewed financial obligations and activities, disposal of expendable supplies and non-expendable property, and transition plans for both projects and personnel.

Three loan projects totaling $11.5 million and five grant projects totaling $3.6 million were reviewed. Our purpose was to measure the progress made in achieving objectives and to identify problem areas requiring management attention.

Conclusions

USAID/Uruguay had made satisfactory progress and arrangements to phase out the program and turn over residual AID activities to the U.S. Embassy. At the conclusion of our field work in Uruguay, the major remaining phaseout item was to prepare a definitive and final transition plan. (See page 5 .)

Of the five grant projects shown in Exhibit B, four have been completed. The fifth project, Credit Union Development, has a terminal date of August 29, 1980. For all five projects, we found that the progress made in achieving objectives was satisfactory, and no significant deficiencies were noted.

Implementation of the Agricultural Research and Technical Assistance Loan 528-T-024 was unsatisfactory due to administrative, logistic, and counterpart problems.

As currently structured, the project cannot be carried out in the time remaining. Project redesign discussions were started in June 1978 but no agreement had been reached on how to proceed. Basic problems that defeated the original project remain unsolved. In the event an acceptable project design is forthcoming, success is contingent upon Host Government support. (See page 6 .)

The project objectives of the Uruguay Agricultural Cooperative Loan 528-T-025 have not been achieved although all $2 million of loan funds have been disbursed. Mission efforts to strengthen the implementing entity's institutional capability were unsuccessful. Long standing management and financial problems still persist. Purchase of a fruit packing line was pending. (See page 13.)

Recommendations

In regard to the Agricultural Research and Technical Assistance Loan 528-T-024, we made two recommendations. The first is that USAID/Uruguay should submit the new project design to AID/Washington for review and approval. The second recommendation is that USAID/Uruguay, prior to release of the remaining loan funds, should obtain irrefutable evidence that the Government of Uruguay will properly support the project, including but not limited to, providing sufficient qualified staff and funding support to ensure effective administration and implementation of the AID loan.

In our opinion, these recommendations should either provide the impetus to bring the project to a successful conclusion, or stop the further expenditure of loan funds on a project which would be certain to fail if allowed to continue under present circumstances.

For the Uruguay Agricultural Cooperative Loan 528-T-025, we recommend that USAID/Uruguay should request that CALFORU provide evidence of purchasing the fruit packing line. If CALFORU should decide not to purchase the line, a refund claim equal to the estimated cost of the line (approximately $600,000) should be made against CALFORU. We believe that without forceful action on the part of the Agency, CALFORU will not fulfill tne agreed upon purchase of the fruit packing line.

BACKGROUND

Since inception of economic assistance to Uruguay after World War II, the United States has provided about $160 million in loans and grants. The Agency's assistance was focused on development of nontraditional agricultural products and sectorial planning, tax administration, export promotion, development planning, and labor development. Major emphasis has been placed on agriculture, where AID's work in applied research has helped develop new methods for fruit, vegetable, and citrus production.

The focus of the AID program in Uruguay over the past few years has been directed towards the improvement and strengthening of agriculture production and marketing. Late in calendar year 1975, the United States, acting through the Agency for International Development (AID), signed three loan agreements for a total of $11.85 million to implement the AID program in Uruguay.

Loan agreement 528-T-024 was to expand and improve agricultural research and extension. Loan agreement 528-T-025 was to strengthen small farmer rural cooperatives through assistance in production and export marketing. Loan agreement 528-T-026 was to foster the establishment and expansion of agri-industries (food processing) with an export orientation. In addition to these loan agreements, AID provided technical assistance under five grant projects to assist low-income rural and urban workers through support for a national credit union federation and cooperative development. (Exhibit B.)

By calendar year 1978 implementation of activities financed by the loan agreements was progressing slowly. In April 1978, USAID/Uruguay prepared option papers for two of the loans (024 and 025) to evaluate what could be done to resolve implementation problems. A new AID Affairs Officer arrived in October 1978 and USAID/Uruguay and Government of Uruguay officials began re-designing the projects to accelerate implementation. Some redesigning efforts were still in process at the time we performed the field work on this audit.

Primary responsibility for administering the loan projects was assigned to various Uruguayan entities. USAID/Uruguay's role has been principally one of monitoring loan performance, and participating in reviews and evaluations.

AID/Washington determined in 1978 that an AID program for Uruguay was no longer needed because of rising per capita income levels (1974 - $1,190), increased potential savings, and Uruguay's access to substantial multilateral and other bilateral assistance. The phaseout of AID assistance began in fiscal year 1978 and all U.S. direct-hire personnel were scheduled to depart from Uruguay by December 31, 1979. After the transition date of December 31, 1979, one small grant and two loans will be active. Responsibility for residual AID activities and projects will be transferred to the U.S. Embassy. Most likely the Economic Officer will be responsible for handling AID's residual activities after the transition date. No new money has been planned for

Uruguay, and the program should be completely phased out by December 5, 1981.

This is a final audit of USAID/Uruguay. We limited the review to three loan projects and five grant projects for which AID had obligated $15.1 million and disbursed $7.9 million as of September 30, 1979 (Exhibit B). We did not review administrative and support activities, regional programs or planning of possible future programs. The period covered was from June 30, 1975, the cut-off date of our last audit, through September 30, 1979.

The purpose of our examination was to see if the program was conducted according to applicable AID regulations, the progress made in achieving objectives, and to identify problems requiring management attention. We also reviewed the adequacy and effectiveness of USAID/Uruguay close-out plans.

Our review included an examination of USAID/Uruguay project records and correspondence, and discussions with cognizant USAID/Uruguay, contractor, and cooperative officials. Visits were made to the Michigan State - Consortium offices in Montevideo to discuss contract implementation, and to the offices and facilities of Cooperativa Agropecuaria Limitada de Sociedades de Fomento Rural located in Montevideo. We visited the Cooperative's fertilizer storage facility and the packing/cold storage facility located near the city to observe the physical facilities and verify compliance with loan terms and commodities.

AUDIT FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

Phaseout of Mission Activities

Our review showed that plans to phase out the USAID/Uruguay Mission and turn over residual AID activities to the U.S. Embassy were proceeding as scheduled.

By the transition date of December 31, 1979, only one small grant and two loans will be active. The Project Assistance Completion Date (PACD) for the grant is August 29, 1980, and the PACD's for the loans are March 3, 1980, and December 5, 1981, respectively. At the completion of our field work on this audit, the parties involved in the transition of AID's residual activities needed to prepare a final transition plan in order to ensure a smooth turnover. We were subsequently advised that the transition was effectively being accomplished.

The USAID/Uruguay Mission was in the process of being phased out. The Controller departed post on September 27, 1979, and the AID Affairs Officer (AAO) was scheduled to depart not later than December 31, 1979. After that date, a U.S. Embassy Officer (most likely the Economic Officer) will be responsible for handling AID's residual activities.

Four direct-hire Uruguayan employees will remain working on AID's activities after December 31, 1979. The Program Officer and a Secretary each have termination dates of September 30, 1980, and the Loan Officer and the Chief Accountant each have termination dates of September 30, 1981. The Program Officer works half-time for AID and half-time for the Embassy Economic Section. Present plans call for this arrangement to continue to the termination date.

Until December 31, 1979, the AAO signed all financial and accounting reports and correspondence. Subsequent to December 31, 1979, the U.S. Embassy Foreign Affairs Administrative Support Officer (who is an authorized Certifying Officer) will sign all pay documents. He will continue to do so until AID's residual activities are completed. The USAID Regional Controller in Paraguay will be available on an as-needed basis and will periodically report on the status of residual AID activities and make recommendations accordingly.

Other residual activities which have been taken care of or have been planned for are as follows:

1. All operating expense obligations made prior to fiscal year 1979 have been liquidated or deobligated. During fiscal year 1979, $133,100 was obligated for operating expense and, based on the Controller's review, unliquidated obligations of $24,783.92 were carried over to fiscal year 1980. For FY 1980, an allotment of $100,000 was requested of AID Washington.

2. Non-expendable property totaled $68,073.95, as of September 30, 1979. This represented office and household furniture and equipment and one vehicle. The plan was for this property to be disposed of by transfer, sale, or grant-in-aid by December 31, 1979.

3. Expendable supplies and other non-accountable materials needed to be disposed of. The plan was to make a room-by-room "house cleaning" prior to December 31, 1979, to dispose of unneeded supplies, materials, files, and reference books.

4. Plans were underway for the Uruguayan employees of USAID/Uruguay to be allocated space within the U.S. Embassy's Economic/Commercial Section. This should provide effective coordination and proper supervision of daily activities after December 31, 1979.

At the completion of our field work, concerned parties had not formally met to prepare an inventory of residual AID activities in order to ensure an orderly transition and to make clear to all parties what remained to be done, and who had to do it. In our draft audit report, we recommended that the USAID/Uruguay AID Affairs Officer prepare a definitive and final transition plan. In response, the AAO stated that substance of the recommendation was being met by a series of meetings between concerned parties, including the Ambassador. Therefore, we make no recommendation here.

Implementation of Loan Activities

Loan activities had been delayed or were not satisfactorily implemented.

Delays and unsatisfactory implementation result primarily from the lack of support by the host country and inaction by implementing agencies. In order to conclude AID activities in Uruguay, action needs to be taken in several areas. We have included in this report recommendations of actions we believe are necessary to be implemented. The status of each loan project and our recommendations of necessary action are discussed below.

Agricultural Research and Technical Assistance - Loan 528-T-024

Implementation of the loan was unsatisfactory due to administrative, logistic, and counterpart problems.

As currently structured, the project cannot be carried out in the time remaining. Project redesign discussions were started in June 1978 but no agreement had been reached on how to proceed. Basic problems that defeated the original project remain unsolved. In the event an acceptable project re-design is forthcoming, success is contingent upon host government support. Remaining loan funds of $2 million should not be released until the host government provides irrefutable evidence of support.

The loan purpose is to assist the Government of Uruguay in carrying out a five-year program to achieve a substantial increase in agricultural production to augment export earnings, reduce food imports, and increase small and medium farmer income productivity. This objective is to be accomplished by: (a) expanding and improving the capacities and support services of the Research Unit staff headquarters and five regional experimental stations; and (b) completing a network of sixteen Experimental and Demonstration farms. At these Experimental and Demonstration Farms, new (crop rotation and grazing) systems are to be developed and then tested on nearby pilot farms. When proven economically and technically feasible at the pilot farm level, these new systems are to be disseminated to farmers.

The estimated project cost was $13.8 million, funded 65 percent by the Government of Uruguay and 35 percent by AID. The Government's contribution will pay for:

-- Additional Personnel and Operating Costs of the Research Unit	$ 2,177,000
-- Land Rentals for 16 New Demonstration Farms	430,000
-- Livestock	195,000
-- Buildings and Other Capital Investments	875,000
-- Research Unit Budget Supporting Expansion Plan	1,063,000
-- Additional Personnel Costs of Cooperating Agencies	4,220,000
	$ 8,960,000
The AID loan finances:	
-- Long and Short Term Advisors	1,980,000
-- Long and Short Term Training	706,000
-- Equipment	1,740,000
-- Contingency	424,000
	$ 4,850,000
Total Project Cost	$13,810,000

The implementing agency provided USAID/Uruguay with a single progress report which covered activities through calendar year 1977. The project status reported below is as of June 30, 1978, and is based on data collected as part of a USAID/Uruguay review as well as contractor reports. We were told by the Mission Project Manager and the Program Officer the situation has not materially changed and the data was still valid.

The following examples highlight specific shortcomings:

-- The project called for the addition of 187 new employees to the Research Unit staff by December 1979. At June 30, 1978, 149 people should have been added. Only 39 were hired.

-- The Michigan State Consortium Team was supposed to be provided office space, a bilingual secretary, an executive assistant and vehicles for technicians and Government field sites. About 37 vehicles were needed. The first team members arrived in May 1977. Adequate office space was provided in May 1978. A secretary and an administrative assistant have been employed intermittently since April 1978. (Office space and local help were paid from loan funds. The use of loan funds was justified on the basis of making the contract team more effective.) Eleven vehicles were provided in August 1978.

-- The Government agreed to provide adequate project administration at all levels. From 1975 to 1979, there have been four Ministers of Agriculture. During part of this time (December 1976 to February 1977; and April 1978 to January 1979), there was no Minister of Agriculture. Several Regional Stations have been without a manager.

-- The Government agreed to provide English language training to long-term training candidates. The initial training was inadequate and it was necessary for the Consortium to establish a program. The program was paid for by loan funds.

-- The Government agreed to provide in-service training courses. The plan called for approximately 78 courses. By January 1979, only one course had been given.

-- Research Unit staff levels should have reached 632 by June 30, 1978. There were 385 on board as of that date, of which only 47 were college-trained agronomists. The plan called for 157 to be college-trained agronomists by June 30, 1978.

-- The heart of the program was the improvement of the capacity of the personnel at the existing five regional stations, two Experimental/Demonstration farms, and the addition of fourteen Experimental/Demonstration farms. No new Experimental/Demonstration farms have been established and the effectiveness of established regional stations and the Experimental/Demonstration farms has been weakened by departure of technical personnel.

-- The Government agreed to several special covenants and warranties: (1) to make available agricultural credit on terms sufficient to permit the attainment of a new National Agricultural Plan; (2) to provide incentives for agriculture production and undertake additional agricultural marketing studies; (3) to identify small farmer problems; and (4) to assist small farmers through special programs relating to credit, marketing, and technical assistance. The Farm Credit Program scheduled for 1978 was never done. No incentives to stimulate production have been provided. The only agricultural studies undertaken were done by USAID/Uruguay. The Small Farmer Survey was done, but was paid for with loan funds, and no special programs for credit, marketing, and technical assistance have been undertaken.

In response to our draft report the AAO said, "Uruguayan Government has numerous agricultural credit programs, incentives for agriculture production, published marketing studies, has identified small farmer problems and has or supports special programs relating to credit marketing and technical assistance". Our statements were based on a review of USAID/Uruguay records. We found no support for these positive statements. USAID/Uruguay in its comprehensive analysis of Government of Uruguay obligations to the loan agreement noted that no special programs had been done up to June 1978. The Mission Project Manager and Program Officer, who did the analysis, confirmed to us that the analysis was still valid.

The reason for inadequate progress was the failure of the Government to support the project. The Government did not put in their counterpart funds. For 1976 and 1977, (no recent estimates were readily available) USAID/Uruguay estimated that less than 50 percent of the $3.2 million agreed to was spent.

In June 1977, the Minister of Agriculture ordered a halt to recruiting and hiring of Uruguayan personnel. The absolute freeze was subsequently lifted but the number of employees hired fell far short of promised levels as shown on page 8 of this report. Concurrent with this action, a program of political security clearance reviews was undertaken. In February 1978, fifteen Research Unit staff members were let go because they did not "qualify" for the proper clearance. This event triggered an atmosphere of uncertainty and fear among the staff. Several experiment station directors and other senior technicians resigned. The net result was that the project implementing agency was actually weaker than when the project started.

Work effort by the Consortium was also hurt. Promised logistic support did emerge but not to the degree anticipated. Support was substantially improved by paying counterpart costs with loan funds.

The consequences of the Government's failure to properly support the project were: (a) the Consortium team did not have adequate numbers of qualified technicians with whom to work in carrying out their assigned tasks. The lack of technicians coupled with the lack of logistic support decreased their effectiveness; (b) there were insufficient numbers of Uruguayan technicians to staff the five research centers, demonstration farms, and headquarters; and (c) very little progress was made in carrying out the work plan, in generating new technology, or in developing the system needed to transfer results to the farmer.

USAID/Uruguay was well aware of the constraints confronting the project. Files document Mission efforts, starting in July 1977. The University consortium showed equal concern. The Deans of the four schools comprising the University Consortium Council met in Uruguay in January 1978. Problems were discussed orally with Government officials and presented in writing to USAID/Uruguay.

The Mission recognized that unless the counterpart problem was resolved the project would fail. In January 1978, a decision was made to hold up on the procurement of $2 million worth of equipment (40 percent of the loan funds) until counterpart personnel were actually hired. This hold was still in effect at the conclusion of our audit field work. However, research equipment lists were in final form and had been put into an Invitation-For-Bid. Extension equipment requirements were unknown because the extension element of the project had to be redesigned.

During April/May 1978, the USAID/Uruguay, with the help of the Consortium, did an in-depth review and prepared a position paper. The paper outlined background, the current situation, and the essential basis for continuing the loan. At that time it was the concensus that the project could not be carried out as planned, and a complete new project design, including a change in the Consortium contract, was required.

Starting in June 1978, informal discussions were held but little progress was made due to the departure of key people. The AID Director and Project Manager both left Uruguay in July 1978, and the Minister of Agriculture post was vacant. The Research Unit Director would not act since project revision seemed imminent.

A new AID Affairs Officer arrived in October 1978 and immediately attempted to save the project. Through his efforts a working group was formed in November 1978 and formal meetings have been held intermittently since that time. A general outline of the new project has been formed. However, progress in the essential agriculture extension area was lacking because the Government extension representative had yet to be named. With the abandonment of the project objective of completing a network of 16 experimental and demonstration farms, a new way was needed to bring together research and extension.

Without the new project plan, little can be discussed in concrete terms. The former AID Director summed up the situation. For AID to be able to continue its assistance, there should be evidence that the Government will provide the money and personnel it agreed to. The level of counterpart resources must correspond closely to the requirements spelled out in the original project presentation and justification to AID. The critical limiting factor is the level of counterpart effort. We agree with this view.

Recommendation No. 1

USAID/Uruguay should submit the new project design to AID/Washington for review and approval prior to formal agreement on the design with the Government of Uruguay.

Recommendation No. 2

USAID/Uruguay, prior to release of the remaining loan funds, should obtain irrefutable evidence that the Government of Uruguay will properly support the project, including but not limited to, providing sufficient qualified staff and funding support to ensure effective administration and implementation of the AID loan.

Training Component

The long-and short-term training planned for in this project will not be accomplished. The long-term training will have a shortfall of 107 man/months and 10 candidates, and the time is past for selecting new candidates for training in the United States. Short-term training will likely fall far short of the work plan. Thus far only five technicians have received about 11 man/months of training. Failure of the Government of Uruguay Research Unit to provide sufficient candidates was the cause.

The original plan in the Capital Assistance Paper of March 26, 1975, had a training component of 648 man/months (36 fellowships of 18 months each) for Uruguayan technicians to study for Master's Degrees in various relevant disciplines. There were also 31 fellowships for short-term training of 5 to 6 months each, or 170 man/months. The total of 818 man/months was estimated at $706,000.

The training component was built into the U.S. University Consortium contract headed by Michigan State University. The contract between Michigan State and the Government of Uruguay was dated December 8, 1976, and showed:

Long-Term Training	$452,358
Short-Term Training	142,794
Total	$595,152

By the end of December 1976, Michigan State had prepared a work plan. This plan anticipated training 27 long-term candidates for Master's Degrees in the U.S. with an estimated 486 man/months needed, and 19 short-term candidates using an estimated 140 man/months.

Approximately 379 man/months of training were to be given to 17 candidates for Master's Degrees under the loan at an estimated cost of $373,905. The shortfall, when measured against the Michigan State work plan, is 107 man/months and 10 candidates. No new candidates should be sent for long-term training after the last two candidates leave in January 1980 because there will not be time enough left for them to finish before the terminal disbursement date of December 5, 1980.

The short-term training component can be used effectively for about one year from September 1979. Thus far only five technicians have received a total of about 11 man/months of training. From September to December 1978, three technicians had their training postponed at the request of the Government of Uruguay. They were not rescheduled. Compared to the Michigan State work plan, 129 man/months remain to be used. It seems doubtful that this present shortfall will be greatly reduced.

Training Follow-up

USAID/Uruguay had not made plans for a follow-up program for returned long-term-training participants.

AID Handbook 10 assigns Missions the responsibility to plan and develop a follow-up program and to maintain follow-up activities for returned participants for a minimum of three years. Missions are encouraged to conduct follow up, at least on a selective basis, for longer periods.

When an AID program in a country has been concluded, and no adverse political considerations exist, participant follow up continues to the extent the Ambassador may deem appropriate. This is a simple and convenient method for preserving the good will and interest in development engendered by the former AID program, particularly with participants who have reached leadership roles.

Four long-term participants who started training at Consortium universities in July 1977, had returned to Uruguay by December 1978. Michigan State University reported in its July-December 1978 semi-annual report that the four returnees were being used as agreed. A later report has not been received. The Michigan State contract ends on December 5, 1980.

Recommendation No. 3

USAID/Uruguay should prepare and implement plans for a follow-up program for returned long-term-training participants.

Uruguay Agricultural Cooperative - Loan 528-T-025

All $2 million of loan funds have been disbursed, but project objectives have not been achieved. Mission efforts to strengthen the implementing entity's institutional capability were unsuccessful. Long standing management and financial problems still persist.

Late in 1977, in an effort to obtain corrective actions, USAID/Uruguay froze the use of $780,000 earmarked for procurement of two fruit packing lines and a cold storage facility. Then USAID/Uruguay management changed in October 1978. The new AID Affairs Officer's handling of the loan was inconsistent with that of his predecessor. A previously discarded proposal to use the last $780,000 for the purchase of fertilizer and to use local resources to purchase the fruit packing lines and cold storage facility was accepted. Earlier demands for evidence of improved management and financial condition were replaced by a list of conditions precedent to disbursement of a non-substantial nature. At the time of our review, loan action was still incomplete and the agreed upon purchase of a fruit packing line was pending.

The overall goal of this loan was to support Government of Uruguay objectives, to achieve a sustained increase in agricultural production, to augment export earnings, reduce food imports, and increase small and medium farmer income and productivity. The purpose was to assist Cooperativa Agropecuaria Limitada de Sociedades de Fomento Rural (CALFORU) to strengthen its institutional capacity to: (a) expand its marketing system: (b) improve its farm supply distribution system: and (c) efficiently manage its expanded activities to better meet the needs of local affiliates and their members.

Project costs were estimated at $3.4 million:

Counterpart Funds	
CALFORU	$ 390,135
Local Source Credit	631,300
Affiliate Cooperative - Construction	362,656
	$1,384,091
Loan Funds	
Fertilizer	$ 965,500
Technical Assistance and Training	100,000
Fruit Packing lines, cold storage facilities, support equipment	934,500
	$2,000,000
	$3,384,091

Efforts to achieve the loan objective to assist CALFORU strengthen its institutional capacity were hindered early on. Concrete evidence reported to USAID/Uruguay in November 1975 disclosed that basic internal financial controls were not in place at CALFORU. An independent accountant found the records in such bad shape that the firm was unable to undertake a financial audit. USAID/Uruguay decided to proceed with disbursements anyway and give CALFORU time to work out the management problems.

As part of a limited scope evaluation done by USAID/Uruguay in early 1977, the evaluation team checked action taken to correct identified management problems. The evaluation showed little progress being made. Implementation had progressed but was slower than expected and the targets reached were to a lesser degree than anticipated. The conclusions drawn from the evaluation were qualified because no data collection system had been established and therefore no specific supporting data had been developed. Some conclusions were:

-- Implementation in general contributed to achievement of project goals.

-- Implementation was slower than expected and institutional as well as human resource development was insufficient.

-- As a direct result of the lack of adequate management capabilities, CALFORU has been delayed in the preparation of: (a) the five-year development plan; (b) annual operating budget and operational plan; (c) financial and progress reports; and (c) economic analysis to support production, credit sales, and price policies.

In an attempt to solve the problems identified, CALFORU agreed to contract an Administrative Services Consulting firm. Such services qualified for financing under the loan.

Despite the shortcomings identified in the evaluation, the AID Affairs Officer approved the second purchase of fertilizer, bringing the total for that purpose to $965,000. USAID/Uruguay staff (Rural Development Officer, Controller, and Loan Officer) advised against the release of funds. However, CALFORU had appealed to the AID Affairs Officer and said that if the second tranche was not released the fertilizer program (farm supply distribution) would be hampered -- hurting the small farmer. Also, CALFORU might go bankrupt because of severe cash flow problems.

In April 1978, one year later, the situation had deteriorated. USAID/Uruguay undertook a comprehensive review with the view of presenting a set of alternative actions. The option paper revealed several important points:

-- Management studies started in 1977 were still underway.

-- Procurement of the fruit packing line (marketing) seemed imminent but no site for installation had been secured. Original plans had been abandoned.

-- CALFORU's financial condition reflected the continuance of unsound operational and management practices and resulted in a precarious financial position. A loss of new pesos 1,590,000 (approximately $300,000) was suffered in a potato seed venture that failed.

CALFORU was pressing for the release of additional loan funds to be used for the purchase of fertilizer over and above the amount in the approved program, promising to use funds generated by the sale of fertilizer to purchase cold storage facilities. The AID Affairs Officer asked the AID Regional Legal Advisor to determine whether an additional "tranche" of fertilizer could be purchased under the loan.

In a written opinion dated April 5, 1978, the legal advisor said, "...I am of the opinion that the AID Representative to Uruguay does not have the authority to approve a substantial shift in the application of loan funds (without doubt over $350 thousand* out of a total $2 million loan, and a 50% increase in the dollar value of fertilizer originally contemplated is substantial) from one project component to another. Further, an amendment to Annex I would be required."

The Mission decided to hold up on the loan until CALFORU provided evidence of an improved management and financial situation. Evidence was to consist of a new management team functioning effectively, substantial collection of accounts/notes receivable, and a reduction in debt.

A new AID Affairs Officer arrived at post in October 1978. About the same time, CALFORU's independent auditors presented their report. In a memo dated October 23, 1978, the Mission Controller said as a conclusion to a review of the report, "In my opinion, CALFORU needs to take certain affirmative steps to put its house in order. The steadily increasing receivables and bank debt indicate to this writer that CALFORU does not have firm control of its operations. If CALFORU does not demonstrate an ability to collect on its debts, the entire financial well being of the firm is in doubt." The Mission Controller's concern was well founded. A quick comparison of key accounts shows the deteriorating financial condition:

* Increased later to $780,000.

As of April 30 - Stated in 000's of New Pesos

	1976	1977	1978	1979*
Cash	433	416	764	1,729
Receivables	2,441	8,664	15,044	20,356
Inventory	5,692	6,578	12,243	13,678
Total	8,566	15,658	28,051	35,763
Accounts Payable	5,494	13,941	22,681	29,594
Notes Payable	1,749	2,566	6,238	8,855
Total	7,243	16,507	28,919	38,449
Ratio - Liquid Assets to Payables				
	1.18	.948	.970	.930

*(Note: Not audited. 1979 not reviewed by the Controller)

During October - December 1978, the AID Affairs Officer held a series of conversations and negotiations with CALFORU and worked out a plan to complete disbursement of the loan quickly. The agreement evidenced by Implementation Letter No. 14, dated January 12, 1979, is essentially the action reported to the AID/Washington Latin American/Caribbean Office of Development Resources in December 1978. USAID/Uruguay agreed to release the remaining $780,000 for purchase of fertilizer in exchange for:

-- actions taken on a discrepancy list and on audit recommendations.

-- purchase of one fruit packing line with CALFORU resources and leasing of cold storage and warehouse facilities.

Before proceeding with the agreement, the AID Affairs Officer consulted with the new Regional Legal Advisor and obtained his opinion. This opinion was that: (1) "AID/W must approve the use of additional funds for fertilizer purchases; and (2) Annex I (the detailed project description) of the loan agreement would have to be amended via an implementation letter". Nevertheless, in a status report to the Latin America Bureau (LAC/DR) dated December 28, 1978, the AID Affairs Officer reported that changes in the use of loan funds were "appropriately within the limits of the existing authorization and loan agreement, and fully meet the original project purpose". In other words, the loan funds earmarked for the purchase of a packing line and cold storage facilities could be used to purchase fertilizer.

Of interest here are several passages from Handbook 3, Chapter 10, paragraph 10D: "Therefore, the Project Agreement should clearly set forth firm commitments or limitations, which must be complied with unless or until the agreement is amended or terminated". ..."Refinement of the description during the drafting and negotiation of the Project Agreement is permitted, but substantive changes in the description, from that in the authorization, would need approval of an authorizing official (underlining supplied)". ..."The initial description should be drafted so that a need to amend it would be unlikely, whereas provision is made to permit minor changes (underlining supplied) in the more detailed description by means short of formal amendment of the Agreement."

We believe that the changes in the use of loan funds were substantial, and that approval to amend the agreement should have been obtained in writing by the AID Affairs Officer from AID/Washington. In response to our draft report, the AID Affairs Officer claimed tentative approval by letter from the Latin America Bureau in January 1979, and approval in detail during AID/Washington consultation in February 1979. We found no approval in writing during our review of USAID/Uruguay files.

We reviewed the actions taken by CALFORU to meet the conditions precedent imposed by USAID/Uruguay in regard to release of the last $780,000 of loan funds. Conditions were listed in two parts: those to be done prior to release of funds, and those to be done sometime in the future. The conditions to be satisfied prior to release of funds were not substantive. Among other things CALFORU was requested to:

-- Name a general manager and financial manager.

-- Submit a plan showing how the $780,000 would be used.

-- Visit affiliates more frequently.

-- Request affiliates to submit lists of accounts receivable, and establish a system to obtain this data on a continuing basis.

-- Request affiliates to list items given as collateral to CALFORU.

-- Take an inventory of harvest boxes and all other merchandize.

-- Adjust current quarter budgets and prepare 1979/80 budgets.

In a January 9, 1979 letter CALFORU said they had leased the required cold storage space and had arranged the purchase of a fruit packing line. Citing these actions CALFORU asked for the release of the $780,000.

AID released the funds on January 12, 1979. CALFORU spent the money for fertilizer and leased cold storage, warehouse, and packing line space. The fruit packing line was never purchased. In a October 4, 1979, letter, CALFORU said they were still up in the air on what to do. Several options were under consideration and a decision is supposed to be forthcoming. One option is not to buy the fruit packing line.

We could make no overall quantitative assessment of progress made against goals and objectives. The planned data collection system was never established and no evaluations have been done since 1977. Quarterly reports did not contain necessary data.

In conclusion, the last $780,000 of loan funds were disbursed without knowing with some degree of confidence whether acceptable progress was being made toward meeting project goals and objectives. The substantial change in project mix (financing more fertilizer) was approved and implemented by the AID Affairs Officer without prior approval by AID/Washington. AID/Washington was knowledgeable of the action taken but only to a lesser degree than the full picture.

Solving long standing management and financial problems was important to achieving project goals and objectives. The problems were never adequately corrected. Loan action is still incomplete. CALFORU has yet to purchase the fruit packing line despite prior claims to having arranged to do so.

Recommendation No. 4

USAID/Uruguay should request that CALFORU provide evidence of purchasing the fruit packing line. If CALFORU should decide not to purchase the line, a refund claim equal to the estimated cost of the line (approximately $600,000) should be made against CALFORU.

Agri-Industry Development - Loan 528-T-026

The most significant conditions we found were:

-- Loan implementation has slipped 18 months since project inception on September 3, 1975. However, the project should be completed by the March 3, 1980, terminal disbursement date, and it appears that the goal and purposes will be reached.

-- Since June 6, 1978, USAID/Uruguay has not received the project status and progress reports necessary to properly monitor the project.

-- End-use checks of loan-financed equipment need to be scheduled.

-- Annual financial audits have never been made.

The goal of the project was to create an agri-industrial infrastructure capable of expanding non-traditional exports. This should contribute to a diversification of agricultural production, increased foreign exchange earnings, and increased production, employment, and income opportunities to small and medium farmers in Uruguay. In support of the goal were three purposes: (1) to provide a package of financial and technical services to private entrepreneurs and cooperatives for the establishment, modernization, or expansion of agri-industries (food processing); (2) to help establish an effective delivery system for these services; and (3) to stimulate new production and marketing alternatives for small and medium farmers through the establishment of viable agri-industrial enterprises.

The loan agreement, signed on September 3, 1975, for $5 million, was subsequently reduced to $4,644,393. The original terminal disbursement date of September 3, 1978, has been extended twice to March 3, 1980, to allow sub-borrowers to complete their AID-financed purchases.

Implementation of the loan agreement had a slow start due primarily to: (1) a need to complete staffing of the Evaluation Unit of the Ministry of Industry and Energy (the Uruguayan implementing agency); (2) a need to expand and intensify promotional effort among banks and the industrial sector; and (3) slower than expected completion of feasibility studies for sub-projects. Considerable effort by the Central Bank of Uruguay was instrumental in overcoming these start-up problems. By the end of December 1976, the Evaluation Unit staffing was nearly complete, consulations with the banking and industrial sectors were well advanced, and information brochures on AID-sponsored industrial sector loans had been widely distributed. The first sub-project for a fruit packing and cold storage operation was approved in December 1976.

By July 31, 1979, the Evaluation Unit had completed their assessment of proposed projects, the Central Bank of Uruguay had completed approval and financial actions, and most sub-borrowers had placed equipment and machinery orders. Thus the project, after a late start, seems to be moving toward a fairly successful completion. Investments have been made, sub-projects were in place, and promotion, analysis, and financing institutions have been set up and were functioning.

A total of 12 sub-loans have been approved and all of the sub-borrowers have initiated procurement, i.e. opened letters of credit. As of September 30, 1979, cash disbursements by AID for equipment and technical assistance were $978,426.87.

The terminal shipping and disbursement dates were five months away, as of our audit cut-off date. January and February are traditional summer vacation months in Uruguay. The Regional Controller in Paraguay has emphasized that, in these circumstances, proper financial tracking of each sub-borrower's status needs immediate attention. USAID/Uruguay should be obtaining frequent status reports on procurement actions, letters of credit opened, dates of shipments, and dates of disbursements.

Project Status and Progress Reports

Since June 6, 1978, USAID/Uruguay has not received the project status and progress reports required by Implementation Letter No. 5 dated May 28, 1976. USAID/Uruguay has not followed up in writing to obtain such reports. The USAID Loan Officer said he has asked repeatedly but the reports have not been forthcoming. The reason given was that the employee who had been preparing these reports left the organization and no one has prepared them since then.

The required reports are:

(1) A monthly Project Status Report showing the status of AID loan funds, counterpart, and subloan applications.

(2) Quarterly progress reports on subloans and technical assistance:

(a) Progress Report on Agri-Industry Development Subprojects which shows subproject status, financing, and other data.

(b) Progress Report on Technical Assistance to Agro-Industry Development Subprojects.

(c) Technical Assistance to the Unidad Asesora and Contracts for Professional Services.

(d) Guarantees by the Central Bank Credit Guaranty Fund designed to help USAID be informed on the status of credit guarantee activities related to subproject financing.

(e) Progress Report on Equipment Use Control and Monitoring Report.

(3) Quarterly Shipping Reports which show deliveries of loan-financed equipment and supplies.

Responsibility for implementing the loan agreement was designated by the Government of Uruguay to the Ministry of Industry and Energy (MIE). The Asesora (Evaluation Unit) of the MIE was authorized to serve as the technical review group and principal executing agency for the administration of this project. One of their duties was to prepare and submit the required reports to USAID/Uruguay.

Utilization Reports

Quarterly shipping reports and quarterly progress reports on equipment use and monitoring are required but these reports have not been prepared by the Evaluation Unit since the period ended March 31, 1978. Thus USAID/Uruguay has not complied effectively with Recommendation No. 3 in our prior audit report issued October 28, 1975.

Our recommendation read, "USAID, in coordination with the borrower, should develop and assure implementation of commodity arrival and disposition control requirements for the new loan". USAID/Uruguay's response was, "USAID plans to issue an implementation letter relating to T-026 requesting the borrower to install a system for monitoring commodity arrival and disposition controls along the lines indicated in AID Handbook No. 15, Chapter 10. Mission will review with borrower plans and procedures for implementing the system. Thereafter, Mission will undertake periodic spot checks to determine if the system is functioning properly".

Subsequently USAID/Uruguay reported they issued Implementation Letter No. 5 on May 28, 1976, which required the borrower to establish a monitoring and reporting system for the arrival and disposition of commodities financed under the loan. On June 14, 1976, the AAG/LA office closed the recommendation.

Of $4,380,666 for equipment, as of August 31, 1979, $721,161 had been disbursed. Because of the lack of reports, exactly what equipment had been received by the loan recipients was not known. Thus USAID/Uruguay is lacking some basic data which will be needed later to make proper end-use inspections of loan-financed equipment.

Recommendation No. 5

USAID/Uruguay should demand in a formal written request to the Ministry of Industry and Energy that the reports required by Implementation Letter No. 5 be prepared and submitted by Unidad Asesora on a timely basis.

End-Use Checks

USAID/Uruguay has not made any end-use checks of equipment received by loan recipients. Thus far only 2 of 12 borrowers have received equipment totaling $721,161. Some equipment had been installed and was observed in operation by the USAID Loan Officer when he visited the two borrowers on January 13, 1978, and November 16, 1978, respectively. However, he did not make any end-use checks.

Exhibit A lists the 12 borrowers and shows the nature of the business for which each loan was made, and the amount approved. By completion of the project, each of the borrowers should have been either visited or scheduled for a visit to make an end-use examination. There should be a determination and/or verification that equipment financed with AID funds has in fact been received, installed (if necessary), and in use for the purpose intended.

Recommendation No. 6

USAID/Uruguay should schedule end-use examinations of the equipment received by the borrowers shown in Exhibit A.

Annual Financial Audit

The annual financial audits during the disbursement period of the AID loan, as required by Implementation Letter No. 5, have not been made. There was no evidence of follow up requests by the Mission to obtain such audits.

This report is supposed to be prepared at least annually during the disbursement period of the AID loan. The report should provide a good financial summary of all loan activities and disbursements as well as a description of accomplishments during the report period. The Controller General (Tribunal de Cuentas) of the Government of Uruguay may prepare the report.

Recommendation No. 7

USAID/Uruguay should request the Controller General of the Government of Uruguay to immediately schedule a financial audit of the Agri-Industry Development loan.

Evaluation Reports

One evaluation of the Agri-Industry Development loan has been made covering the period from September 1975 to December 1977. The next scheduled evaluation was deferred until completion of the project. A final evaluation has yet to be scheduled.

An evaluation plan was established by Implementation Letter No. 7, dated September 10, 1976. The initial evaluation was suggested for June 1977 with subsequent dates to be established by the Ministry of Industry and Energy with USAID concurrence. Later this schedule was changed to September 1977.

After several delays and postponements, the loan evaluation was concluded on February 15, 1978. It was expected that the report would be forwarded to AID Washington by the end of March 1978, but this didn't happen until June 12, 1978. Although about a year-and-a-half behind schedule, the evaluation showed the project to be basically sound. The project was continued without change.

On June 21, 1979, USAID/Uruguay deferred the scheduled FY 1979 evaluation until project completion. The extended terminal disbursement date (originally September 3, 1978) is March 3, 1980. The project should be completed within about six months thereafter. At that time, the Embassy Officer handling AID affairs will request the Evaluation Unit of the Ministry of Industry and Energy to make a final evaluation.

EXHIBIT A

USAID/URUGUAY
AGRI-INDUSTRY DEVELOPMENT
AID LOAN 528-T-026
LISTING OF APPROVED SUB-LOANS

Name of Borrower	Type of Business	Amount Approved
Lipena, S.A.	Corned Beef Processing Plant	$ 451,064
Massaro, S.A.	Packing of Fruit & Fruit Byproducts	418,278
Terfrusa	Cold Storage for Fruit	270,096
Lactaria Nueva Helvecia	Dairy Products Plant	436,779
Coleme	Dairy Products Plant (Cooperative)	529,612
Cooperative San Jacinto	Farmer's Machinery Service	60,148
Sudy and Cia., S.A.	Vegetable Dehydration	335,544
Frigorifica Arbiza, S.A.	Cold Storage Plant	547,540
Urreta, S.A.	Fruit Concentrates	684,159
Queseria Helvetica	Dairy Products Plant	122,780
Jean Carsey Touya	Chicken Processing Plant	317,266
Coleque	Dairy Products Plant (Cooperative)	207,400
		$4,380,666

EXHIBIT B

USAID/URUGUAY
AID-FINANCED PROJECTS
As of September 30, 1979

Project Name and No.		Obligated	Disbursed	Unliquidated Obligations
Grants				
Agri-Institutional Development	- 041	$ 2,734,000	$2,734,000	-0-
Economic & Management Training	- 096	363,238	363,238	-0-
Fiscal Policy Management	- 098	231,907	231,907	-0-
Cooperative Development	- 105	100,000	92,861	7,139
Credit Union Development	- 106	200,000	164,835	35,165
Loans				
Agricultural Research and Technical Assistance	- 024	4,850,000	1,453,056	3,396,944
Agricultural Cooperative	- 025	2,000,000	1,939,350	60,650
Agri-Industry Development	- 026	4,644,393	978,427	3,665,966
Total		$15,123,538	$7,957,674	$7,165,864

LISTING OF RECOMMENDATIONS

Recommendation No. 1

USAID/Uruguay should submit the new project design to AID/Washington for review and approval prior to formal agreement on the design with the Government of Uruguay.

Recommendation No. 2

USAID/Uruguay, prior to release of the remaining loan funds, should obtain irrefutable evidence that the Government of Uruguay will properly support the project, including but not limited to, providing sufficient qualified staff and funding support to ensure effective administration and implementation of the AID loan.

Recommendation No. 3

USAID/Uruguay should prepare and implement plans for a follow-up program for returned long-term-training participants.

Recommendation No. 4

USAID/Uruguay should request that CALFORU provide evidence of purchasing the fruit packing line. If CALFORU should decide not to purchase the line, a refund claim equal to the estimated cost of the line (approximately $600,000) should be made against CALFORU.

Recommendation No. 5

USAID/Uruguay should demand in a formal written request to the Ministry of Industry and Energy that the reports required by Implementation Letter No. 5 be prepared and submitted by Unidad Asesora on a timely basis.

Recommendation No. 6

USAID/Uruguay should schedule end-use examinations of the equipment received by the borrowers shown in Exhibit A.

Recommendation No. 7

USAID/Uruguay should request the Controller General of the Government of Uruguay to immediately schedule a financial audit of the Agri-Industry Development loan.

APPENDIX B

REPORT RECIPIENTS

	Copies
Deputy Administrator, AID/W	1
Assistant Administrator - Bureau for Latin America and the Caribbean (LAC), AID/W	1
Assistant Administrator, Office of Legislative Affairs (LEG), AID/W	1
Controller, Office of Financial Management (OFM), AID/W	1
General Counsel, GC, AID/W	1
AID Affairs Officer, USAID/Uruguay	5
Country Officer, ARA/ECA, AID/W	1
Director, LAC/DP/PO, AID/W	3
Director, OPA, AID/W	1
DS/DIU/DI, Room 813, SA-18, AID/W	4
Auditor General, AID/W	1
AAG/AFRICA (West), AID/W	1
AAG/AFRICA (East), Nairobi, Kenya	1
AAG/E, Cairo, Egypt	1
AAG/EA, Manila, Phillipines	1
AAG/W, AID/W	1
AG/EMS/C&R, AID/W	12
AG/PPP, AID/W	1
Inspector-In-Charge, IIS/Panama	1