

PDAAP-894

101136246

**MONITORING DOLLAR AND LOCAL CURRENCY  
RESOURCES UNDER ECONOMIC RECOVERY AND  
P.L. 480 TITLE I AND III PROGRAMS  
IN HONDURAS**

**MEMORANDUM SURVEY REPORT NO. 1-522-85-1**

**October 25, 1984**

MEMORANDUM SURVEY REPORT

**MONITORING DOLLAR AND LOCAL CURRENCY  
RESOURCES UNDER ECONOMIC RECOVERY AND  
P.L. 480 TITLE I AND III PROGRAMS  
IN HONDURAS**

SUMMARY

USAID/Honduras (USAID) and the Government of Honduras (GOH) started the above programs for balance of payments support in order to promote financial stabilization and economic recovery. The USAID has obligated \$150 million under these programs since June 1982. The principal purpose of the survey was to determine the effectiveness of program controls and monitoring over the resources provided by AID and local currency generated from these resources. The Government of Honduras had established a number of central systems and was planning other oversight actions with respect to these programs. However, we also found some weaknesses in program controls and monitoring which the USAID has corrected or agreed to correct. We are making no formal recommendations because USAID/H is taking action to address the weaknesses we discovered, and because we plan to review these programs again at a later date.

BACKGROUND

Economic Recovery Program

On September 24, 1982, AID started a financial assistance program to the Government of Honduras (GOH) for balance of payments support to promote financial stabilization and economic recovery. The funds have been provided under the Economic Recovery Program (Agreement No. 522-0230). As of July 31, 1984, AID had obligated \$121 million under this program of which \$91 million had been transferred to the GOH. These resources were both loan (\$70,550,000) and grant (\$50,450,000) financed.

The status of these funds as of July 31, 1984 was:

<u>Agreement</u>	<u>Date</u>	<u>Amount</u>		<u>Date</u>
		<u>Obligated</u>	<u>Disbursed</u>	<u>Disbursed</u>
Original	9/24/82	\$35,000,000	\$35,000,000	9/29/82
Amend. 1	3/29/83	3,000,000	3,000,000	4/29/83
Amend. 2	7/30/83	15,000,000	15,000,000	08/1/83
Amend. 3	9/30/83	8,000,000	8,000,000	03/7/84
Amend. 4	9/30/83	30,000,000	4,000,000	03/7/84
			26,000,000	6/12/84
Amend. 7	7/9/84	30,000,000	-0-	---
TOTALS		<u>\$121,000,000</u>	<u>\$91,000,000</u>	

U.S. dollar funds were disbursed to the GOH on a cash transfer basis. One condition to the use of the dollar funds was that the GOH make available an equivalent amount of foreign exchange to import from the United States raw materials, intermediate goods, and spare parts within 12 months from the dates of the respective agreements. Another condition was that the equivalent amount in local currency (counterpart funds) was to be deposited into a special account and used for purposes agreed to by the two governments.

As of June 30, 1984, the GOH had deposited the equivalent of \$91 million of local currency in special accounts of which \$45.6 million had been disbursed. The funds have been programmed for 109 development activities such as GOH counterpart for AID and other donor projects, credit for the private sector and PVO projects. In addition to the above, the GOH had earned the equivalent of \$2.2 million of interest on loans to the private sector of which the equivalent of \$702,165 had been disbursed for two development activities.

The program agreements also provided that the GOH would comply with an International Monetary Fund (IMF) Standby Agreement and take other steps to promote economic recovery as required by conditions precedent to disbursement and as covenants to the agreements.

The USAID and the Ministry of Finance are responsible for programming and monitoring the use of local currency. The Central Bank is responsible for (1) checking the prices of imports and exports to prevent the flight of foreign exchange, (2) attributing imports to dollars provided under the program, and (3) maintaining the special account for local currency generated under the program.

#### P.L. 480 Title I and III Programs

AID has issued seven Purchase Authorizations to the GOH to import \$29 million of wheat under Title I and III agreements signed between June 11, 1982 and June 19, 1984. The U.S. Government loaned the GOH the funds to buy the wheat and the GOH agreed to use the local currency generated from the sale of the wheat for mutually agreed development activities. Under the Title III agreements, the U.S. Government forgives the purchase price of the wheat if the GOH uses the local currency generated for specific Food for Development projects.

As of June 30, 1984, \$16,872,926 of principal and \$561,971 of interest had been paid by the millers and deposited into the

special account. The USAID and GOH had programmed the equivalent of \$10 million under Title III program for eleven activities and \$6 million under Title I program for seventeen activities as of June 30, 1984, of which \$13,319,070 had been disbursed.

The Honduran Agricultural Marketing Institute is responsible for purchasing and selling the wheat imported under the program. The Ministry of Finance is responsible for collecting the sales proceeds from the millers and accounting for the local currency disbursed for approved projects.

### PURPOSE AND SCOPE

A survey of the Economic Recovery Program and the P.L. 480 Title I and III Programs was made in July and August 1984. The objective of the survey was to determine the effectiveness of program controls and monitoring over the resources provided by AID as well as the local currency generated in connection with the transfer of these resources. An in-depth audit of these programs was not conducted.

We interviewed USAID, Central Bank and Ministry of Finance personnel and reviewed pertinent records of these institutions. Our review covered the amounts disbursed as of July 31, 1984: \$91 million in economic support funds and \$13.3 million in P.L. 480 Titles I and III resources.

### SURVEY FINDINGS

#### Economic Recovery Program Price Control Unit

USAID and Central Bank officials agreed in December 1983 to establish a Price Control Unit to verify that import transactions are not overpriced and export transactions are not underpriced in order to prevent capital flight. On April 26, 1984, the USAID approved a Central Bank request with Implementation Letter No. 72 to provide the equivalent of \$92,500 in local currency to establish a Price Control Unit and finance its first year of operation. The Central Bank staffed this Unit with three professionals and one secretary in June 1984. The Unit had not started price-checking operations because they were still getting organized and had not fully developed its policies and procedures.

In early August 1984, we reviewed the activities of the Price Control Unit (Unit) and found the following:

- The Chief of the Price Control Unit reports to the Chief of the Department of Exterior Regulation. This is the Department which approves import and export licenses.
- The Unit has taken the following actions:
  - a) They have begun to analyze and summarize prices, specifications and other data of commodities imported and exported to develop a price list.
  - b) They have subscribed to various publications to obtain information on commodity prices and specifications as well as importers and exporters in the U.S.
  - c) They reviewed the operation of the Price Control Unit in San Salvador for one week in July 1984 in order to gain information on administering this type of program.
- The Unit needs to complete the following actions to become fully operational.
  - a) Review the operations of a similar Price Control Unit in Colombia. (In September 1984, the USAID reported to us that the personnel of the Honduran Unit had visited Colombia.)
  - b) Complete the review of past commodity transactions in order to assist in developing a price list.
  - c) Develop a system to maintain prices on a current basis. (In September 1984, the USAID advised us that a system has been developed.)
  - d) Establish a data bank of prices using the Central Bank's computer. (In September 1984 the USAID advised us that pricing data is recorded manually.)
  - e) Purchase a telex to obtain price quotations and other data from companies in the U.S. (In September 1984, the USAID advised us that the Unit is using the Central Bank's telex but will obtain its own telex when the Unit is permanently located.)
  - f) Develop policies and procedures for its operation.
- The Unit plans to use the following procedure for checking prices:

- a) The employees of the Department of Exterior Regulation who approve import and export licenses will first compare pro forma prices to a price list prepared by the Price Control Unit. If the prices proposed for the transaction seem too high or low the Price Control Unit plans to review the transaction. The Price Control Unit will also review 100 percent of the transactions for some commodities that do not lend themselves to verification against a price list, such as equipment and fertilizers.

Based on our review of the operations of the Price Control Unit, we believe the following changes are needed in order to accomplish its mission:

- The Unit has not prepared an implementation plan to identify and time-phase the actions required to start its price-checking operations. Such a plan should be developed as soon as possible.
- The professional staff of the unit needs to be increased. The current staff of three professionals will not be able to review a sufficient number of import and export transactions to provide adequate control over capital flight. The USAID believes the staff should be increased to 10 professionals.
- The location of the Unit in the organizational structure of the Central Bank does not provide effective internal controls over the approval of import and export transactions. Also, it does not provide sufficient authority to the Chief of the Unit to expeditiously process administrative actions. The Unit has been placed in the Department of Exterior Regulation. Since this Department is responsible for approving import and export transactions, the Unit cannot serve as an effective internal check over the approval of transactions. To avoid this internal control weakness and give the Unit more authority to expeditiously process administrative actions, we believe the Unit should be transferred to the office of the vice president of the Central Bank.
- No technical assistance has been planned to help the Unit develop its policies and procedures, establish a computer-based data bank of prices or train its staff in price-checking operations. Prior to our review the USAID had discussed the need for technical assistance with the Central Bank to ensure that the Unit was successfully organized and established. Technical assistance needs should be identified as soon as possible.

We discussed the above problems with USAID/Controller personnel and they agreed that action is needed in these areas. Prior to our departure from Honduras on August 8, 1984, the USAID presented us with a draft letter to the Central Bank that addressed these issues. This letter was subsequently sent to the Central Bank on August 10, 1984.

#### Attribution of Cash Transfers to Imports

The program agreements required the Central Bank to attribute eligible import transactions to cash transfers within 12 months from the date of each agreement.

The Central Bank has so far submitted documentation acceptable to the USAID for the first two cash transfers totaling \$38 million.

The attribution process has been very time-consuming and cumbersome for USAID personnel because a high percentage of the transactions submitted by the Central Bank were not eligible and the Central Bank did not maintain sufficient documentation in its files to expeditiously verify the eligibility of the transactions. To support the cash transfers totaling \$38 million, the Central Bank had to submit to the USAID 2,828 import transactions valued at \$68.3 million. About \$30.3 million of these transactions were rejected as ineligible by the USAID because the country of origin, dates of entry, and categories of merchandise were questionable.

The documents maintained in Central Bank files (import permits and applications for foreign exchange) were not adequate to verify the eligibility of the imports. As a result, USAID personnel had to visit commercial banks and the customs offices all over the country to locate and review commercial invoices, bills of lading, letters of credit, and customs entry policies to determine commodity eligibility.

To avoid these time-consuming reviews in the future, the USAID issued Implementation Letter No. 96 on August 3, 1984 to require the Central Bank to maintain adequately documented files and report eligible transactions on a quarterly basis using an improved reporting format.

On August 2, 1984, we visited the Central Bank's Department of Exchange and found that they were already starting to establish new systems for filing and reporting import transactions to USAID/Honduras.

USAID/Controller personnel advised us that once the new filing and reporting systems are established, they plan to verify only

a sample of the transactions for eligibility rather than reviewing all the transactions as they had in the past.

### Special Accounts Maintained for Local Currency Generations

The Ministry of Finance is responsible for managing four special accounts maintained by the Central Bank for local currency generated under the program. The Ministry authorizes The Central Bank to disburse all funds from the accounts except for disbursements to PVOs which are authorized by USAID implementation letters sent directly to the Central Bank.

We reviewed some transactions charged to these accounts and found that some disbursements were not charged to the correct account. For example, we found that disbursements equivalent to \$373,650 for six PVO projects were erroneously charged to account No. 2300826 by the Central Bank instead of Account No. 2300761. This happened because the USAID did not identify the account numbers to be charged in the implementation letters sent to the Central Bank authorizing the disbursements. Because of these errors, the accounts have to be reviewed monthly by USAID and Ministry personnel to identify the errors and make adjusting entries. The USAID advised us in September 1984 that the errors found during our review have been corrected by the Ministry of Finance. To avoid these time-consuming reviews in the future, we suggested that all funds be transferred to one account and that the other accounts be closed. USAID/Controller personnel agreed with this suggestion. On September 18, 1984, the Office of the Controller requested the Director General of Public Credit to establish one special bank account for ESF funds.

### GOH Reporting Requirements

The implementation letters (PIL) issued under the program required the GOH to submit various reports to the USAID:

- quarterly reports on the use of local currency funds allocated to the public sector (Implementation Letter (PIL) Nos. 2 and 20)
- quarterly reports on the use of local currency funds for private sector credit (PIL No. 2)
- quarterly reports on the attribution of imports to dollars provided under the program (PIL Nos. 5 and 96)
- copies of monthly bank statements of the Special Account (PIL No. 5)

- copies of weekly reports prepared by the GOH for the IMF (PIL No. 5)

USAID/Controller personnel advised us that they have not set up a system to verify the receipt of these reports but plan to do so and, at the same time, to review the need for all these reports.

#### USAID/Controller Verification of Local Currency Utilization

As of June 30, 1984, the GOH had deposited the equivalent of \$91 million in local currency in special accounts, of which \$45.6 million had been disbursed. The funds have been programmed for 109 development activities such as GOH counterpart funding for AID and other donor projects, credit for private sector borrowers and PVO projects.

Between October 1983 and June 1984, the USAID/Controller's Office had performed financial reviews of seven of the 22 PVO projects financed with local currency generations as well as three banks under the line-of-credit program to the private sector. The USAID has focused on PVO projects because the USAID has assumed all of the responsibility for planning and monitoring PVO projects. To increase USAID/Controller surveillance over non-PVO projects, local currency generations will be used by the USAID to hire four more financial analysts.

#### Evaluation of Program

Implementation Letter No. 2 provided that the Ministry of Finance, the Central Bank and the USAID were to conduct a joint evaluation of the program in August 1983. This evaluation was not held because of the unavailability of key personnel, and lack of sufficient data regarding local currency disbursements. Furthermore, given the USAID's active surveillance activities, this evaluation requirement should be reviewed for possible redundancy.

#### P.L. 480 Title I and III Program

##### Collection of Sales Proceeds

The Honduran Agricultural Marketing Institute (IHMA) is responsible for purchasing and selling wheat imported under the Title I and III programs. The responsibility for the collection of the sales proceeds and interest due was shifted from IHMA to the Ministry of Finance about one year ago. The Ministry of Finance is depositing checks received from the millers (generally through IHMA) in a special account but the Ministry has not set up any accounting controls to verify that the millers are paying the amounts due when required.

The USAID said they have held meetings with Ministry of Finance and IHMA officials to establish accounting controls over the amounts millers are required to pay and subsequently remit to the GOH. On October 1, 1984, USAID Controller and Ministry of Finance personnel traveled to San Pedro Sula and verified that two of the three millers had paid the Ministry of Finance the amounts due.

#### USAID/Controller Review of Local Currency Projects

USAID/Controller personnel have not done any financial reviews of the local currency projects financed under the Title I and III programs because of a lack of staff. These reviews will be made as soon as the planned staff increase of four financial analysts mentioned previously is realized.

#### GOH Reporting Requirements

The agreements and implementation letters issued under the program require the GOH to submit numerous reports to the USAID:

- quarterly shipping report
- quarterly marketing reports
- annual progress reports on the Food for Development program
- annual evaluation report
- annual report on self-help measures and use of local currency generations
- annual financial report of local currency collected and expended.

USAID/Controller personnel advised us that they have not set up a system to verify the receipt of these reports but plan to do so.

**APPENDIX**

**LIST OF REPORT RECIPIENTS**

	<b><u>Copies</u></b>
USAID/Honduras	5
AA/LAC	2
LAC/CAP	2
LAC/DR	1
LAC/DP	1
LAC/CONT	1
GC/LAC	1
FVA/PPE	1
FVA/PPP	3
LEG	1
AA/M	1
M/FM/ASD	2
AA/XA	1
DAA/XA/PA	1
PPC/CDIE	1
PPC/CDIE/DI	1