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AUDIT
OF USAID/HONDURAS' COMPLIANCE WITH AID'S REVISED PAYMENT VERIFICATION GUIDELINES

Audit Report No. 1-522-87-28
April 28, 1987

AGENCY FOR INTERNATIONAL DEVELOPMENT

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA · HONDURAS

April 28, 1987

MEMORANDUM

TO : USAID/Honduras Director, John Sanbrailo

FROM : RIG/A/T, Coinage N. Gothard, Jr. Coinage N. Gothard

SUBJECT: Audit of USAID/Honduras' Compliance with AID's Revised Payment Verification Guidelines, Report No. 1-522-87-28

This report presents the results of audit of your compliance with AID's Revised Payment Verification Guidelines. The Office of the Regional Inspector General for Audit/Tegucigalpa made a limited financial and compliance audit at USAID/Honduras. The specific audit objectives were to determine whether your office had submitted timely general assessments and updates required by the payment verification guidance, test the accuracy of these self-assessments and determine reasons for any inaccuracies, analyze areas where responsible offices were not in compliance and determine the effects, assess whether justifications for noncompliance were reasonable at the time they were made, and determine whether subsequent actions had been taken by your office to conform to AID payment verification policies.

USAID/Honduras had realized limited success in implementing AID's Revised Payment Verification Guidelines. Some of the Policy Statements such as Statement No. 15 on Commodity Import Programs (CIP) were not applicable to USAID/Honduras' situation. One of three general assessments was not furnished to AID/Washington in a reasonable or within the required time. The assessments were generally complete but were not supported by evidence of tests of random samples, and USAID/Honduras was not in compliance with the Policy Statements in seven instances. Justifications to deviations in financing methods were made and were reasonable. Subsequent USAID/Honduras actions to comply with the Policy Statements included the use of random sample techniques to support future assessments, reiteration of certain of the Policy Statements, and the Implementation of tightened review and verification controls.

At USAID/Honduras, there was inadequate support for the Controller's voucher approval and examination procedures because a randomly selected sample of vouchers to assure the adequacy of the Mission's voucher approval and examination process was not tested. Voucher approval and examination procedures for local Private Voluntary Organizations (PVOs) needed strengthening, and, based on USAID/Honduras accounting records, AID recipients received advances far in excess of immediate disbursing needs. USAID/Honduras had not received prompt reimbursement from commercial carriers for the unused portion of airline tickets, and fuels were purchased at commercial, tax-laden prices. Audit tests of 10 USAID/Honduras project papers totaling $45.1 million in obligations disclosed that the project papers did not contain specific provisions for audit coverage, and only one earmarked funding for independent audits. While project officers' checklists were generally appended to vouchers processed by the USAID/Honduras Controller, they were not adequate due to omissions or due to the absence of evidence supporting the claimed contracts.

We have recommended that USAID/Honduras make and test a randomly selected sample of vouchers, resolve or recover over $21,000 in questionable costs, and take action on about $3 million in advances that have been outstanding for more than 90 days. We have also recommended that USAID/Honduras strengthen follow-up procedures on unused airline tickets, discount benefits offered, and sales tax exemptions. Finally, we have recommended that certain of the Policy Statements be reiterated to assure the reservation of funds for audit and improved administration of project officer's checklists.

Generally, you have not concurred with the report findings. In all reasonable instances we have accomodated management concerns by modifying the report findings and recommendations. Moreover, USAID/Honduras should be complimented on completing several of the recommended actions prior to issuance of this report.

Please provide written notice within 30 days of any additional information related to actions planned or taken to implement the recommendations.

EXECUTIVE SUMMARY

Consistent with the Agency for International Development (AID) Administrator's emphasis on implementation of AID programs and for consistency with the Federal Managers Financial Integrity Act and Office of Management and Budget Circular A-123 on internal control, the AID Administrator approved 16 policy statements on financial and administrative management, intended to complement efforts in improving AID's system of internal control. The United States Agency for International Develcpment Mission in Honduras (USAID/Honduras) was one of the AID offices responsible for implementing the Revised Payment Verification Guidelines. As of December 31, 1986 USAID/Honduras' program portfolio consisted of about 75 projects totaling $613.1 million in obligations.

The Office of the Regional Inspector General for Audit/Tegucigalpa made a limited financial and compliance audit at USAID/Honduras. The specific audit objectives were to determine whether USAID/Honduras had submitted timely general assessments and updates required by the payment verification guidance, test the accuracy of these self-assessments and determine reasons for any inaccuracies, analyze areas where responsible offices were not in compliance with AID policies and determine the effect of the noncompliance, assess whether the justifications for noncompliance were reasonable at the time they were made, and determine whether subsequent actions had been taken by responsible offices to conform to AID payment verification policies.

The audit disclosed that one of three general assessments was not furnished to AID/Washington in a reasonable or within the required time. The assessments were generally complete but were not supported by evidence of tests of random samples, and USAID/Honduras was not in compliance with the Policy Statements in seven instances. Justifications to deviations in financing methods were made and were reasonable. Subsequent USAID/Honduras actions to comply with the Policy Statements included the use of random sample techniques to support future assessments, reiteration of certain of the Policy Statements, and the implementation of tightened review and verification controls.

USAID/Honduras' Controller's Office operated with a full complement of experienced supervisors, analysts and voucher examiners. However, it also acted as the primary accounting station for the AID Affairs Office (AID/Belize) located in Belize City, Belize. For two of the three reporting years USAID/Honduras carried the additional responsibility of making and reporting the assessments on AID/Belize's behalf.

USAID/Honduras can more effectively implement the Guidelines by correcting conditions identified by audit. There was inadequate support for the Controller's voucher examination and approval procedures, and such procedures for local private voluntary organizations needed to be strengthened. Recipients received advances made by USAID/Honduras far in excess of immediate disbursing need. Also, USAID/Honduras had not received reimbursement from commercial carriers for the unused portions of airline coupons in a timely manner. A 10 percent discount on purchases for merchandise from a local hardware store was not realized, and USAID/Honduras did not effectively use duty-exempt privileges in making fuel purchases on a project's behalf. Ten project papers tested did not contain specific language for audit coverage; only one earmarked funding for audit. Improvements were needed in the preparation of project officers' checklists, and USAID/Honduras did not follow contractual requirements in obtaining heavy equipment for a project.

To ensure accountability and other implementation planning objectives the AID Administrator issued Payment Verification Policy Statement No. 8, which required Mission controllers to provide annual assessments of the Missions' voucher approval and examination procedures. At USAID/Honduras, there was inadequate support for the Controller's voucher approval and examination procedures because a randomly selected sample of vouchers to assure the adequacy of the Mission's voucher approval and examination process was not tested. As a result, the adequacy of USAID/Honduras' voucher approval and examination processes to support the integrity of its $613 million portfolio was not verifiable. We have recommended that USAID/Honduras make random samples of vouchers and document the results.

The AID Administrator's Policy Statement No. 8 required Mission Controllers to provide annual assessments of their Mission voucher approval and examination procedures. At USAID/Honduras, voucher approval and examination procedures for local private voluntary organizations needed strengthening. The organizations were not required to submit supporting detail of expenditures with their liquidating vouchers, thus voucher examiners had no documentation to verify expenses. This decision was based on positive Controller assessments of the organizations' accounting and internal control systems based on criteria set forth in Office of Management and Budget Circular A-110 and AID Handbook 13. However, based on an examination of the procedures for two organizations, accounting procedures for project funding required closer supervision by USAID/Honduras' Controller. As a result, USAID/Honduras reimbursed almost $10,200 in advances, unallowable costs and non-supported expenditures to one organization and almost $11,600 to another. We have recommended that USAID/Honduras collect or account for $21,800 in advances, unallowable costs and unsupported cost claims made by certain recipients.

Based on USAID/Honduras' records, recipients either had not used or had not liquidated millions of dollars in advances. In total $4.4 million (51.8 percent) of USAID/Honduras' $8.5 million in advances were outstanding. We recommended that USAID/Honduras review and justify or recuperate about $4.4 million in outstanding advances.

USAID/Honduras had not received prompt reimbursement from commercial carriers for the unused portion of airline tickets. This slow redemption process for unused airline tickets was not in accordance with AID Handbook No. 19 which required USAIDs to make every effort to collect payments owed the U.S. Government in a timely manner. USAID/Honduras was slow to follow-up on collections because it assumed that the turnaround time for commercial carriers to process refund checks was three months.

As a result, 15 of 26 tested requests for refunds of unused tickets totaling $7,056 had not been refunded by the commercial carriers even though these requests were from two to eighteen months old. Of the $3,552 refunded by the carriers, only $955 was refunded in a timely manner. We recommended that USAID/Honduras improve controls over collections for unused airline coupons.

The other findings discuss the discounts on purchases and tax exemptions, provisions for audit coverage, and use of checklists. We recommended that the Mission take advantage of the savings available, provide for audit coverage, and properly use checklists.

The Mission requested the inclusion of the following in the Executive Summary:

"USAID believes that the report does not present a balanced view of how it has complied with AID's revised payment verification guidelines. USAID disagrees with some of the findings and recommendations, especially the conclusions leading to recommendation 3 and recommendations 2, 3, 5(a), 7, and 8. It believes that the Mission has effectively implemented the guidelines on cash management procedures by (i) requiring entities to use their own resources to finance initial operations where feasible, (ii) limiting advances to immediate disbursing needs for those entities that do not have sufficient operating funds, (iii) closely monitoring cash management practices of recipients to ensure that no excess cash balances are held and (iv) attempting to obtain regular reports from recipients on the use of AID advances. USAID also observed that the conclusions of the report contradicted recent project audits which concluded that it needed to ensure a more steady and dependable source of funding to ensure better implementation."

Office of the Inspector General

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PART I - INTRODUCTION

A. Background

Consistent with the Agency for International Development (AID) Administrator's emphasis on implementation of AID programs and for consistency with the Federal Managers Financial Integrity Act and Office of Management and Budget (OMB) Circular A-123 on internal control, the AID Administrator approved 16 policy statements on financial and administrative management, intended to compliment efforts in improving AID's system of internal control. On December 30, 1983 AID's Assistant to the Administrator for Management (AA/M) published these statements for implementation by responsible AID Offices effective January 1, 1984. Accordingly, applicable AID Handbook and policy guidelines were to be revised within calendar year 1984.

The United States Agency for International Development Mission in Honduras (USAID/Honduras) was one of the AID offices responsible for implementing the Revised Payment Verification Guidelines. USAID/Honduras' existence could be traced back to an Economic, Technical and Related Assistance agreement between the Government of Honduras and the United States dated April 12, 1961. As of December 31, 1986 total staffing at USAID/Honduras was about 176 individuals, there were 43 U.S. direct-hire positions of which 37 were filled, and USAID/Honduras' program portfolio consisted of about 75 projects totaling $613.1 million in obligations.

B. Audit Objectives and Scope

The Office of the Regional Inspector General for Audit/Tegucigalpa made a limited financial and compliance audit at USAID/Honduras. This audit was conducted in conjunction with an Inspector General worldwide audit of compliance with the AID Administrator's Revised Payment Verification Guidelines. The purpose of the audit was to determine whether or not USAID/Honduras was in compliance with AID's Revised Payment Verification Guidelines. The specific audit objectives were to determine whether USAID/Honduras had submitted timely general assessments and updates required by the payment verification guidance, test the accuracy of these self-assessments and determine reasons for any inaccuracies, analyze areas where responsible offices were not in compliance with AID policies and determine the effect of the noncompliance, assess whether the justifications for noncompliance were reasonable at the time they were made, and determine whether subsequent actions had been taken by responsible offices to conform to AID payment verification policies.

Audit work was done at USAID/Honduras in Tegucigalpa. Audit verification included reviews of records and files, interviews with responsible officials, and tests of $5.4 million in vouchers received and cost claims made by certain AID-funded recipients. Audit field verifications were made during the period October 10, 1986 through November 10, 1986 and audit coverage extended from the date of issuance of the Payment Verification Guidelines (December 30, 1983) to December 1986. Tests of systems of internal control were not made; internal control practices were tested as they related to the guidelines. (See Part II, B.) An exit conference was held on November 10, 1986 and USAID/Honduras provided written comments to 11 of our Records of Audit Findings (RAFs). On April 15, 1987 USAID/Honduras formally responded to our draft audit report. Their comments were considered in the preparation of this report and are included as Appendix I. Other than limited tests of internal controls, the audit was made in accordance with generally accepted government auditing standards.

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PART II - RESULTS OF AUDIT

USAID/Honduras had realized limited success in implementing AID's Revised Payment Verification Guidelines. Some of the Policy Statements such as Statement No. 15 on Commodity Import Programs (CIP) were not applicable to USAID/Honduras' situation. One of three general assessments was not furnished to AID/Washington in a reasonable or within the required time. The assessments were generally complete but were not supported by evidence of tests of random samples, and USAID/Honduras was not in compliance with the Policy Statements in six instances. Justifications to deviations in financing methods were made and were reasonable. Subsequent USAID/Honduras actions to comply with the Policy Statements included the use of random sample techniques to support future assessments, reiteration of certain of the Policy Statements, and the implementation of tightened review and verification controls.

USAID/Honduras' Controller's Office operated with a full complement of experienced supervisors, analysts and voucher examiners. However, it also acted as the primary accounting station for the AID Affairs Office (AID/Belize) located in Belize City, Belize. For two of the three reporting years USAID/Honduras carried the additional responsibility of making and reporting the assessments on AID/Belize's behalf.

USAID/Honduras can more effectively implement the Guidelines by correcting conditions identified by audit. There was inadequate support for the Controller's voucher examination and approval procedures, and such procedures for local PVOs needed to be strengthened. Recipients received advances made by USAID/Honduras, far in excess of immediate disbursing need. Also, USAID/Honduras had not received reimbursement from commercial carriers for the unused portions of airline coupons in a timely manner. A 10 percent discount on purchases for merchandise from a local hardware store was not realized, and USAID/Honduras did not effectively use duty-exempt privileges in making fuel purchases on a project's behalf. Ten project papers tested did not contain specific language for audit coverage; only one earmarked funding for audit. Improvements were needed in the preparation of project officers' checklists.

We have recommended that USAID/Honduras make random samples of vouchers and document the results, and collect or account for $21,800 in advances, unallowable costs and unsupported cost claims made by certain recipients. We have also recommended that USAID/Honduras review, justify or recuperate about $4.4 million in outstanding advances, and improve controls over collections for unused airline coupons. Moreover, it is recommended that USAID/Honduras take advantage of local discounts and request a refund for unnecessary taxes paid. Finally, we have recommended that USAID/Honduras comply with Policy Statements No. 6 and 7.

A. Findings and Recommendations

1. Adequacy of the Voucher Examination and Approval Procedures Was Not Supported

To ensure accountability and other implementation planning objectives the AID Administrator issued Payment Verification Policy Statement No. 8, which required Mission controllers to provide annual assessments of the Missions' voucher approval and examination procedures. At USAID/Honduras, there was inadequate support for the Controller's voucher approval and examination procedures because a randomly selected sample of vouchers to assure the adequacy of the Mission's voucher approval and examination process was not tested. As a result, USAID/Honduras was not in compliance. The recommendation refers to USAID/Honduras' next reporting cycle.

Recommendation No. 1

We recommend that USAID/Honduras:

a) ensure the adequacy of the voucher approval and examination process by performing a randomly selected sample of vouchers; and

b) document the work performed to ensure the adequacy of the voucher approval and examination process.

Discussion

The implementing guidelines under Payment Verification Policy Statement No. 8 required that, "The annual review called for under this policy directive is designed to formalize a process which should already be in place. The review should involve a randomly selected sample of vouchers large enough to provide reasonable assurance that the voucher approval and examination procedures in place are adequately represented by the assessment."

The Mission's general assessments for 1983, 1984 and 1985 may not have represented a true picture of its voucher approval and examination process because the adequacy of the system already in place was not assured. The Mission did not perform a random sample of vouchers to provide it reasonable assurance that the voucher approval and examination procedures already in place were adequately represented by the assessments. Instead, the Mission relied on personal knowledge of supervisory personnel to assure that the system in place was adequate. Because all vouchers were reviewed upon receipt, and voucher examiners were knowledgeable about their functions, supervisory personnel assumed that the system in place was adequate to provide reasonable assurance that it was working properly.

Management Comments

USAID/Honduras tested 100 vouchers at random to support its 1986 assessment and determined that the vouchers were properly supported with required documentation.

Office of Inspector General Comments

In light of the Mission's subsequent actions to test the adequacy of the voucher approval and examination processes, Recommendation No. 1 is closed the date of issuance of this report.

2. Voucher Examination and Approval Procedures for PVOs Needed Strengthening

The AID Administrator's Policy Statement No. 8 required Mission Controllers to provide annual assessments of their Mission voucher approval and examination procedures. At USAID/Honduras, voucher approval and examination procedures for local Private Voluntary Organizations (PVOs) needed strengthening. The PVOs were not required to submit supporting detail of expenditures with their liquidating vouchers, thus voucher examiners had no documentation to verify expenses. This decision was based on positive Controller assessments of PVOs' accounting and internal control systems based on criteria set forth in OMB Circular A-110 and AID Handbook 13. However, based on an examination of the procedures for two PVOs, accounting procedures for project funding required closer supervision by USAID/Honduras' Controller. As a result, USAID/Honduras reimbursed almost $10,200 in advances, unallowable costs and non-supported expenditures to one PVO and almost $11,600 to another.

Recommendation No. 2

We recommend that USAID/Honduras:

a) recover $1,260 in unallowable sales taxes reimbursed to Centro de Estudios y Promocion del Desarrollo;

b) require Centro de Estudios y Promocion del Desarrollo to provide documentation for $1,527 in questioned costs under voucher 522-87-0447; and collect any unsupported amounts;

c) reconcile the advance and expenditure records to show the correct status of $7,389 subadvanced by Centro de Estudios y Promocion del Desarrollo to a contractor;

d) collect $66 in unallowable costs from Advisory Council on Human Resources Development and recover $125 advanced to Dialog Information Services under voucher 522-86-3647;

e) require the Advisory Council on Human Resources Development to provide documentation for $11,409 in unsupported costs under vouchers 522-86-4086 and 522-86-3647; and collect any unsupported amounts; and

f) determine whether international travel performed by members of the Advisory Council on Human Resources Development in Honduras was justified, and if so;

   i) ensure that the grant officer's justification is included in documentation of the payment voucher; and

   ii) ensure that a cumulative detailed report of disbursements by budget line item is submitted quarterly to AID.

Discussion

Review of liquidating Voucher No. 522-87-0447 dated October 14, 1986 for $90,638.70 submitted under Project No. 522-0303 by Centro de Estudios y Promocion del Desarrollo (CEPROD), a local PVO resulted in the following:

Sales Taxes - The PVO was reimbursed for sales taxes in the amount of $1,126.50. According to Appendix C of the Grant Agreement between USAID/Honduras and the PVO, taxes were unallowable costs. USAID/Honduras believed that the determination of allowability should have been made in accordance with the cost principles of OMB Circular A-122. The Circular provides that taxes which an organization pays are allowable if the organization is not exempt from the taxes. Since CEPROD did not have a tax exemption and it was not cost effective for USAID/Honduras to make tax-free purchases on CEPROD's behalf, USAID/Honduras concluded that sales taxes were eligible costs under the Grant Agreement. But the binding document, the Grant Agreement, dictated that sales taxes were not eligible for reimbursement and OMB Circular A-122 provisions were not incorporated therein. Thus, there is no alternative but to question the costs. Subsequent to audit, USAID/Honduras received a copy of STATE 397888 in which AID's Directorate for Program and Management Services (M/SER) advised that taxes imposed on AID grantees in Guatemala were considered allowable if the organization had been unable to receive tax exemptions from the Government of Guatemala. We consider this criterion equally applicable in Honduras.

Foods and Beverages - The PVO billed USAID/Honduras $133.65 for the consumption of food and beverages. These expenditures were entertainment expenses thus unallowable under Appendix C of the Grant Agreement.

Incomplete or Non-Supporting Data - The PVO's supporting documentation was not detailed enough to determine the propriety of expenditures totaling $1,193.67 for the period July-September 1986. In addition, the PVO could not support expenditures totaling $332.88 for the same period.

Advances Claimed as Expenses - For the period July-September 1986, the PVO claimed costs of $7,389.30 for funds subadvanced to a contractor for the construction of a Health Center. These subadvances exceeded the actual monthly costs of the contractor. The PVO was subtracting the excess amount from the subsequent month's billings, evidencing control over the subadvance. But, the practice of reporting advances as expenses to AID by the PVO was not proper. The reporting of actual expenses was required. USAID/Honduras responded that they, did "...not view the PVO's error of including subadvances on his quarterly liquidation voucher as requiring collection of the funds and submission of detailed documentation for the balance of the grant." We agree with USAID/Honduras' view from a standpoint of "accountability" for the subadvance. However, the crediting or reimbursing of advances as if they were expenditures affected the fiscal integrity of accounting records and subsequent reporting. That is, actual expenditures were overstated by $7,000. Therefore, we believe the recommendation, as modified, is warranted.

Because the PVO was not required to provide supporting documentation with the liquidating vouchers, these practices could not be detected through voucher reviews. Almost $10,200 in project funds were reimbursed the PVO even though they were not justified or supported at the time.

Our examination of liquidating vouchers 522-86-3647 dated August 8, 1986 and 522-86-4086 dated August 28, 1986 submitted under Project No. 522-0257 by the Advisory Council on Human Resources Development in Honduras (CADERH) resulted in the following:

International Travel - Annex C, Section 14(a) of the Grant Agreement required the grant officer's written approval for international travel to be reimbursed under the Grant, and the Grantee was to provide to the cognizant Mission or U.S. Embassy advance notification of the arrival date and flight identification of Grant-financed travelers. Also, Section 14(c) of the agreement required all international air travel funded under the Grant to be made on United States flag air carriers to the extent service by such carriers was available. Voucher No. 522-86-4086 included travel expenses of $2,823.70 for a trip to Bogota, Colombia and Rio de Janeiro, Brazil. Voucher No. 522-86-3647 included travel expenses of $8,758.21 for trips to the states of Texas, Oklahoma, Pennsylvania and Minnesota. The PVO could not produce AID grant officers' travel approvals to any of these locations nor was documentation available to justify the use of non-U.S. flag carriers. As a result, USAID/Honduras reimbursed almost $11,600 to the PVO for questionable transactions or for international travel that had not been approved by the grant officer in accordance with the Grant Agreement.

USAID/Honduras pointed out that U.S. flag carriers did not fly from Honduras to New Orleans, Houston or South America. They said that travel was made with the full knowledge of the project officer who had been delegated approval responsibilities from the grant officer based on Annex C, Section 14(a) of the Grant. USAID/Honduras proposed to review the justification for use of non-American carriers and to furnish the PVO a letter formally approving the trips. We believe that U.S. carriers, especially to eastern destinations such as Pennsylvania, could have been used.

Purchase of Books - The PVO was reimbursed $200 for the purchase of a catalog. The PVO made an advance payment of $200 to a vendor for the purchase of books for which only one catalog valued at $75 was received. The remaining $125 was being held by the vendor as a deposit for future purchases. Because there had not been an expense for the $125 held by the vendor, the PVO should not have been reimbursed the entire $200 advanced the vendor. In addition, a PVO member purchased a book for $40, however, there was no support for this purchase.

Personal Expenses of Traveler - A PVO member incurred $44 in personal medical expenses during a trip to the USA. The traveler claimed the medical expenses as reimbursable items which were then included on the payment voucher to USAID/Honduras. These costs were ineligible for payment by AID.

Excess Baggage Payment - A PVO member was charged $40 for excess baggage but was reimbursed $60 by the PVO which in turn billed and received $60 from USAID/Honduras. The difference of $20 was unallowable.

Cumulative Detailed Report - According to attachment E of the Grant, the Grantee was to provide to AID on a quarterly basis a cumulative detailed report of disbursements by budget line item. Although the PVO was providing reports, they were not cumulative as required by attachment E of the Grant.

The above examples illustrate the limits to which the Agency's voucher examination and approval processes extend to PVOs and certain grant recipients. OMB Circular A-110 and AID Handbook 13 criteria contain provisions that require PVOs to provide only quarterly certified disbursing reports without supporting documentation. As of December 31, 1986 USAID/Honduras' portfolio consisted of about 75 projects totaling about $613.1 million in obligations. At least 15 executing instruments (about $10.1 million), representing only two percent of the Mission's portfolio, were Operational Program Grants (OPGs) to recipients or to PVOs.

Management Comments

USAID/Honduras did not concur with the sales tax issue and requested reconsideration in light of their recent receipt of M/SER's instruction set forth in STATE 397888. USAID/Honduras also caused CEPROD to provide supporting documentation for the $1,527 in questioned costs, including recoveries of $17.50 and $133.65. USAID/Honduras determined that there was an unliquidated balance of $2,983 for the $7,389 that had been subadvanced by CEPROD to a contractor, and USAID/Honduras caused CADERH to deposit in the project dollar account $229 covering the unauthorized advance, unsupported book purchase and expenses incurred of a personal nature. The Mission provided project officer's concurrence for international travel, but the grantee had yet to explain the use of foreign carriers for travel between Honduras and Miami. Finally, the Mission provided an adequate budget and expenditure report by CADERH.

Office of Inspector General Comments

Based on USAID/Honduras actions we have closed Parts a), b), d), and f) of Recommendation No. 2 effective the date of issuance of this report. Parts c) and e) remain open pending completion of management actions.

3. Control Over Advances Needed Improvement

Based on USAID/Honduras' accounting records, recipients either had not used or had not liquidated millions of dollars in advances. However, USAID/Honduras believed that it was more appropriate to state that large, book balances of unliquidated advances remained on the USAID's accounting records even though the cash had been completely used months before. The Agency's cash management procedures, stemming from U.S. Treasury regulations, advise that "immediate disbursing needs" may be assumed to be cash requirements for as much as 30 days from the date a recipient receives an advance until it is expended. In unusual instances the advance may extend for as long as 90 days. However, USAID/Honduras used a format that aged the so-called current advances from 0 to 120 days rather than from 0 to 90 days. Included in this category was an additional $1.4 million in advances that had been outstanding for more than 90 days. In addition, as of December 11, 1986, $1.1 million (13.2 percent) of USAID/Honduras' $8.5 million in advances had been outstanding about a year or more; $998 thousand (11.8 percent) had been outstanding for 181 days up to one year; and $928 thousand (11 percent) had been outstanding for 121 days up to 180 days. To sum up, $4.4 million (51.8 percent) of USAID/Honduras' $8.5 million in advances were outstanding.

Recommendation No. 3

We recommend that USAID/Honduras review and justify, liquidate or recuperate (including interest income) about $4.4 million in advances that have been outstanding for more than 90 days.

Discussion

As of December 11, 1986, USAID/Honduras' record of outstanding advances was:

No. of Days			
0 to 120	121 to 180	181 to 360	361 or More
$5,421,454*	$928,259	$997,837	$1,116,811

Nine entities exceeded advance liquidation limits.

GOH Ministry of Finance - retained 21 outstanding advances totaling $1.7 million dating back to September 1982.

* Included $1,391,568 in advances that were outstanding for more than 90 days.

Peace Corps - had six outstanding advances totaling $45,000 dating back to March 1984.

Winrock International - retained nine outstanding advances totaling $108,300 dating back to August 1984.

Partners of the Americas - had 10 outstanding advances totaling $169,500 dating back to March 1985.

Instituto Nacional Agrario (INA) had 12 outstanding advances for $737,600 dating back to May 1985.

Ministry of Health - retained 12 oustanding advances for $1.4 million dating back to August 1985.

Fundacion para la Investigacion y el Desarrollo Empresarial (FIDE) - retained four outstanding advances for $173,500 dating back to September 1985.

Volunteers in Technical Assistance (VITA) - had five outstanding advances for $227,000 dating back to November 1985.

Federacion de Organizaciones Privadas de Desarrollo de Honduras (FOPRIDEH) - had two outstanding advances for $87,000 dating back to December 1985.

USAID/Honduras had initiated actions on the outstanding advances by issuing notices to individual employees and contractors, and to responsible project officers. The first of these notices was issued on November 18, 1986. As of December 16, 1986 USAID/Honduras had collected $21,688 in funds advanced to individuals, and another $29,583 in advances outstanding more than a year had been collected from FIDE. USAID/Honduras needs to strongly pursue and obtain refunds or an accounting for outstanding advances.

Management Comments

USAID/Honduras provided these comments to audit report finding No. 3:

"Your statement in the first paragraph on page 5 of the results of audit and the third paragraph on page ii of the summary that 'Recipients received advances made by USAID/Honduras far in excess of immediate disbursing need' is not supportable. Neither is the second paragraph on [draft] page iv discussing the alleged failure of the USAID to follow established procedures a fair presentation of the facts. ...The write up in the summary indicates that large amounts of cash advances remain outstanding. We believe that it is more appropriate to state that large, book balances of unliquidated advances remain on the USAID's accounting records even though the cash had been completely used months before. Our estimate is that recipients of all projects have cash on hand of just over one million dollars which given the size of the program is, in our opinion, reasonable. Moreover, we would like to point out that the cash on hand is, for all practical purposes, money that has been received recently from the Mission." They also noted that follow-up on advances had existed since 1983.

Office of Inspector General Comments

We believe the wording contained in this finding is supportable based on the Mission's own records. By its own account, the Mission does not even know the exact amount of cash on hand by project recipients and has estimated that such amount is over a million dollars. Moreover, the Mission stated that there was over $5 million in documentation either on-hand or at the implementing agencies. If the Mission believes that it is more appropriate to state that large, book balances of unliquidated advances remain on the USAID's accounting records even though the cash had been completely used months before, then there is another problem, that of untimely processing of liquidating vouchers. In either case the fact remains that large amounts of cash advances remain outstanding according to USAID's own records and despite the fact that USAID/Honduras has extended the U.S. Treasury's limit on advances of 30 days' needs to 90 days.

We believe that the steps taken by the Mission are a positive beginning to resolving and clearing this recommendation. However, the recommendation remains open until USAID/Honduras provides evidence that adequate progress has been made to liquidate the $4.4 million in advances that have been outstanding for more than 90 days.

4. Collection Procedures for Unused Airline Tickets Needed Improvement

USAID/Honduras had not received prompt reimbursement from commercial carriers for the unused portion of airline tickets. In at least 6 instances, commercial carriers had taken no action on requests for refunds ranging between 4 and 18 months. In eight other requests for refunds, the commercial carriers were between two and three months late in refunding the costs of unused tickets. This slow redemption process for unused airline tickets was not in accordance with AID Handbook No. 19 which required USAIDs to make every effort to collect payments owed the U.S. Government in a timely manner. USAID/Honduras was slow to follow-up on collections because it assumed that the turnaround time for commercial carriers to process refund checks was three months. As a result, 15 of 26 tested requests for refunds of unused tickets totaling $7,056 had not been refunded by the commercial carriers even though these requests were from 2 to 18 months old. Of the $3,552 refunded by the carriers, only $955 was refunded in a timely manner.

Recommendation No. 4

We recommend that USAID/Honduras:

a) review the portfolio of unused airline tickets, and initiate immediate follow-up requests for refunds on all previous requests that are over 30 days old; and,

b) establish procedures to monitor, control and document redemptions in process by carriers.

Discussion

Examination of 26 known unused airline tickets purchased by USAID/Honduras disclosed that 11 of those tickets had been refunded by the commercial carriers, but only 3 refunds had been made within 30 days of the refund request. Of the remaining eight refunds, two were made within two months, four within three months, one within four months, and one could not be determined. A total of 15 requests for redemption for the carriers were in process, 1 of these requests had been in process less than 30 days, and all but 2 of the remaining 14 requests were over 2 months old, including one request that was approaching 18 months in process.

According to AID Handbook No. 19, Missions were to bill commercial carriers for unused portions of tickets on Standard Form 1170, maintain records for control and follow-up of redemptions and make every effort to collect payments within 30 days. The Mission was following up on requests for redemption, although no record was kept of telephone calls. However, the follow-up requests were delayed for three months or longer because the examiner who processed the requests assumed that the commercial carriers took that long to refund unused tickets. According to interviews of personnel processing redemption requests for unused tickets at the three airlines involved, TAN/SAHSA, Challenge, and Eastern, the redemption process was up to four weeks. Thus, USAID/Honduras collection procedures for unused airline tickets were not assertive enough to obtain prompt refund checks from the commercial carriers. As a result, a total of $7,056 had not yet been collected from the commercial carriers, and of $3,552 collected only $955 was received expeditiously.

USAID/Honduras concurred with the finding and had taken action to implement the recommendation by establishing procedures and developing a new form to control and to follow-up redemptions in process by carriers. Follow-up requests for refunds that were outstanding for over 30 days had been made.

The recommendation is closed the date of audit report issuance.

5. Project Savings Could Have Been Obtained

USAID/Honduras purchased merchandise valued at almost $37,000 during 1985 for the Mosquitia Relief and Development Project No. 522-0278. It also purchased 27,130 gallons of diesel fuel and 6,760 gallons of gasoline from Dippsa (a local petroleum firm) for the project. Fuels were purchased at commercial, tax-laden prices because purchasing agents did not effectively use USAID/Honduras' duty-exempt criterion. Project assistance was to be free from any taxation or fees imposed under laws in effect in the territory of the Borrower/Grantee. As a result, $5,700 in savings for Project No. 522-0278 were not realized. In addition, the Mission did not take advantage of a 10 percent discount on purchases for merchandise from a local hardware store (Ferreteria Rene J. Handal) which was available to buyers who paid within 30 days. Purchasing agents either did not pursue, or did not know that this benefit was available.

Recommendation No. 5

We recommend that USAID/Honduras request a refund from Dippsa, a local fuel vendor, in taxes paid for fuel purchases on behalf of Project No. 522-0278.

Discussion

USAID/Honduras paid more than necessary for fuel and merchandise purchased for the Mosquitia Relief and Development Project.

Fuel Taxes - Since 1985, USAID/Honduras has purchased 27,130 gallons of diesel fuel and 6,760 gallons of gasoline for Project No. 522-0278 from Dippsa, a local fuel merchant. Because these products were imported into the host country, a duty tax of $.025 per gallon of diesel fuel and $.19 per gallon of gasoline was imposed by the host country.

According to project agreements signed by AID, project assistance was to be free from "any taxation or fees imposed under laws in effect in the territory of the Borrower/Grantee." USAID/Honduras' contracting office advised us that this merchant was chosen to provide gasoline and diesel fuels to Project No. 522-0278 because the fuel could be delivered to the project site. The duty-free provisions in the project agreement were overlooked resulting in the loss of almost $2,000 in project funds.

Discounted Prices - During 1985, USAID/Honduras purchased merchandise valued at almost $37,000 from a local hardware store for Project No. 522-0278. A review of the invoices submitted with payment vouchers revealed that the available discount was not deducted from the purchase price. The store owner said that the current discount policy of 10 percent of the total sales price, if paid within 30 days of purchase, had been in effect prior to and during 1985. However, he said that the discount was given only upon request. Although the review consisted of vouchers submitted for Project No. 522-0278, the store owner was certain that AID had purchased over $50,000 in 1985 without asking for discounts.

But, savings of almost $3,700 were not realized because Mission personnel making these purchases did not request discounts in prices at the time of the purchases. According to the store owner, the discount could not be applied retroactively because sales for taxation by the host government had already been reported. Hence, the savings are lost.

Management Comments

USAID/Honduras pointed out that the requirement to specifically solicit discounts was not a procurement policy, and generally disagreed with the finding and recommendation, as presented. While discounts may not be a procurement policy, it is AID's policy to use public resources effectively and economically. USAID/Honduras also responded that it had approached Dippsa and was advised that a credit for duties paid this year would be made. This recovery is to be in the amount of $1,985 in local currency equivalents.

Office of Inspector General Comments

We have modified Recommendation No. 5 so that it can be effectively acted upon by USAID/Honduras. The recommendation will remain open pending evidence that a refund or credit has been obtained.

6. Project Paper Provisions For Audit Were Needed

Audit tests of 10 USAID/Honduras project papers totaling $45.1 million in obligations disclosed that the project papers did not contain specific provisions for audit coverage, and only one earmarked funding for independent audits. USAID/Honduras thought that separate provisions in project papers for audit coverage and funding were not needed because these components were considered to be included in funds budgeted to make evaluations. Policy Statement No. 6 called for evaluations of the need for audit coverage, and for reservations of funds budgeted for independent audits to be included in project papers. USAID/Honduras had not fully implemented the policies set forth in this Statement.

Recommendation No. 6

We recommend that USAID/Honduras establish procedures to include in project papers language specifically designed to fund audit coverage and earmark funds that are budgeted for independent audits.

Discussion

Audit tests of 10 project papers signed between April 1984 and September 1985 revealed: one project paper contained language establishing the evaluation of the project and audit with Program Development and Support (PD&S) funds, however, a specific amount for audit was not earmarked; another project paper budgeted $6,000 for an internal audit; and three project papers contained no specific language for audit coverage and the financial plans had no provisions for audit funding or for evaluations; a project agreement and three project papers mentioned funds for evaluations but did not discuss funds budgeted for audit; and a project agreement contained a provision for audit coverage but no funds were budgeted.

According to USAID/Honduras' Financial Review Section Supervisor, the funds budgeted for evaluations included funds for audits. However, because the language included in the project papers was vague, he agreed that specific amounts for audit funding should be included in project papers. The Mission did not fully implement the intent of Policy Statement No. 6 which states, "Project Papers are to include an evaluation of the need for audit coverage in light of potential risks and are to describe planned contract and project audit coverage by the host government, AID, and/or independent public accountants. Project funds should be budgeted for independent audits unless adequate audit coverage by the host country is reasonably assured or audits by third parties are not warranted..."

USAID/Honduras reviewed some of the 10 project papers discussed and responded that 2 of the 10 projects were Operational Program Grants (OPGs), and it was not clear if Payment Verification Policy Statement No. 6 was applicable. By this, USAID/Honduras recognized that OPG-recipients and Private Voluntary Organizations (PVOs) use criteria established by the Office of Management and Budget's (OMB's) Circular A-110 and AID's Handbook 13. The criteria therein are more lenient. We agree with

USAID/Honduras that applicability of Statement No. 7, as well as others, to OPG-recipients and PVOs is not clear.

Management Comments

USAID/Honduras also responded that it had strengthened its procedures to assure that all project papers include an evaluation of the need for audit coverage. They added that USAID/Honduras' two most recent project papers contained independent sections discussing audit needs and clear provisions for funding of audits in the projects' budgets.

Office of Inspector General Comments

Based on information provided by the USAID, recommendation No. 6 is closed the date of issuance of this report.

7. Project Officers' Checklists Were Not Adequately Supported

The AID Administrator's Policy Statement No. 7 required project officers to provide to Controllers a statement advising of the basis upon which administrative approval of vouchers was given. AID Handbook 3, Chapter 11, contains responsibilities for monitoring a project and USAID/Honduras Mission Order No. 19-80 required project officers to maintain records on site-visits. While checklists were generally appended to vouchers processed by the USAID/Honduras Controller, they were not adequate because: some were not filled in properly and thus did not provide the basis for administrative approval; in cases where the basis for approval was given, there was no support, i.e., trip reports, and/or record of meetings to substantiate the basis of approval; some were not signed by the project officers; and, still others were not attached to the vouchers evidencing a misunderstanding of requirements in preparing the checklists. Consequently, USAID/Honduras' compliance with Policy Statement No. 7 needed to be better documented.

Recommendation No. 7

We recommend that USAID/Honduras reiterate to project officers the provisions and intent of the AID Administrator's Payment Implementation Guideline No. 7.

Discussion

Effective January 1, 1984 the project officer was to use a clarifying addendum entitled Project Officers' Checklist of Administrative Approval of Vouchers that contained five parts to denote the basis for administrative approval.

The following examples of non-compliance with Payment Verification Policy Statement No. 7 were identified during a review of 52 project vouchers submitted for nine projects:

Project No. 522-0256 - four project officers' checklists were certified by two separate project officers but the bases upon which administrative approvals were given did not substantiate the approvals. For example, a statement provided by the project officers indicated that, "Payment is to cover liquidation of advances to GEMAH." The other three checklists contained statements by the project officers which the payee had included on the first page of the Standard Form 1034 under Articles or Services. Project officer justifications should have been independent of the recipient.

Project No. 522-0166 - the project officer's checklist noting administrative approval was not attached to a voucher for payment in the amount of $63,075. The checklist was not located in the project file.

Project No. 522-0257 - three vouchers for payment did not have project officer's administrative approval checklists. The checklists were not located in the project file. In addition, one of these vouchers contained a contractor's fiscal report attachments prepared from the books and records of the contractor in accordance with the terms of the contract. But the contractor's voucher was processed and paid even though the statement provided by the contractor was not certified. Six other vouchers contained the project officer's administrative checklist for approval but the statements made by the project officers were identical to that included by the payee under Articles or Services on Standard Form 1034. Project officer justifications for approval should have been independent of the recipient.

Project No. 522-0278 - the project officer's checklist was not attached to one voucher, the checklist was not located in the project file. Two other project officers' checklists were not completed properly. The bases for administrative approval were: a) recommendation of Project Manager; and, b) recommendation of project health coordinator. Still, on another voucher, the project officer signed the checklist but did not fill in any of the information requested on the checklist to form a basis for administrative approval.

According to AID Handbook 3, Chapter 11, "The primary responsibility for monitoring a project lies with the Project Officer to whom that project has been assigned." Furthermore, Handbook 3, Chapter 11, states that, "The purpose and coverage of site inspection is best illustrated by the report which should be prepared and filed by AID staff conducting the site visit." In addition, Mission Order No. 570.25 of July 7, 1986, states that, "within five days after each visit, a brief report of one to two pages will be prepared" and "it is the responsibility of the Approving Officer of the Travel Voucher to assure that the Site Visit Report is prepared."

USAID/Honduras did not agree with the audit finding and requested that the recommendation be withdrawn. There was a misunderstanding as to what documentation was required to support the project officers' checklists. It was agreed at the exit conference that calendar annotations supporting local contacts with recipients was a sufficient device. Actually, this was only one of several alternatives that could have been used in support of entries made to the checklists. AID Handbook 3 and USAID/Honduras' Mission Order provide sufficient criteria on documenting field trips.

Management Comments

USAID/Honduras said that voucher examiners had been instructed not to process vouchers that did not have checklists, and to return to project officers vouchers with checklists that were not properly completed or that contained questionable comments. Page 7 of Appendix 1 furnishes USAID/Honduras' rationale for not using other alternatives.

Office of Inspector General Comments

Recommendation No. 7, as modified, is closed the date of issuance of this report.

B. Compliance and Internal Control

Compliance

There were six compliance exceptions:

-- There was inadequate support for the Controller's voucher approval and examination procedures (Finding 1).

-- Recipients received advances far in excess of immediate disbursing needs (Finding 3).

-- USAID/Honduras had not received reimbursement from commercial carriers for the unused portion of airline tickets in a timely manner (Finding 4).

-- Available discounts on purchases of merchandise were not received, and fuels were purchased at commercial, tax-laden prices (Finding 5).

-- Ten project papers did not contain specific provisions for audit coverage, and only one earmarked funding for independent audits (Finding 6).

-- USAID/Honduras' compliance with Policy Statement No. 7 needed to be better documented (Finding 7).

Other than these conditions, nothing came to our attention as a result of specified procedures that caused us to believe that untested items were not in compliance with applicable laws and regulations.

Internal Control

The audit disclosed two internal control exceptions:

-- USAID/Honduras reimbursed almost $10,200 in advances, unallowable costs and non-supported expenditures to one PVO and almost $11,600 to another (Finding 2).

-- $3 million in overdue outstanding advances had not been collected (Finding 3).

Other than these internal control exceptions, nothing came to our attention to indicate that the integrity of internal control systems and practices had been compromised.

C. Other Pertinent Matters

Procurement requirements for a wheel loader imported specifically for Project No. 522-0278 were confusing, and it appeared that, USAID/Honduras did not follow special contract requirements in obtaining heavy equipment for the project. Part H-1 of Contract No. 522-0278-C-00-5547-00 dated September 24, 1985, stated that "The origin of the equipment and major components shall be from the United States of America (AID Geographic Code 000) and source can be either the U.S., Honduras or any other country included in AID Geographic Code 941." This procurement action occurred because the criteria established for source and origin of goods and services in the project grant agreement required the goods and services under the project to have their source and origin in Geographic Code 941 countries, while the contractual agreement required the origin of equipment and major components to be from AID Geographic Code 000. USAID/Honduras followed the criteria contained in the project grant agreement and a waiver was not sought to obtain the equipment having an origin in AID Geographic Code 941. As a result, a new wheel loader costing $57,810 was obtained from a manufacturer in Brazil rather than from a U.S. manufacturer on the basis of the general project agreement rather than the executing instrument. But the contract, too, contained conflicting terms. In addition to the origin requirement, page 2 of the contract listed the origin for the wheel loader to be from Brazil, not from the United States. Since the contract was executed in good faith, it would have been less than prudent to penalize the contractor on these bases by requiring a refund to the project. USAID/Honduras needs to improve contract administration to ensure that terms are not in conflict so that procurement activities may be implemented effectively and efficiently.

AUDIT
OF USAID/HONDURAS' COMPLIANCE WITH
AID'S REVISED PAYMENT VERIFICATION
GUIDELINES

PART III - EXHIBITS AND APPENDICES

AUDIT OF USAID/HONDURAS' COMPLIANCE WITH AID'S REVISED PAYMENT VERIFICATION GUIDELINES

POLICY STATEMENT (NO.)	STATUS
1. A comprehensive general assessment of methods of implementation and financing, reviewed from the standpoint of accountability, is to be presented on a regular basis and more specific assessments are to be included in the Project Papers.	USAID/Honduras provided comprehensive general assessments of methods of implementation and financing for reporting years 1983, 1984 and 1985. The assessment for reporting year 1985 was sent to AID/W over three months late because the official assigned the task of preparing and submitting the assessment was not at Post, and other officials were not reassigned the task. Specific assessments were generally complete for the ten project papers reviewed.
2. AID/W Controller concurrence on the implementation and financing aspects are to be included in the general assessment and the more specific PP assessments requiring AID/W review.	It could not be determined at USAID/Honduras if the AID/W Controller concurred with the implementation and financing aspects included in the USAID/Honduras general assessments. It was assumed that there was tacit concurrence in that there was no feedback to the contrary. However, four of the ten project papers reviewed, while not requiring AID/W Controller review, did not have USAID/Honduras Controller's concurrence.
3. As a part of the assessments under 1. above, a justification is to be submitted whenever the mission proposes to depart from any of the following general policies:	USAID/Honduras used 11 Direct and 14 Bank letters of commitments during the reporting years. Each departure was justified.
(a) The use of Fixed Amount Reimbursement (or modified Fixed Amount Reimbursement) as the preferred method in financing multiple unit construction.	See above.

POLICY STATEMENT (NO.)	STATUS
(b) Use of the Federal Reserve Letter of Credit (FRLC) procedure. (Note that FRLCs may be used only in the case of non-profit organizations. They cannot be used in any case for host country contracts or loan-financed contracts.)	See above.
(c) The use of the direct reimbursement procedure (reimbursing the host country, contractors and others) instead of other methods of payment which entail AID financial credit instruments to direct payments for contractors and suppliers.	See above.
4. As part of the assessments under 1. above, a justification is to be provided whenever the mission proposes use of the bank letter of commitment rather than the direct letter of commitment except for CIP and project commodity financing for which the mission anticipates a proliferation of invoices.	USAID/Honduras provided justifications for use of each of the 14 Bank letters of commitment.
5. Where host country contracting is proposed as a means of implementation, the assessments required under 1. above must set forth a realistic appraisal of the prospective contracting agency's ability to (a) advertise, award and negotiate contracts, (b) monitor contract implementation, (c) examine invoices and (d) audit contractor records and reports. If local currency is to be made available to an ICI or to any other organization responsible for controlling and reporting on the use of such funds, the mission should first assess the organization's financial management procedures and related internal controls. Such an assessment should also be performed	USAID/Honduras had made on-site visits to about 30 host country agencies (representing $58 million in obligated receipts from AID) in order to assess their capabilities in accordance with Policy Statement No. 5. Another five formal reviews were planned for the near future.

POLICY STATEMENT (NO.)	STATUS
5. (Cont'd) as a prerequisite for providing grants to indigenous PVOs. Subsequent audit or evaluation reporting on the project should measure performance in reference to the assessments made under 1. above, as well as other appropriate factors.	
6. PPs are to include an evaluation of the need for audit coverage in light of potential risks and are to describe planned contract and project audit coverage by the host government, AID, and/or independent public accountants. Project funds should be budgeted for independent audits unless adequate audit coverage by the host country is reasonably assured or audits by third parties are not warranted as, for example, in the case of direct AID contracts or direct placement of participants by AID.	Only one of the 10 project papers (representing $45.1 million in obligations) contained evaluations of the need for audit coverage. Officials maintained that the provisions for audit were commingled with the evaluation components. Nonetheless, they agreed that more specific language was needed in project papers.
7. In lieu of the current negative statement, the project officer is to provide to the Controller a statement advising of the basis upon which administrative approval is given.	Statement No. 7 was to be implemented in accordance with a newly designed project officers' checklist. Only five of the fifty-two vouchers reviewed were without the checklists.
8. Mission controllers are responsible for providing annual assessments of the mission voucher approval and voucher examination procedures. Such assessments should indicate the adequacy of supporting documents submitted with contractor invoices and the ability of project officers and authorized certifying officers to relate contractor performance with contractor invoices.	The implementing guidelines called for the assessments to be supported by tests of random samples of vouchers. USAID/Honduras did not make and test random samples of vouchers for reporting years 1983 through 1985. In response to the audit finding and recommendation contained in this report, USAID/Honduras made and tested a random sample of 100 vouchers in the amount of $2.8 million in claims to support its 1986 general assessment.

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POLICY STATEMENT (NO.)	STATUS
9. Mission controllers are to provide annual assessments of the adequacy of the monitoring and invoice examination procedures followed by host country contracting agencies. Such assessments should serve as the basis for reliance on host country performance certificates and voucher review.	See status of Policy Statement No. 5, above.
10. (a) USAID Controllers are encouraged to utilize the services of competent public accounting firms to a greater degree in providing accounting and financial management consulting services within the project design as a part of program funding and in auditing host country contracts. Auditing services will be conducted on the basis of pre-approval by the Inspector General staff.	The non-Federal component of RIG/A/T had initiated negotiations to attract qualified accounting firms to be used in Central America on a regional basis. At the time of audit, the paperwork lay with USAID/Honduras' contracting officer. USAID/Honduras had already used about $12,000 for non-Federal audits.
(b) In their areas of responsibility, USAID controllers are encouraged to use contract personnel to supplement direct-hire foreign nationals for voucher examinations.	USAID/Honduras' voucher examining staff was adequately balanced with foreign service and contract personnel.
11. The agency's commodity price analysis function should be strengthened to permit more adequate pre- or post-payment audit of commodity costs.	The Policy Statement called for AID/Washington rather than field implementation.
12. Where suitable and subject to Federal and AID control guidelines, the agency should place greater reliance upon incentive contract approaches, where contractors share in savings or receive extra benefits for timely completion.	The Policy Statement called for AID/Washington implementation and requested examples from the field. There was no evidence that USAID/Honduras had provided examples.

POLICY STATEMENT (NO.)	STATUS
13. Host country contracts should include definitive requirements for submission of invoices and supporting documents.	USAID/Honduras was in compliance.
14. Models for use of the Fixed Amount Reimbursement concept for non-construction projects should be developed for consideration.	The implementing instructions called for AID/Washington action and requested examples from field stations. There was no evidence that USAID/Honduras had provided examples.
15. Definitive requirements for arrival accounting should be developed and published for CIP programs. Assessments of arrival accounting systems should be included in all CIP approval documents (PAADs).	There was no Commodity Import Program (CIP) in effect in Honduras.
16. The agency will explore resuming use of formal two-step loan agreements given the increased emphasis on private sector participation.	The implementing guidance called for AID/Washington action.

AGENCY FOR INTERNATIONAL DEVELOPMENT

UNITED STATES OF AMERICA AID MISSION TO HONDURAS
AMERICAN EMBASSY
TEGUCIGALPA, HONDURAS

MEMORANDUM

April 15, 1987

TO: Coinage Gothard, RIG

FROM: John Sanbrailo, Mission Director

SUBJECT: Response to the Draft Audit Report, Audit of USAID/Honduras' Compliance with AID's Revised Payment Verification Guidelines

We have additional comments and observations on the draft report which we believe are required to give perspective and balance to the report. As you will see from USAID's comments, we believe that the draft report still requires additional work before release. The report, as currently written, presents an unbalanced view of our efforts and successes in implementing the revised payment verification guidelines. The unbalanced view in the report does not, in our judgment, present an accurate picture to the reader.

Moreover, the conclusions drawn from the facts presented are not, in every case, logical and the recommendations do not always flow from the conclusions. As a result, we recommend that you utilize our comments to prepare a revised draft report and resubmit it to USAID for final comments. We believe that such action in this case would produce a more useful report. Should this not be possible, we request that you incorporate the gist of our comments in the body of the report and attach our complete comments as an annex to the final report.

Should you decide not to produce a revised draft report, we include below a USAID statement that we request be included in the Executive Summary of the final report. This statement is being offered per our earlier discussions on how RIG can produce more balanced reports.

> "USAID believes that the report does not present a balanced view of how it has complied with AID's revised payment verification guidelines. USAID disagrees with some of the findings and recommendations, especially the conclusions leading to recommendation 3 and recommendations 2, 3, 5(a), 7, and 8. It believes that the Mission has effectively implemented the guidelines on cash management procedures by (i) requiring entitites to use their own resources to finance initial operations where feasible, (ii) limiting advances to immediate disbursing needs for those entities that do not have sufficient operating funds, (iii) closely monitoring cash management practices of recipients to ensure that no excess cash balances are held and (iv) attempting to obtain regular reports from recipients on the use of AID advances. USAID also observed that the conclusions of the report contradicted recent project audits which concluded that it needed to ensure a more steady and dependable source of funding to ensure better implementation."

RESPONSE TO FINDINGS/RECOMMENDATIONS OF THE DRAFT RIG PAYMENT VERIFICATION AUDIT

In general, our comments made on the findings and recommendations in the body of the report will, if accepted, require corresponding changes in the Executive Summary.

Page ii of the Summary and page 4 of the results of audit state that ". . . . USAID/Honduras was not in compliance with the Policy Statements in seven instances." We are unable to reconcile this statement with the findings and data in the report. Exhibit 1 lists sixteen payment verification guidelines, four of which do not apply to this Mission. We believe that at the time of audit, USAID/Honduras was in compliance with all twelve policy statements that were to be implemented by field missions. The statement coupled with your judgment that we had realized only limited success in implementing the guidelines indicates a serious failing on the part of the Mission and we would like an opportunity to respond if your recount still shows us not in compliance. Perhaps the problem is that you are talking about the entire period of time from the issuance of the guidelines to the time of the audit and we are looking for a snapshot on the date of the audit.

In the second paragraph on page 4 of the results of audit and on page ii of the summary, we believe that the word "burden" should be changed to responsibility.

Your statement in the first paragraph on page 5 of the results of audit and the third paragraph on page ii of the summary that "Recipients received advances made by USAID/Honduras far in excess of immediate disbursing need" is not supportable. Neither is the second paragraph on page iv discussing the alleged failure of the USAID to follow established procedures a fair presentation of the facts. We believe the data for this finding stems from a review of our aging report on advances and not a review of the processes and procedures. This Mission strongly supports and has effectively implemented the guidelines on cash management procedures. We monitor cash management practices of recipients to ensure that excess balances of cash are not held and we attempt to have the entity regularly report on the use of funds. In 1986, we issued 43 reports, many of which included reviews of cash managment practices of entities. The write up in the summary indicates that large amounts of cash advances remain outstanding. We believe that it is more appropriate to state that large, book balances of unliquidated advances remain on the USAID's accounting records even though the cash had been completely used months before. Our estimate is that recipients of all projects have cash on hand of just over one million dollars which given the size of the program is, in our opinion, reasonable. Moreover, we would like to point out that the cash on hand is, for all practical purposes, money that has been received recently from the Mission.

On page 6, you conclude that since the adequacy of the Mission's voucher approval and examination processes were not tested through a randomly selected sample of vouchers, the adequacy of the voucher approval and examination processes to support the integrity of the portfolio was not <u>verifiable</u>. The processes were and are verifiable. As you point out, the Mission relied on personal knowledge of supervisory personnel to assure that the system in place was adequate. In the sample that was done to support our 1986 assessment, we chose 100 vouchers at random and found that the vouchers were properly supported with required documentation. We believe that the results of this sample fully support our decision to rely on personal knowledge of the supervisory personnel in the earlier assessments. The language in the policy guidelines indicates that the sample is desirable but optional. Even though there is a disagreement between USAID and RIG on the adequacy of earlier assessments, we hope that this is not one of the guidelines that you feel we were not in compliance with.

We believe that the title of section No. 2 on page 8 should be revised since, in our judgment, voucher examination of PVO's claims is more than adequate. We do not believe that you can conclude, based on a limited review of two local PVOs, that the voucher approval and examination procedures for local PVOs need strengthening. Both of these grants were executed in accordance with Handbook 13 procedures and use the formats suggested in the appropriate chapter of the Handbook. Our local procedure requires, as a precondition to making a grant, an examination of the accounting and internal control systems used by the grantee.

In addition, we make periodic on site financial reviews of the documentation supporting the expenditures reflected on vouchers that have been sent to USAID to liquidate advances. For your information, we have performed two financial reviews of the Advisory Council on Human Resources (CADERH). On April 15, 1985, we issued Financial Report No. 85-20 which covered ESF local currency expenditures totalling $88,388 for the period August 1, 1984 to February 28, 1985. On October 6, 1986, Financial Review Report No. 86-50 on CADERH's operations was issued. We examined $729,115 of expenditures for the period ending May 31, 1986. Our review questioned many items, including the items questioned by RIG auditors on international travel, purchase of books by a PVO member, and excess baggage payments. Documentation was submitted by CADERH for the questioned transactions.

On March 10, 1986 we issued Financial Review Report No. 86-10 which was made to determine the adequacy of CEPROD's accounting and internal control systems. Four recommendations were made to improve the internal controls. We have completed another financial review of the documentation supporting CEPROD's expenditures to determine which costs are allowable for the period beginning September 4, 1986 to December 31, 1986. A draft report has been prepared on the results of the examination. We reviewed $261,130 of expenditures for the period.

Based on our experience with PVO's receiving grants financed by USAID including the two PVO's covered in the audit, we do not agree with the statement on page 8 that "USAID/Honduras could conceivably be losing an estimated $420,000 annually in payments for questioned or ineligible cost claims". The statement is, in our opinion, unprofessional and without foundation and strikes us as pure speculation. The statement should be deleted unless the auditors can substantiate in a credible manner the methodology involved in the projection. We are particularly distressed by the inappropriate use of questioned costs, 99% or more of which will end up being accepted, and simply multiplying by the number of entities in the universe. The initial review of PVO payment documents usually discloses items which are not properly supported for one reason or another. However, the documentation is almost always presented at a later date for the questioned items.

We also find somewhat incongruous your determination that a disproportionate amount of time would be expended by USAID/Honduras to effectively monitor PVO claims by making periodic field tests and the implied suggestion that a detailed review of payment documents in the office would represent an effective use of resources. We do not agree with the conclusions on page 14 concerning monitoring the costs of PVO's and relying only on annual audits made by external auditors. The Mission's policy for PVO's which submit summary type billings calls for making periodic financial reviews of the organizations. These reviews are being performed by external auditors, Mission personnel and by RIG auditors. Three of the fifteen PVO's receiving dollar assistance have been submitting to the Mission detailed documentation to support claims for payment. The documents are examined by the Mission voucher examiners. There are four U.S. PVO's that are subject to I.G. audits verifying allowable expenditures since the records are in the U.S. Mission personnel have made financial reviews of the 15 PVO's accounting and internal control systems. Some PVO's operations have been reviewed twice and financial reports issued on the results of the examination.

The Mission will continue to make financial reviews of PVO's dollar expenditures that are managed in Honduras. We believe that the Mission is effectively monitoring PVO's and OPG payment claims for dollar and lempira costs. Your comments on page 14 should be revised or deleted from the final report.

In summary, we do not believe that the types of expenses that you are questioning on both PVO's warrant the space being devoted to the finding in the draft report or the lengthy recommendations that you are proposing. Our detailed comments on recommendation number 2 follow:

a. We do not agree with the recommendation to collect $1,126.50 from CEPROD for sales taxes. Some of the unallowable costs listed in the standard provisions (Attachment 3) of CEPROD's grant agreement and commented on in your finding are authorized in appropriate circumstances. Under the terms of the Standard Provisions clause entitled "Allowable Costs", the determination of allowability is made in accordance with the cost principles of OMB Circular A-122. This circular provides that, in general, taxes which the organization is required to pay and which are paid are allowable so long as exemptions from the taxes are not available to the organization. CEPROD does not have a tax dispensa and it is not cost effective for local PVOs to request that the Mission make a series of small purchases using the general exemption from taxes afforded AID under the bilateral agreement. In our judgment, sales taxes incurred by this organization are eligible costs under the grant agreement. Since the Grant Agreement incorporates OMB Circular A-122 provisions, we believe that you should accept the Mission's position which has subsequently been validated by State cable 397888 and drop the finding and recommendation. We request that you consider such action.

b. The amount of $1,193.67 (L.2,387.55) was questioned by the auditors due to the lack of detail to determine the propriety of the expenditures. An additional amount of $332.88 (L.665.76) was reported as undocumented. The Grantee furnished us the documentation supporting the questioned amounts of $1,193.67 and $ 332.88 ($1,527 in total):

Advance to electrical contractor	L.	2,300.00
Food for seminar participants on community health		52.55
Purchase of a pie - "Childs day"		15.00
Magician's fee for seminar		20.00
TOTAL	L.	2,387.50
Freight - transported lumber	L.	25.00
Contribution to hygiene campaign		40.00
Food for participants - seminar		574.50
Freight - transported blocks of cement		26.26
TOTAL		665.76

CEPROD has deposited to the Project's account the amount of $ 17.50 (L.35.00) for the cost of the pie and the magician's fee. The work by the electrical contractor has been completed but his final claim has not been submitted to liquidate the advance. We regard all items other than the pie and magician's fee as proper project disbursements. Although not covered in the recommendation, on February 19, 1987, CEPROD deposited in Banadesa Bank Account No. 7-0419-18 the amount of $133.65 (L.267.30) for food and beverages that were disallowed.

c. The building construction was in process in January 1987 and billings were submitted to CADERH by the contractor for completed work. In addition, other improvements have to be made by the contractor before completing the job. There was a balance of $2,983.50 (L.5,967.00) that was pending liquidation by the contractor. CEPROD has asked the contractor to liquidate the outstanding advance as soon as possible. We will examine the supporting documents to verify the actual expenditures of the contractor and determine if they are allowable.

d. On March 25, 1987 CADERH deposited to the dollar account $229.00. This amount was to cover the $125.00 advanced to Dialog Information Services Development, $40.00 for the purchase of a book required but without an invoice, $44.00 for personnel medical expenses and $20.00 for excess baggage.

e. As previously noted in our response to the RAF, the $11,409 in travel by CADERH was done with the full knowledge and concurrence of the Project Officer and was essential to accomplish the purposes of the grant. Indeed, the Mission was involved in the travel plans and informally approved the disbursements made to travelers for each trip. Annex C, Section 14(a) contained the grant officer's approval for international travel provided that the grantee obtained written concurrence from the Project Officer. On March 27, 1987, the Mission approved the travel made by CADERH members since the beginning of the Project. The Mission has also formally approved the use of non-US flag carriers for travel between Honduras and Houston, New Orleans, Panamâ, Colombia, and Costa Rica. Approval for the use of foreign carriers for travel between Honduras and Miami and other points is still pending an explanation by the PVO. It should be noted that U.S. carriers were not always available because of maintenance or other mechanical problems and climatic conditions.

f. CADERH has prepared and submitted to the Mission a cumulative budget report showing the total budgeted amount for the Project, total costs to date, and the unexpended balance (see attachment).

Based on the corrective actions taken and comments offered, we ask that the recommendations be closed and the findings appropriately modified.

The title to section No. 3 of the report should be changed as the Office of the Controller is maintaining an effective control on advances made to AID projects and to individuals.

We take issue with your stating that recipients received advances far in excess of immediate disbursing needs because prescribed policies and procedures were not followed. This Mission strongly supports and has effectively implemented the guidelines on cash management procedures. Not only do we attempt to have entities use their own resources to finance their operations and limit advances to immediate disbursing needs for those who cannot, but we also monitor cash management practices of recipients to ensure that excess balances of cash are not held and we have the entity regularly report on the use of funds. The write up in the summary indicates that large amounts of cash advances remain outstanding. The auditors concluded that $3 million in outstanding advances exceeded the parameters of Agency policy, that is, cash requirements for a 30 to 90 day period. We believe that it is more appropriate to state that large, book balances of unliquidated advances remain on the USAID's accounting records even though the cash had been completely used months before. Our estimate is that recipients of all projects have cash on hand of just over one million dollars which given the size of the program is, in our opinion, reasonable. Moreover, we would like to point out that the cash on hand is, for all practical purposes, money that has been received recently from the Mission. Your computation of the annual cost in interest to the U.S. Treasury because of our failure to comply with Agency policy is wrong and should be dropped from the report.

For example, our analysis of projects with outstanding advances showed the following (see attachment):

Balance as of 3/6/87	$	6,714,572
Documents on hand or at the implementing agencies		5,004,562
Cash on hand at verified Agencies		1,183,248
Amount not verified		526,762

Time did not permit us to verify the breakdown of certain projects due to entities being located in the United States or outside of Tegucigalpa. The Mission is continuing to aggresively press recipients of advances to liquidate the outstanding amounts on a timely basis. Contrary to your statement on page 17 of the report, the first follow-up on advances did not occur on November 18, 1986 but has been a feature of the system going back at least to 1983. Our aging report that you used to present the data was programmed in late 1983. With additional staff, the persistence and timeliness of the follow-ups have improved. We believe the finding and recommendation No. 3 should be deleted from the final report.

Recommendation No. 5(a) on page 21 does not follow from the finding which we believe is off base. We do not believe that you can conclude that there is anything wrong with our procedures for making prompt payments to take advantage of discounts when the terms on your alleged discount were neither offered in the propcsal received nor included on the invoice submitted. We see no need to establish additional procedures for taking discounts. It is standard Mission practice to accept offered vendor discount terms if payment is made within the discount period and the discount results in a monetary advantage to the U.S. Government. We would also like to note that while AID's policy is to use public resources effectively and economically, we believe that the policy can best be accomplished by scrupulously following established procurement procedures to obtain a reasonable price. Nothing in your finding indicates (nor could the finding indicate) that the Mission followed anything other than correct procurement procedures. Whether the local hardware store would have provided a discount, as indicated in your report, is hindsight regardless of what they say they would have done. We request the finding and recommendation be omitted from the final report.

The Mission has initiated action to recover the hidden taxes paid for fuel purchased on behalf of Project No. 522-0278. The documentation for obtaining the refund or credit has been processed and forwarded to the Embassy's JAO for securing the tax exemptions on the fuel. Please close this recommendation as we have taken corrective action.

To close recommendation number 6, the RIG asked for documentation showing that project papers now include funds and language on audit coverage. We are attaching two documents for Projects No. 522-0246 and 522-0257 that were recently processed by the Mission. The documents clearly show funds have been set aside to pay for audits of the projects. Please close the recommendation.

The Mission is not in agreement with the finding leading up to recommendation No. 7 or recommendation No. 7 because, in our judgment, we are complying with the intent of Policy Statement No. 7. Project Officers are aware they must administratively approve vouchers and complete and attach a checklist to vouchers. These actions provide reasonable assurances that the voucher charges represent actual performance, delivery or other benefits received. Further, voucher examiners have been instructed to not process vouchers that do not have attached a Project Officer's checklist. Voucher examiners were also instructed to return to Project Officers vouchers with checklists that are not properly completed or contain questionable comments. We do not believe it is necessary to repeat to Project Officers the intent of Guideline No. 7 as the same information is provided in Handbook No. 3, Project Officers' Handbook and covered in the Project Implementation Course that each project officer takes normally within three years of entering on duty with AID. All USAID project officers who have not attended the PIC course will be attending in May 1987. Moreover, our review of 100 vouchers drawn at random indicates that the project officer's checklist is being used as designed and intended which is as an aid in assuring the certifying officer that the project officer has reasonable knowledge of the status of the project in approving payments.

On page 30, second paragraph, we did not agree that calendar annotations must be used to support the completion of Project Officers' checklists. Such a technique is appropriate and is used by some officers but should not be mandatory for all. It would be extremely onerous for a Certifying Officer to depend on a calendar annotation for approving a voucher for payment and, in the final analysis, you would end up with essentially the same system that we have now where the integrity of the project officer is a key element of the project management system. The project officer approval system is a standard world wide system that USAID/Honduras relies on to protect the interest of the

Agency. We do not believe that any tinkering with the system at the local level is called for since any improvements in the system must be weighed against the costs of the improvements and we do not believe that a case has been made that the suggested changes will improve the system and/or be cost effective. We again ask that the finding and recommendation be omitted from the final report.

In Section No. 8, the draft report states that the USAID failed to obtain a source/origin waiver to authorize procurement of the equipment from AID Geographic Code 941, and the USAID should recover the acquisition cost of $57,810 from the supplier for the wheel loader procured from Brazil. It is the Mission's opinion, concurred in by legal counsel, that the action taken to acquire the equipment was in compliance with Agency source/origin rules and policies and federal acquisition policies, principles, and procedures.

The intent of the Project Agreement with SECOPT, as specified therein, was to authorize the procurement of goods and services from AID Geographic Code 941. The intent of the contracting parties, as evidenced by Casa Mathews' quotation accepted by the USAID, and as specified in the contract schedule, was to acquire the wheel loader from Brazil. It is apparent that an inapplicable boilerplate clause was mistakenly included in the contract, and the Contracting Officer cannot knowingly enforce his own mistake since that would abrogate the agreement of the parties.

The fundamental issue is a question of contract interpretation not source/origin, since the Mission purchased the equipment in accordance with the authorized source/origin under the Project. To further define the issue, one should ask why a Contracting Officer would insert a special provision into a contract whereby he abrogates his authority so that he has to seek a waiver to reinstate authority that he had by virture of the project agreement absent the special contract language. Absent the special provision, the contract would meet the objective intent of the contracting parties and conform to the project agreement. We suggest that the contract be read and interpreted on that basis. A basic rule of contract interpretation is that contract provisions are to be constructed to accord with the "objective" intent of the parties, i.e., could the contractor reasonably interpret the requirement, and the answer is yes, as evidenced by the concurrent interpretation given by the parties in the course of actual contract performance. As for the apparent conflict between the Specific Provisions (the schedule) and the general provisions (Special Contract requirements Boilerplate), a basic rule of common law and acquisition regulation is that, unless specified otherwise, the Specific Provisions control. Furthermore, a general provision joined with a specific one will be deemed to include only those things which are similar to the specific provision. Finally, it would seem that since many general provisions are incorporated without complete consideration of their application to the particular contract, they should be particularly subject to

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limitation by proof of course of dealing, trade practice, concurrent interpretation and other principles of contract interpretation.

The essence of our response and interpretation, as stated, is that the contract must be interpreted reasonably under all circumstances. Any observation and/or recommendation which results in an illogical, strained, impractical or unjust interpretation, or in any way conflicts with the basic concept is erroneous and without merit. We request that the finding and recommendation be omitted from the final report.

List of Recommendations

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Recommendation No. 1 4

We recommend that USAID/Honduras:

a) ensure the adequacy of the voucher approval and examination process by performing a randomly selected sample of vouchers; and

b) document the work performed to ensure the adequacy of the voucher approval and examination process.

Recommendation No. 2 6

We recommend that USAID/Honduras:

a) recover $1,260 in unallowable sales taxes reimbursed to Centro de Estudios y Promocion del Desarrollo;

b) require Centro de Estudios y Promocion del Desarrollo to provide documentation for $1,527 in questioned costs under voucher 522-87-0447; and collect any unsupported amounts;

c) reconcile the advance and expenditure records to show the correct status of $7,389 subadvanced by Centro de Estudios y Promocion del Desarrollo to a contractor;

d) collect $66 in unallowable costs from Advisory Council on Human Resources Development and recover $125 advanced to Dialog Information Services under voucher 522-86-3647;

e) require the Advisory Council on Human Resources Development to provide documentation for $11,409 in unsupported costs under vouchers 522-86-4086 and 522-86-3647; and collect any unsupported amounts; and

f) determine whether international travel performed by members of the Advisory Council on Human Resources Development in Honduras was justified, and if so;

   i) ensure that the grant officer's justification is included in documentation of the payment voucher; and

   ii) ensure that a cumulative detailed report of disbursements by budget line item is submitted quarterly to AID.

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Recommendation No. 3 10

We recommend that USAID/Honduras review and justify, liquidate or recuperate (including interest income) about $4.4 million in advances that have been outstanding for more than 90 days.

Recommendation No. 4 13

We recommend that USAID/Honduras:

a) review the portfolio of unused airline tickets, and initiate immediate follow-up requests for refunds on all previous requests that are over 30 days old; and,

b) establish procedures to monitor, control and document redemptions in process by carriers.

Recommendation No. 5 15

We recommend that USAID/Honduras request a refund from Dippsa, a local fuel vendor, in taxes paid for fuel purchases on behalf of Project No. 522-0278.

Recommendation No. 6 17

We recommend that USAID/Honduras establish procedures to include in project papers language specifically designed to fund audit coverage and earmark funds that are budgeted for independent audits.

Recommendation No. 7 19

We recommend that USAID/Honduras reiterate to project officers the provisions and intent of the AID Administrator's Payment Implementation Guideline No. 7.

APPENDIX 3

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