PD-AAV-992

AUDIT OF
THE SOUTH PACIFIC
PRIVATE AND VOLUNTARY ORGANIZATION
CO-FINANCING PROJECT
NO. 879-0001

Audit Report No. 2-879-87-09

August 18, 1987

a

OPTIONAL FORM NO. 10
MAY 1962 EDITION
GSA GEN. REG. NO. 27
5010-104

UNITED STATES GOVERNMENT

Memorandum

TO: Mr. William E. Paupe
Director, USAID/RDO/SP

DATE: August 12,1987
RIG/EA-87-185

FROM: Leo L. LaMotte
RIG/A/M

SUBJECT: Audit Report No. 2-879-87-09
Audit of the South Pacific Private and Voluntary Organization Co-Financing Project

This report presents the results of audit of the South Pacific Private and Voluntary Organization (PVO) Co-Financing Project No. 879-0001. This was primarily a program results audit which focused on the specific objectives of determining if the grantees' project activities met A.I.D.'s programming and management requirements, the adequacy of PVO local office accounting systems, and whether the U.S. was adequately recognized as the grantor.

The audit showed that small project activities funded by the Co-Financing Project were too technically varied and geographically dispersed to be managed economically and efficiently and generally could not demonstrate a development impact; accounting and financial management systems at local offices of some grantees were inadequate; and A.I.D. grant-assisted activities were not adequately identified as American aid.

The report contains three findings, i.e.: most small project activities funded under the Co-Financing Project could not demonstrate a development impact and were uneconomical and inefficient to manage; the financial management systems of six of the eight grantee field offices reviewed were deficient; and grantees which received assistance under this project frequently did not inform subproject recipients that the funding was from A.I.D..

Report recommendations relating to your office are that: 1) new project funded activities should be concentrated technically or geographically and have a demonstrable economic development focus; 2) more specific guidance be provided to grantees as to A.I.D.'s financial management and audit requirements; and 3) more specific guidance be provided to PVOs as to marking of A.I.D.-funded commodities and recognition of A.I.D. funding of other activities. The Controller, Philippines, has primary responsibility for Recommendation 3.

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In the response to the draft of this report, you neither agreed nor disagreed with Recommendation 1, but indicated an understanding of the issues and concerns raised. However, you stated that they should be considered in a broader context. RIG/A Manila believes the issues raised in this report should be addressed now and the recommendation implemented. You stated general agreement with the spirit of Recommendation 2. The Controller, Philippines agreed to Recommendation 3 for which he has responsibility. Your response also indicated general agreement with the spirit of Recommendation 3.

Please advise us within 30 days of any additional information relating to actions planned or taken to implement the recommendations for which your office has responsibility. We appreciate the cooperation and courtesy extended to our staff during the audit.

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Memorandum

TO: Mr. Loc Eckersly
Controller
USAID/Philippines

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Report Recommendation 3 directed to your office is that assistance be arranged for local offices of PVOs in establishing adequate accounting systems. In the response to the draft of this report, your office agreed to Recommendation 3 and indicated some progress in implementing it.

Please advise us within 30 days of any additional information relating to actions planned or taken to implement the recommendation. We appreciate the cooperation and courtesy extended to our staff during the audit.

EXECUTIVE SUMMARY

The Private and Voluntary Organization Co-financing Project was authorized $20 million in grant funds between 1984 and 1988 to promote development activities in the South Pacific for low-income groups utilizing U.S. and local private and voluntary organizations. This project was the continuation of a similar 1977 A.I.D. project which was said to be the foundation of A.I.D.'s program in the South Pacific. The South Pacific Regional Development Office in Suva, Fiji, managed the program. As of September 1986, $10.9 million had been obligated and $7.7 million expended to implement 29 subprojects in a variety of areas.

This was primarily a program results audit. Eleven grantees in eight countries received funds under this project. Audit efforts were concentrated on five grants which totalled $5.2 million of the $7.7 million expended. These grantees were located in the countries of Fiji, Papua New Guinea, Solomon Islands and Tonga. After a broad based survey, the audit focused on the specific objectives of determining (1) if the grantees' project activities met A.I.D.'s programming and management requirements, (2) the adequacy of the Private and Voluntary Organization local office accounting systems, and (3) whether the U.S. was adequately recognized as the grantor.

The audit showed that: (1) small project activities funded by the Co-Financing Project were too technically varied and geographically dispersed to be managed economically and efficiently and generally could not demonstrate a development impact; (2) accounting and financial management systems at local offices of some grantees were inadequate; and (3) A.I.D. grant-assisted activities were not adequately identified as American aid.

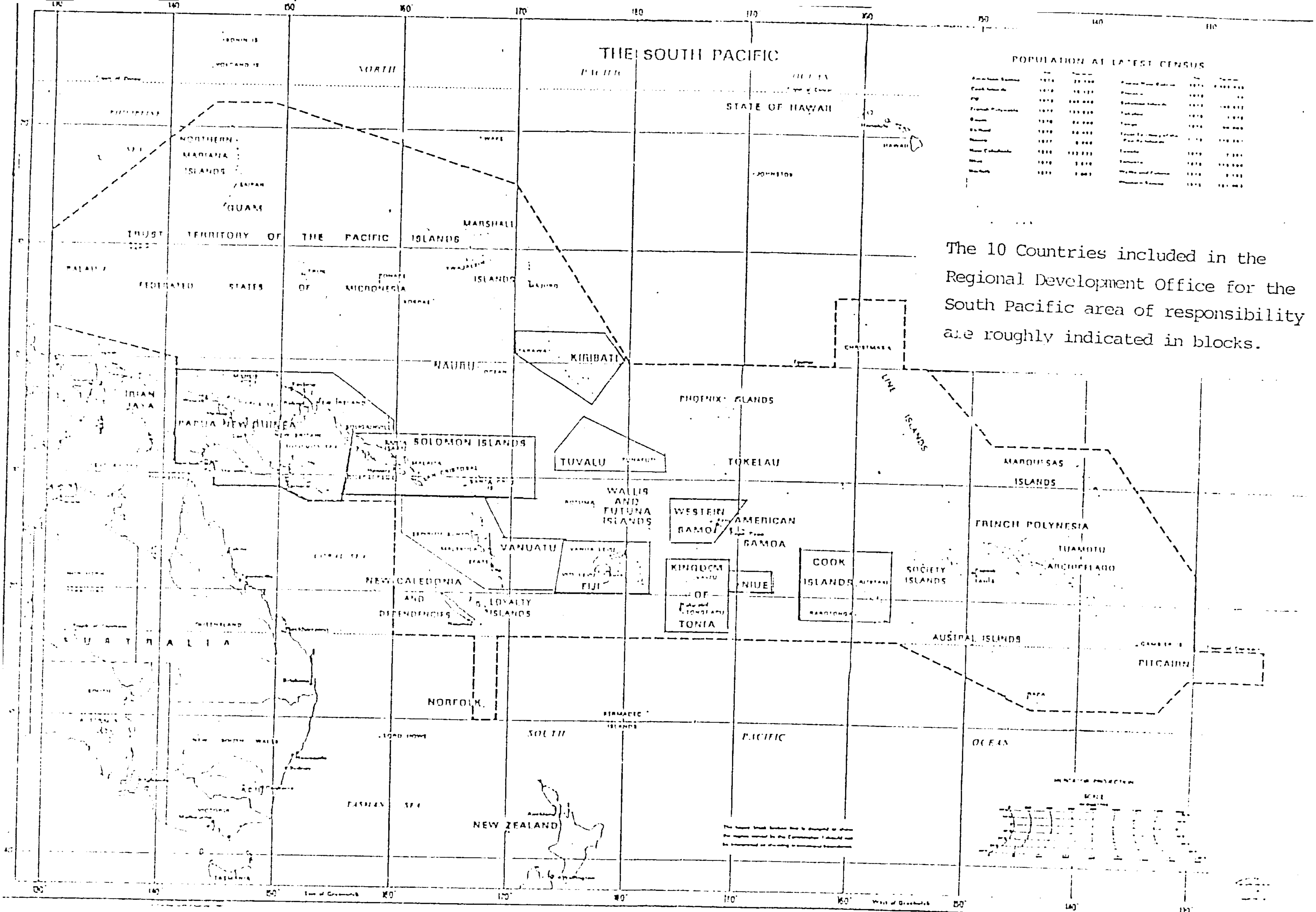
A.I.D.'s 1987 Congressional Presentation stated that the U.S. has important interests in the South Pacific, including ensuring that it has regional goodwill. A.I.D.'s objective in advancing these interests is to maintain a useful and meaningful presence in concert with the major donors, Australia, New Zealand, and Great Britain. Providing assistance through voluntary agencies allows A.I.D. to achieve this objective with a minimum of direct-hire personnel. This objective was largely being achieved as grantees were operating in the area and had established linkages with host governments and local organizations. A number of project activities were functioning well and being implemented as planned.

A.I.D.'s policy is to increase the economic development impact of voluntary agency programs, focus resource use, and utilize funds economically and efficiently. Most small project activities funded under the Co-Financing Project could not demonstrate a development impact and were uneconomical and inefficient to manage. This occurred because subprojects were too technically varied, geographically dispersed, and lacked a specific economic development focus. As a result, A.I.D. funds were expended uneconomically for subprojects that did not demonstrate a significant development impact. We recommended that the project fund only project activities that are concentrated technically or geographically and have a demonstrable economic development purpose. The Regional Development Office did not agree nor disagree with the recommendation, but indicated an understanding of the issues and concerns raised. However, it believes they should be considered in a broader context. The Regional Inspector General's office believes the issues raised in this report should be addressed now and the recommendation implemented.

A.I.D. regulations specify criteria as to the financial management systems of grantees and that the Mission Controller determine whether the systems are adequate. The financial management systems of six of the eight grantee field offices reviewed were deficient. These deficiencies resulted from inadequate guidance to these field offices as to A.I.D's financial management requirements, the lack of audits at these offices, and failure of the responsible Controller to ensure that these local offices had adequate accounting systems. As a result, expenditures were made for unauthorized purposes and A.I.D. cold not be assured that funds were used properly. We recommended that more specific guidance be provided to grantees as to A.I.D.'s financial management and audit requirements and assistance be provided to local offices of grantees to establish adequate accounting systems. The Regional Development Office generally agreed with the spirit of these recommendations. The Controller, Philippines agreed to see that assistance is provided to Private and Voluntary Organization local offices.

A.I.D. is required by law to ensure that its programs are identified overseas as "American Aid". Grantees who received assistance under this project frequently did not inform subproject recipients that the funding was from A.I.D.. This condition resulted from the lack of guidance to A.I.D. offices and private and voluntary agencies generally as to requirements for marking and other recognition of A.I.D.-funded activities under grantee management. It also resulted from inadequate specific guidance to the offices reviewed. As a result, recipients frequently did not know that they were receiving assistance provided by the U.S. Government and the intent of the law was not complied with. We recommended that more specific guidance on marking requirements be provided to the grantees. The Regional Development Office generally agreed with the spirit of this recommendation.

Office of the Inspector General



The 10 Countries included in the Regional Development Office for the South Pacific area of responsibility are roughly indicated in blocks.

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PART 1 - INTRODUCTION

A. Background

The Private and Voluntary Organization (PVO) Co-financing Project (879-0001) for the South Pacific Region was authorized to promote development activities in the South Pacific Island nations and to improve the social and economic status of rural and urban low-income groups utilizing the management expertise of U.S. and local private and voluntary organizations. The South Pacific regional program area is made up of 10 independent island nations: Cook Islands, Niue, Tonga, Tuvalu, Western Samoa, Fiji, Papua New Guinea, Solomon Islands, Vanuatu, and Kiribati. Geographically, the nations comprise over 1,300 islands with a population of 4.3 million, mostly in Papua New Guinea (70 percent) and Fiji (14 percent). The region contains a wide variety of cultures, environments, and political systems. Most of the countries have serious problems, including a lack of basic infrastructure, high unemployment rates, and limitations on development.

The PVO Co-financing Project started in Fiscal Year 1984 and was scheduled for completion in Fiscal Year 1988. This project was a continuation of a similar 1977 A.I.D. project which was said to be the foundation of A.I.D.'s program in the South Pacific. The Regional Development Office for the South Pacific (RDO/SP) in Suva, Fiji, manages the program with assistance from the USAID/Philippines Area Contracting Office, and Controller and the USAID/Indonesia Regional Legal Office.

The Project was authorized not to exceed $20 million in grant funds over the five-year period. As of September 30, 1986, $10.9 million had been obligated, of which $7.7 million had been disbursed to implement a variety of subprojects. A listing of the 19 grants to 11 PVOs in eight countries funded under this project is in Exhibit 2.

B. Audit Objectives and Scope

This audit of the South Pacific PVO Co-financing Project by the Office of the Regional Inspector General/Manila was primarily a program results audit. After a broad-based survey, the audit focused on the specific objectives of determining

-- if the PVOs' project activities met A.I.D.'s programming and management requirements;

-- the adequacy of PVO local office accounting systems; and

-- whether the U.S. was adequately recognized as the grantor.

To accomplish these objectives, RDO/SP and Controller/ Philippines internal controls were reviewed and tested by examining pertinent reports, files, and related documents. Selected PVOs' local office accounting systems were also reviewed to determine if they adequately accounted for A.I.D. funds. Interviews and discussions were conducted with RDO/SP project and management officials, grantee officials having project management responsibilities, beneficiaries, and Controller/Philippines personnel.

Site visits included the country offices and selected subprojects of five PVOs receiving eight grants in the countries of Fiji, Papua New Guinea, Solomon Islands, and Tonga. At the time of the review, these grants totalled $5.2 million of the $7.7 million expended by the project. The bases for the selection of PVOs for review were the dollar value of the grant, the time frame of the grant, and the location of project activities. A listing of the grants reviewed is in Exhibit 1.

There was an audit survey of the RDO/SP in 1982 to assess its financial and operational controls.1/ One of the activities reviewed was the predecessor project. Several areas were noted then where project management and monitoring could be improved. One recommendation was that the RDO establish procedures for ensuring that grantees carry out effective on-site project reviews and audits to ensure that project resources are properly used. While that recommendation had been closed, this audit found the problem still existed.

The audit was conducted from September 1986 to January 1987 and was made in accordance with generally accepted government auditing standards.

1/ Survey of A.I.D.'s South Pacific Operations, Memorandum Survey Report No. 2-498-82-06, March 1, 1982.

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PART II - RESULTS OF AUDIT

The audit showed that (1) small project activities funded by The Co-Financing Project were too technically varied and geographically dispersed to be managed economically and efficiently and generally could not demonstrate a development impact; (2) accounting and financial management systems at local offices of some grantees were inadequate; and (3) A.I.D. grant-assisted activities were not adequately identified as American aid.

A.I.D.'s 1987 Congressional Presentation states that the U.S. has important interests in the South Pacific, including ensuring that it has regional goodwill. A.I.D.'s objective in advancing these interests is to maintain a useful and meaningful presence in concert with the major donors, Australia, New Zealand, and Great Britain. The project paper indicates that providing assistance through voluntary agencies allows A.I.D. to achieve this objective with a minimum of direct-hire personnel. We determined that this objective was largely being achieved as grantees operating in the area were generally recognized as American organizations and had established linkages with host governments and local organizations. A number of project activities were functioning well and being implemented as planned.

The report presents three findings, i.e.: (1) most small project activities funded under the Co-Financing Project could not demonstrate a development impact and were uneconomical and inefficient to manage; (2) the financial management systems of six of the eight grantee field offices reviewed were deficient; and (3) grantees which received assistance under this project frequently did not inform subproject recipients that the funding was from A.I.D..

This report recommends that: 1) the project fund only activities that are concentrated technically or geographically and have a demonstrable economic development focus; 2) more specific guidance be provided to grantees as to A.I.D.'s financial management and audit requirements; 3) assistance be arranged for local offices of Private and Voluntary Organizations in establishing adequate accounting systems; and 4) more specific guidance be provided to PVOs as to marking of A.I.D.-funded commodities and recognition of A.I.D. funding of other activities.

A. Findings and Recommendations

1. Many Project Activities Lacked Focus and Impact and Were Inefficient

A.I.D.'s policy is to increase the economic development impact of voluntary agency programs, focus resource use, and utilize funds economically and efficiently. Most small project activities funded under the Co-Financing Project could not demonstrate a development impact and were uneconomical and inefficient to manage. This occurred because subprojects were too technically varied, geographically dispersed, and lacked a specific economic development focus. As a result, A.I.D. funds were expended uneconomically for subprojects that did not demonstrate a significant development impact.

Recommendation No. 1

We recommend that any new funding under the Private and Voluntary Organization project by the Regional Development Office for the South Pacific be only to activities that are concentrated technically or geographically and have a demonstrable economic development focus.

Discussion

A.I.D.'s policy paper on private and voluntary organizations (PVOs) indicates that A.I.D.'s broad objective is to increase the economic development impact of PVO programs through increased program integration and focusing resources on field programs. A.I.D. Handbook 19 requires that funds be used economically and efficiently and only for authorized purposes. Handbook 3 specifies that approved projects should represent the best alternative to the solution of a problem and that addressing the problem is necessary to fulfill development objectives.

Of the sample of eight grants to five PVOs reviewed under the Regional Development Office for the South Pacific (RDO/SP) PVO Co-financing Project, six involved providing sub-grants for small projects. While the specific objectives and methods of operation of these grants varied, they each provided funds for a variety of types of activities over a large geographic area. The review determined that these small project activities lacked a technical or geographic focus, were difficult and costly to manage, and could demonstrate very little actual development impact.

Small Project Grants Lacked Focus - Each of the six grants which supported small project activities accepted proposals from applicants on a nationwide basis and for a wide variety of project activities. Administration of the program was handled by the PVO at the country office or in some cases with a small field staff. Because of their geographic dispersion and small size, it was not possible for PVOs to oversee or check on project implementation on a regular basis and in many cases they did not even check on the activity before it was approved or determine the end result. For example, one PVO in Papua New Guinea approved 63 subprojects in one year with a planned expenditure of $377,000. While each subproject had a narrow focus, the diversity of activities precluded the project itself from having a focus. The following provides some examples of project activities:

Examples of Subproject Diversity in Papua New Guinea

Name of Subproject	Location	Funding
Buying Fund	Various/Morobe	$10,227
Outrigger Fishing Canoes	Various	9,755
Shoe Repair Business	Lae/Morobe	2,759
Women's Group Development	Various	10,795
Community Pit Latrines	Various	1,932
Health Publications	Various	19,250

This particular program was run by two Americans with extensive overseas experience, yet they had significant difficulty in overseeing project activities. They reported that it was very hard to get recipients of funds to provide adequate accounting and to determine the end result of many projects. A similar small project scheme funded by the Government of New Zealand and the European Economic Community was suspended because both donors were having difficulties in accounting for funds, beneficiaries were not reporting on how the grant funds were used, and an excessive administrative burden was placed on the staff.

In this case, even with a qualified staff and a major effort to review subprojects before funding and to follow their implementation, considerable management difficulties were experienced. An internal evaluation by the PVO of 41 subprojects illustrated the difficulties encountered, e.g.:

- Support for a rice growing project was dropped after the government expressed serious reservations about the commercial viability of rice growing.

- A chicken raising project did not result in success or replication because many chickens died, egg production was low, and reliance on imported feeds made it too expensive.

- Because of tribal fighting, construction of a drier was delayed indefinitely after materials were purchased and delivered.

- One year after purchase, a sawmill had not produced a single piece of sawn timber and the mill was later repossessed.

A.I.D. provided almost $150,000 to a local PVO in Fiji in 1985 to fund 39 small projects and administrative costs. Here again there were a wide variety of types of projects funded over a broad geographic area. The average cost of these projects was about $2,700 each. Some of the projects funded are listed below:

Examples of Subproject Diversity in Fiji

Name of Subproject	Location	A.I.D. Funding
Fish Pond	Kuku	$3,409
Carpentry Workshop	Narunaruku	1,919
Extension of Store	Lutu	2,856
Farming	Bethel Gospel	1,327
Men's Fishing	Veirapa	3,803

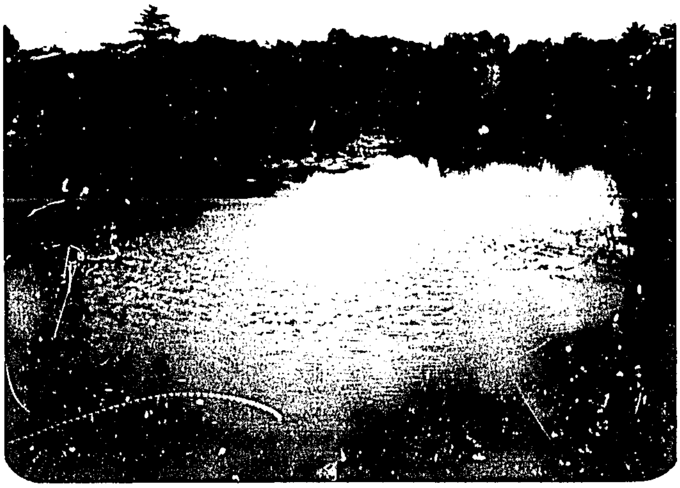
The Executive Director of the PVO admitted that they did not really know whether the projects were successfully implemented in most cases as they relied on the implementing agency which had applied for the grant to provide them information on projects. The grants were generally provided in cash and the recipient was requested to provide receipts of expenditures, but because of the wide geographic dispersion and the variety of sponsors, these were not always received. At the end of the year, the PVO had over $40,000 in grants outstanding that had not been accounted for.

The auditors visited six subprojects of the PVO during the audit and found two to be unsatisfactory and two others to have a questionable development impact, e.g.:

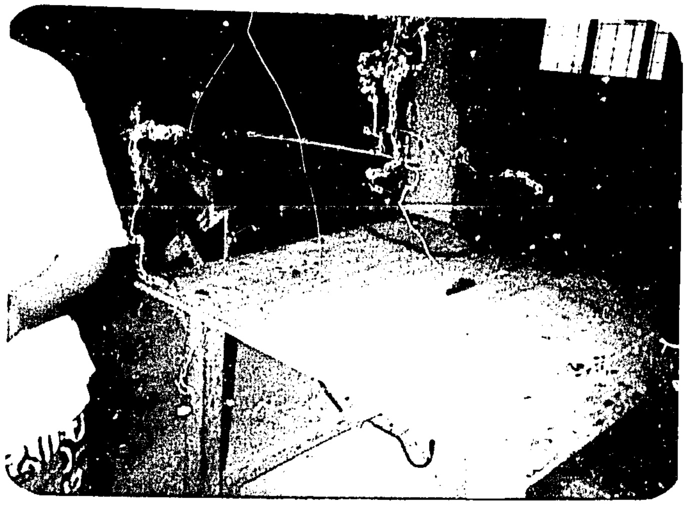
- A fish pond built with $3,409 of project funds was not producing fish at the time of the visit just over a year after it was built. Eels and ducks had eaten the fish. A letter in the project file at the PVO office from the government Senior Fisheries Officer advised that the project would prove to be not economically feasible, but the project was funded anyway.

- Over $3,000 was provided to build and equip a carpentry workshop. At the time of the visit, most of the equipment which had been purchased was missing and a village leader stated that the workshop was not being used because the youth were not interested in building things.

- About $1,400 was spent to build a cement stairway in a village. This did not appear to be a priority development-oriented activity.



Eels and ducks had eaten all the fish in this pond built with $3,409 in project funds.



Carpentry workshop built and equipped with $3,000 A.I.D. funds not being used and most equipment missing.

Stairway built with $1,400 in A.I.D. funds for village not a high development priority.

The Development Impact Was Questionable - A review of selected small project activities of the PVOs in the audit sample and many project evaluations that were conducted by the PVOs themselves or outside evaluators showed that in a significant percentage of cases, the projects were not implemented as planned. In other cases, though implemented, the project subsequently failed. And in almost all cases, while specific outputs may have occurred, little or no development impact could be demonstrated.

In the Solomon Islands, a PVO approved 186 projects in eight provinces and nationwide with a total value of $467,000 from July 1985 to June 1986. These projects were for a wide variety of purposes as shown in the following table.

Examples of Subproject Diversity in the Solomon Islands

Project Name	Location	A.I.D. Funding
Nutrition Workshop	Nationwide	$1,640
Youth Center Building	Ngongona	734
Copra Buying	Avuavu	8,140
Workboat	Papari	8,414
Women's Poultry	Oloburi	1,251

An internal evaluation by the PVO showed that many projects did not have a lasting impact on development, e.g.:

- A small project to start a village store did not succeed because of lack of community interest and the $490 spent was lost.

- A piggery funded for $918 was not succeeding because of lack of interest by the project leader and villagers. The materials supplied were lying idle and some funds advanced were used for other purposes.

- A water supply project for which $1,224 was spent to provide water to a new settlement had come to a standstill with no benefits.

In the sample of projects observed by the audit team, significant problems were observed in half, e.g.:

- The PVO had provided almost $28,000 to the Young Women's Christian Association to develop their program over several years, but at the time of our review there was no executive director and the record books could not be located. A training center built with project funds was unused.

- Video equipment provided to a Health Department at a cost of $9,000 to improve health education was largely unused for the intended purposes and most of it was in a storeroom.

In Fiji another PVO provided about $30,000 of A.I.D. funds to 33 small projects between January 1 and June 30, 1986. For example, these projects included those listed in the following table.

Examples of Other Subproject Diversity in Fiji

Subproject	Location	Cost
Gardening Tools and Seeds	Navatukia	$1,700
Maize Planting	Narata	473
Fish Drying	Beach-de-Mar	918
Nutrition Computer Program	N/A	1,066
Youth Council Workshop	Lomawiti	1,404

The auditors visited several projects funded by the PVO from A.I.D. grants. These included a community hall which was not in use, several kitchens at personal residences, some small plots of corn and broomstraw, and a fish-drying project. All of the small projects were managed by one local employee and the American supervisor had not visited any of them. For the small projects visited during the audit, no development impact could be determined nor could the PVO demonstrate any.

Administrative Costs Were High - The implementation on a nationwide basis of a program of small projects for a wide variety of purposes is costly to administer. Travel to outlying areas, especially in these island countries, is difficult, expensive, and time-consuming. Generally, project managers were dealing with inexperienced people and had to lead them through the process of applying for and implementing grants from project funds. It was very difficult to exercise technical and financial control over the projects. This resulted in administrative costs which were quite high in relation to actual program funds or benefits delivered to the recipients. For example, in the sample of six PVO country offices conducting small project activities, four had higher costs to administer the program than actual funds delivered to recipients, as demonstrated in the following chart.

Comparison of Administrative to Program Costs for Small Project Activities of Selected Private and Voluntary Organizations

PVO	Administrative Costs	%	Program Expenditures	%	Total
1.	$228,000	61	$145,000	39	$ 373,000
2.	126,000	52	118,000	48	244,000
3.	770,000	57	578,000	43	1,348,000
4.	610,000	55	498,000	45	1,108,000
5.	227,000	42	316,000	58	543,000
6.	43,000	15	245,000	85	288,000

Because the RDO/SP is responsible for programs in 10 South Pacific countries, management and evaluation of these widely dispersed country grant programs was largely the responsibility of the PVOs themselves. The RDO/SP Project Officer responsible for this project also has other major duties and can spend only about half his time on overseeing this widely dispersed project.

The RDO/SP has been aware for some time of the problems of managing PVO projects of this nature and their high relative administrative costs and has gradually reduced the percentage of PVO funding in its total program.

An evaluation conducted in 1982 by A.I.D. of the prior similar project recommended that the program concentrate on moving from outputs to achievement of project purpose and that grants include baseline data, specific purposes, and evaluation plans. This had not been done in the programs observed by the auditors. The auditors believe this was because the subprojects were so widely dispersed geographically, so small in size, and had such diverse objectives that it was not feasible.

While the auditors agreed that the PVO program is addressing an important need and should be retained, A.I.D.'s policy of achieving economic development impact and focusing resources was not being complied with. Considering the limited funds available and the great geographic dispersal, the program was not focusing on achieving economic development of the recipients, and the funding of such small projects was not efficient and economical.

RDO/SP should ensure that future grants are focused on specific economic development activities or on a designated manageable geographic area. The criteria for funding grants to PVOs should be modified to exclude small project activities which are widely dispersed geographically and lack a specific economic development focus. Funding preference should be given to projects that can be efficiently and economically managed.

The auditors discussed the desirability of limiting the geographic coverage or technical scope of these small grant programs with four PVO country directors. Three agreed that this change would be desirable as it would reduce overhead costs, improve management, and assist in demonstrating development impact. The fourth objected to limiting his country program because of political reasons.

Management Comments

RDO/SP comments on the draft report indicated an understanding of the audit's concerns regarding geographic concentration and functional (technical) focus but neither agreed nor disagreed with the recommendation. The comments address a number of concerns and broader issues, e.g., A.I.D. has a mandate to cooperate with PVOs in development, and consideration should be given to the costs of delivering other types of assistance such as central PVO programs or government-to-government programs. They reiterate the need to stretch the American presence in a region of 10 independent countries spread over 5.6 million square miles with only four A.I.D. officers.

IG/Comments

We do not take issue with the RDO/SP comments. However, while the broader issues may be worth future inquiry, we believe the issue presented in this report should be addressed now. This report does not advocate the reduction of funds provided for the PVO Co-Financing program, only that these funds be better used to achieve A.I.D.'s development objectives. The project could be significantly improved if grants were focused on specific areas or activities so that baseline data could be collected, clear purposes established, and accomplishments measured. In this way the grants could be managed better and would have a greater chance of achieving verifiable development objectives. This would strengthen, not weaken the PVO Co-Financing activity and place the grantees in a significantly better position to demonstrate the effectiveness of their programs in achieving A.I.D.'s development and other objectives in the South Pacific.

2. <u>Some Private and Voluntary Organization Accounting Systems Were Inadequate</u>

A.I.D. regulations specify criteria as to the financial management systems of grantees and that the Mission Controller determine whether the systems are adequate. The financial management systems of six of the eight grantee field offices reviewed were deficient. These deficiencies resulted from inadequate guidance to the private and voluntary organization (PVO) field offices as to A.I.D.'s financial management requirements, the lack of audits at these offices, and failure of the Controller, USAID/Philippines, the responsible Controller, to ensure that these local offices had adequate accounting systems. As a result, expenditures were made for unauthorized purposes and A.I.D. could not be assured that funds were used properly and only for authorized purposes.

<u>Recommendation No. 2</u>

We recommend that the Regional Development Office for the South Pacific:

a. provide specific guidance to grantees as to A.I.D.'s financial management requirements and

b. require audits of local offices of grantees every two years.

<u>Recommendation No. 3</u>

We recommend that the Controller/Philippines arrange for assistance to local offices of private and voluntary organizations in establishing adequate accounting systems.

<u>Discussion</u>

A.I.D. Handbook 3 requires that grantees maintain books and records in accordance with generally accepted accounting principles and practices. It also requires that grantees' books and records be audited regularly in accordance with generally accepted auditing standards. A.I.D. Handbook 13 requires that the grantee's financial management system shall provide for:

a. accurate, current, and complete disclosure for each A.I.D.-sponsored project or program;

b. effective control over and accountability for all funds, property, and other assets; and

c. accounting records that are supported by documentation that at a minimum will identify, segregate, accumulate, and record all costs incurred under a grant.

Further, A.I.D. Handbook 19, Chapter [illegible], requires that the Mission Controller review or arrange for reviews of borrower/grantee accounting records as necessary to determine whether they are adequate to ensure and disclose compliance with all conditions in the agreement concerning systems of accounts and related reporting.

The accounting systems used at the eight field offices of the PVOs in the audit sample were reviewed to determine whether they met the above criteria. While results varied, all but two were deficient to some degree. One PVO local office had no accounting system at some point during the grant period. Five PVO local office accounting systems could not adequately identify and segregate A.I.D. costs incurred under the grant. Four grantees also had no control or accountability over property purchased with A.I.D. funds.

The grant agreements made by South Pacific Regional Development Office (RDO/SP) included the standard provisions for such grants specified in A.I.D. Handbook 13, including the one for accounting, which specifies "With respect to accounting, records and audit, the Grantee shall comply with the requirements set forth in paragraphs 1I, 1J, 1L and 1M of Handbook 13". No local grantee office had these A.I.D. handbook provisions available. It is the detailed requirements the grantees need and they should be provided with copies of the A.I.D. Handbook 13 sections referred to.

The grants to U.S.-based PVOs were made to their headquarters offices which received funds from A.I.D./Washington for grant expenditures. The audit did not review these PVO headquarters offices and could not fully determine the basis for their claims. However, it is clear that they must rely on the inputs from the field offices to determine most of the expenditures to claim from A.I.D. under the grants. If the local accounting system was not adequate to identify and segregate expenditures to be claimed from A.I.D. under the grant, neither the headquarters offices nor A.I.D. could be sure the claims were correct.

The PVO Co-Financing grants usually specified that the PVO would provide some funding for the project from its own resources. The PVO headquarters provided a monthly advance to its local office, but in most cases did not specify whether these funds were from the A.I.D. grant or from its own resources. However, based on the A.I.D. grant budget amounts and actual funds received from the PVO headquarters by the local offices, these offices generally concluded that the funds provided to them were all A.I.D. funds. Even where PVO financial inputs were specified in the grant, these were not generally provided to the field offices. They may have been applied against headquarters expenses related to that project, but this could not be determined.

In most cases the headquarters office of the PVO did not provide the local office with information on headquarters expenditures under the grant. Sometimes these expenses were charged against amounts previously budgeted for the field office. Thus the field office could not exercise adequate control over its budget and could not be sure what funds were still available for the project.

The only local offices with accounting systems considered adequate were the two International Human Assistance Programs (IHAP) offices. IHAP has a policy requiring audits of their local offices every two years or when a director leaves. One of these offices had been audited twice by a qualified CPA firm and the other once. The auditors made suggestions for improving the accounting systems which were made. The systems benefited from these audits and A.I.D. and the PVO were provided some assurance that funds were properly controlled and used for grant purposes. None of the other U.S.-based PVO local offices had been audited. The indigenous PVO in Fiji had no real accounting system until it was audited in 1985. It subsequently instituted an accounting system, but there were still important financial management difficulties, e.g., funds advanced to subprojects were not always accounted for by proper receipts and costs that were supposed to be paid by the sponsoring group were charged to the grant.

In another case, the lack of an accounting system at the local office of a PVO made it impossible to determine the amounts expended under the grant for project purposes. From receipts retained at the office, however, it could be ascertained that A.I.D. had been billed for three trucks and other equipment that should not have been purchased under the grant. A.I.D. also was billed by the PVO for construction materials provided to a school that had not been approved as a grant recipient. The RDO/SP agreed to take action to correct these specific problems, but the system deficiencies causing them should also be addressed.

Therefore, the controls over A.I.D. grant funds in most PVO local offices were inadequate and did not meet A.I.D. regulatory requirements. This condition resulted from a number of factors, including failure to inform the local offices of the A.I.D. financial management requirements referred to in the grant agreements, the small size and lack of accounting expertise of local PVO offices which made it difficult for them to establish adequate accounting systems, and the failure of some PVOs to require audits of local offices. As a result, A.I.D. could not be sure funds charged were in accordance with law, policy, and grant requirements.

USAID/Philippines, encountering a similar problem in managing its PVO Co-Financing program, hired a local management firm to systematically review PVO accounting systems and upgrade those systems to meet Agency standards. Funds were provided through the Co-Financing budget. Managers at the Mission stated that such action greatly improved the accounting practices of participating PVOs.

The PVO accounting systems can be corrected if the RDO/SP provides more specific guidance in grant agreements as to A.I.D.'s financial management requirements and requires audits of local PVO offices every two years. The Controller, Philippines, who provides financial management services to RDO/SP, should also arrange for assistance to these local PVO offices to establish adequate accounting systems.

Management Comments

RDO/SP generally agreed with the recommendations, but felt that A.I.D. Handbook 13, Chapter 4 guidance for grants could be strengthened and PVOs should integrate financial control requirements into their internal management systems. The response also encouraged more tying together of PVO home office and local office audits.

The Controller, USAID/Philippines, agreed to the recommendation addressed to him and has initiated action to provide the accounting assistance required.

3. A.I.D. Recognition As Grantor Could Be Improved

A.I.D. is required by law to ensure that its programs are identified overseas as "American Aid". Grantees which received assistance under this project frequently did not inform subproject recipients that the funding was from A.I.D.. This condition resulted from the lack of guidance to A.I.D. offices and private and voluntary organizations (PVOs) generally as to requirements for marking and other recognition of A.I.D.-funded activities under grantee management. It also resulted from inadequate specific guidance to the PVOs reviewed. As a result, recipients frequently did not know that they were receiving assistance provided by the U.S. Government and the intent of the law was not complied with.

Recommendation No. 4

We recommend that the Regional Development Office for the South Pacific provide more specific guidance to grantees as to marking of A.I.D.-funded commodities and structures and recognition of A.I.D. funding in other ways.

Discussion

Section 641 of the Foreign Assistance Act requires that all programs carried out under the Act be identified overseas as "American Aid". The purpose of the requirement was to ensure an awareness of beneficiaries and the public of the recipient country that the resources were donated by the people of the United States.

Except for local inputs, usually labor and local materials, the PVO activities under the grants reviewed were funded almost completely by A.I.D.. In the countries where most of these PVOs operated, there were no bi-lateral direct A.I.D. programs. Therefore, the PVO activities were usually the only evidence of U.S. assistance to these small countries except for the Peace Corps.

Generally the PVOs reviewed did not make a significant effort to ensure that A.I.D. or the U.S. Government were credited with providing the assistance they administered. The PVOs generally made sure that the PVO itself was credited, thus to some extent identifying the assistance with the United States.

The older grant agreements did not contain any provision requiring marking of A.I.D.-provided equipment or buildings funded by A.I.D. and referred only to the standard grant provisions which did not contain marking or publicity requirements. In an effort to comply with A.I.D. policy and ensure recognition of the U.S. contribution to the countries benefitting from these grants, starting in 1984 the South Pacific Regional Development Office (RDO/SP) inserted a special provision into their grant agreements which specified:

"Marking Requirements. It is A.I.D. policy that projects and imported commodities financed under A.I.D.-supported programs be suitably marked to identify them as supported by U.S. foreign assistance. Grantee agrees to suitably mark appropriate activities and items supported by A.I.D. under this grant."

The PVO country directors in most cases stated that they have been exhorted by the RDO/SP Director to ensure that A.I.D.-supported activities and commodities were marked. However, eight site visits made during the audit showed no A.I.D. markings on five of seven project-funded structures, such as community centers and training facilities, and marking of project-funded commodities was spotty. PVO personnel stated that they were unsure as to what types of things to mark and what types of markings to use. However, the RDO/SP stated that they have held four A.I.D./PVO planning and evaluation conferences at which "A.I.D. Recognition" was a theme.

This school was supported and the trucks funded by A.I.D. but there were no A.I.D. markings at the project

Some PVOs on occasion did attempt to give the U.S. Government credit in press releases and ceremonies dedicating projects or activities, but there is no specific guidance on this and performance varied widely.

In interviews with about 20 actual project recipients, only two were aware that the assistance they received was provided by the U.S. Government. Most attributed the assistance to the PVO itself. At two of the PVOs funded almost exclusively by the A.I.D. grant, no A.I.D. emblems or other U.S. markings were seen by the auditors. At others, the were used irregularly.

A.I.D. has extensive criteria as to marking of commodities funded by its regular programs. However, no specific guidance was found in A.I.D. handbooks as to marking requirements for commodities used in PVO projects funded largely or completely by A.I.D.. Also, no specific guidance was identified for ensuring that A.I.D.-funded activities other than commodities be given appropriate recognition. This lack of guidance by A.I.D. leaves missions and PVOs unsure of what to do and results in a lack of recognition by beneficiaries of U.S.-funded programs of the source of the funds. Therefore, the intent of the requirement in the Foreign Assistance Act that all programs carried out under the Act be identified overseas as "American Aid" was not complied with.

The grant provision on A.I.D. marking inserted by RDO/SP into newer grants is commendable, but too vague. More specific criteria as to marking structures and project commodities and giving recognition to A.I.D. in press releases and other means should be provided to PVOs.

Management Comments

The RDO/SP agreed with the spirit of this finding and had recommended that marking requirements be a part of the revisions to A.I.D./PVO collaboration guidelines being coordinated by the Office of Private and Voluntary Cooperation in A.I.D./Washington for inclusion into Chapter 4 of A.I.D. Handbook 3. Or, they suggest, more specific language should be included in Handbook 1 procurement guidance.

B. Compliance and Internal Control

Compliance

Management's system for ensuring compliance with laws and A.I.D. regulations and actual compliance at the locations visited were tested. Except as noted in this report, compliance was adequate for those items tested. The audit did determine that compliance with A.I.D. financial management requirements by some private and voluntary organizations (PVOs) local offices was inadequate and that PVOs did not adequately comply with the legal requirement to identify A.I.D. grant-assisted activities as American aid. Nothing came to the auditors' attention that would indicate that untested items were not in compliance.

Internal Control

The internal controls over financial activities and projects of the local offices of PVOs in the audit sample were examined. The controls over A.I.D. funds at South Pacific Regional Development Office (RDO/SP) and the Controller/Philippines were also examined. However, the headquarters offices of the PVOs were not examined. The audit determined that the financial management systems of six of the eight grantee field offices reviewed were deficient. As a result, expenditures were made for unauthorized purposes and A.I.D. could not be assured that funds were used properly and only for authorized purposes.

AUDIT OF
THE SOUTH PACIFIC
PRIVATE AND VOLUNTARY ORGANIZATION
CO-FINANCING PROJECT

PART III - EXHIBITS AND APPENDICES

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EXHIBIT 1

PRIVATE AND VOLUNTARY ORGANIZATION
CO-FINANCING PROJECT 879-0001
GRANTS REVIEWED

Name	Location	Grant Number	Amount Obligated	Amount Expended
International Human Assistance Program	PNG *	4010	$ 632,850	$ 543,191
International Human Assistance Program	SI **	1653	561,702	520,276
The Foundation for the People of the South Pacific	Fiji	4008	1,956,485	1,524,604
The Foundation for the People of the South Pacific	Tonga	4007	868,956	656,737
The Foundation for the People of the South Pacific	SI **	1650	569,010	569,010
Agricultural Cooperative Development International	Tonga	1013	592,505	338,608
Salesian Society, Inc.	PNG *	5009	1,093,429	350,000
Fiji Council of Social Services	Fiji	4004	678,039	653,613
TOTAL			$6,952,976	$5,156,039

* Papua New Guinea

** Solomon Islands

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EXHIBIT 2

PRIVATE AND VOLUNTARY ORGANIZATIONS
CO-FINANCING PROJECT 879-0001
LISTING OF GRANTS

Grantee	Number	Obligated	Expended
The Asia Foundation	1003	$ 17,680	$ 17,680
	4013	32,000	28,880
	4014	96,518	91,201
The Foundation for the People of the South Pacific	1005	78,937	78,937
	1012	30,000	30,000
	1323	28,620	28,620
	1650	569,010	569,010
	1726	190,000	190,000
	3016	75,335	75,335
	4007	868,956	656,737
	4008	1,956,485	1,524,604
	4009	626,704	530,021
	4011	550,916	524,800
Agriculture Cooperative Development Int'l	1013	592,505	338,608
International Human Assistance Program	1653	561,702	520,276
	4006	465,000	225,691
	4010	632,850	543,191
	6019	150,000	-0-
Fiji Council of Social Services	3026	29,860	29,860
	4004	678,039	653,613
Young Men Christian Association	1605	16,500	-0-
Helen Keller International	4001	296,857	271,337
	6012	200,000	-0-
Catholic Relief Services	4005	193,586	143,586
	5006	125,797	125,797
Save the Children Federation	1654	66,872	-0-
	5005	320,820	123,322
Salesian Society, Inc.	5009	1,093,429	350,000
South Pacific Family Health	6026	446,000	-0-
Total	29	$10,990,978	$ 7,671,106

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OPTIONAL FORM NO. 10
MAY 1962 EDITION
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5010-104

UNITED STATES GOVERNMENT

Memorandum

TO : Mr. Leo L. LaMotte, RIG/A/M DATE: May 8, 1987

FROM : Loc Eckersley, Controller

SUBJECT: Draft Audit Report on the PVO Co-Financing Project (Project No. 879-0001)

Thank you for the opportunity to comment on the subject draft report.

Finding No. 2 "Some PVO's Accounting Procedures Were Inadequate" is directly related to our area of responsibility, and our comments are limited to that section. Recommendation No. 3 recommends that the Controller/Philippines arrange for assistance to local offices of PVOs in establishing adequate accounting systems. We agree that there is an obvious need for the PVOs in the South Pacific to establish adequate accounting systems. We have discussed this need and ways of meeting it with Mr. Paupe the Director, South Pacific Regional Development Office (SPRDO).

We recommended that the SPRDO consider hiring the local management firm used by USAID/Philippines to assist its PVOs in upgrading their budgeting, accounting, and financial reporting systems. Mr. Paupe agreed with our recommendation and we are sending him copies of our contract covering those services, and sample manuals prepared by our contractor for use by a Grantee and Sub-grantee. Please be assured that we will provide the SPRDO whatever assistance is necessary to get a contract signed. For your information, it is our understanding that the SPRDO will most likely be getting its own Controller in the near future. Significant increases in the SPRDO's program is making this change necessary.

We would like to suggest an editorial change on page 23, third paragraph, second sentence of the draft. This sentence should read: "The Controller, Philippines, who provides financial management services to the RDO/SP,***." We would also like to point out that any future correspondence dealing with this office's responsibilities to the SPRDO should be directed to me. For your information, Mr. Schieck, the USAID/Philippine Mission Director, does not have any responsibility for SPRDO activities.

cc: Mr. William Paupe, Director, SPRDO

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UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT

South Pacific Regional Development Office

American Embassy
P.O. Box 218
Suva, Fiji.

JUNE 01, 1987

TO: Mr. Leo L. LaMotte, RIG/A/Manila

FROM: William E. Paupe, Regional Director, USAID/RDO/SP

SUBJECT: Draft Audit Report on the PVO Co-Financing Project (Project No. 879-0001)

The RDO/South Pacific appreciates the opportunity to comment on the subject draft audit report. As preface to those comments, we wish to acknowledge the draft report's statement on page 4, namely, that the U.S. has important interests in the South Pacific; that AID's objective in financing these interests is to maintain a useful and meaningful presence in concert with the major donors; that providing assistance through voluntary agencies allows AID to achieve this objective with a minimum of direct hire personnel; that this objective is largely being achieved; and that many project activities are functioning well and being implemented as planned.

Our comments on the draft audit report are divided into four sections corresponding to the recommendations of the draft audit report, and the concluding section on compliance and control.

I. Recommendation No. 1: Focus, Impact and Efficiency of Programs

USAID understands the issues and concerns expressed by the draft audit report regarding geographical concentration and functional focus of PVO programs. As the audit's findings are presented, however, USAID wishes to reiterate the following points for considering the issues and concerns in a broader context:

1) Emphasis on income generating projects, in a variety of programs, has been an objective of the "phase II" PVO Co-Financing project (i.e. the current project No. 879-0001 which began in FY 1984). The more recent project has attempted to focus PVO programs by emphasizing an income generating theme in small projects assistance.

2) Reductions in RDO/SP funding to PVO programs indeed reflect some agreement with the draft audit report findings. However, it also most certainly reflects AID/W reductions in DA funding at the same time RDO/SP's program has been addressing AID/W directives for Mission responsiveness to other AID priority areas, e.g. training and private enterprise development. With maintained or modestly increasing levels of DA funding, RDO/SP would sustain a more substantive PVO program, albeit as a smaller percentage of the total RDO/SP portfolio.

3) The draft audit report states that "generally project managers were dealing with inexperienced people and had to lead them through the process of applying for and implementing grants from project funds. It was very difficult to exercise technical and financial control over the projects" (p.14). This is precisely AID's mission, in part, i.e. to directly assist in meeting basic human needs of rural beneficiaries; the control issue is the dilemma and challenge of any USAID Mission (especially one whose area is as widely disbursed as that of the RDO/SP). Delivering economic assistance to needy populations by its very nature is often labor intensive and time consuming, and therefore costly. That's part of AID's and RDO/SP's commitment to development assistance.

4) AID's "legislative mandate" directs USAID to actively collaborate with PVO's in development. This collaboration has its costs, as well as benefits. While always striving for greater economic development impact and efficiency in delivery, AID needs to objectively identify and accept these costs if it and PVO's are to maintain some measure of collaboration.

5) The draft audit report states that it would be "interesting" to compare the costs of delivering economic assistance via G-to-G programs or via centrally funded PVO programs, with the costs of delivering them via USAID-funded, in-country PVO programs. However, the report states further that the efficiency of USAID-funded PVO programs should be considered on its own merits without comparison. USAID/RDO/SP suggests that the mode of delivery is indeed an integral part of the efficiency question, and should be considered:

a) The implication is that larger, usually meant to mean "government", programs are more cost-efficient in delivering aid assistance. Is that so? The costs of administering small project assistance in PVO programs should be compared with hard data detailing the costs of delivering small project assistance in G-to-G programs.

b) "PVO Co-Financing" within AID has come to mean "USAID's working with PVO's in the field". The draft audit report discusses this relationship. Another relationship, of course, exists between AID/W (FVA/PVC) and the PVO's. Any discussion of the efficiency of a USAID's PVO Co-Financing program should also factor in the lessons learned and cost/impact ratios of centrally funded PVO programs. Given AID's legislative mandate to collaborate with

PVO's in development, perhaps centrally funded PVO programs (e.g. Matching Grants) could more effectively and efficiently deliver economic assistance to needy populations. Should the AID/W Matching Grant mechanism replace the USAID "Co-Fi" mechanism? RIG/A should investigate this possibility.

6) In the South Pacific, AID assistance to PVO's (and other small project programs) has also been motivated by the desire to stretch the American presence in a region of ten independent countries spread over 5.6 million square miles with only four USDH AID officers. The costs of working with up to ten PVO's and 25 on-going PVO programs to effect the U.S. presence objective needs also to be seen in this light and compared to the costs of delivering more U.S. presence in other ways. Of course, how effectively the U.S. presence and recognition of USG assistance are actually being accomplished by PVO's is another and important issue discussed in other sections of the draft audit report. Nevertheless, this broader purpose needs to be considered when discussing how "costly" it is to collaborate with PVO's in the Pacific region.

II. Recommendation No.'s 02 and 03: PVO Financial Management Requirements and Establishing Adequate Accounting Systems:

USAID/RDO/SP generally agrees with the spirit and recommendations of this section. However, we wish to make the following comment:

1) Chapter 4 appendixes in AID Handbook 13 provide the form and substance for specific support grants to PVO's. The Grant Agreement format and standard provisions for PVO grants include specific instruction on financial reporting, allowable costs, title to and management of property, auditing, etc. These are all included in RDO/SP grants to PVO's. If this Handbook 13 form and substance is not judged to be adequate, perhaps RIG/A should make recommendations to M/FM for Handbook revisions. We suggest that the current Handbook 13 form and substance format for PVO grants provide the guidance needed. Nevertheless, RDO/SP is willing to consider incorporating "more specific guidance" in grant Attachment 1 ("Program Description and Schedule"). USAID can provide copies of Handbook 13 sections 1I, 1J, 1L and 1M with grant signing, but suggests it is more appropriate for PVO's to incorporate the substence of these sections into their own management manuals and integrate the requirements into their internal management systems.

2) RDO/SP agrees that local PVO offices should be audited every two years, but would also encourage more tying together of home-office and local-office audits, which now seem to take place almost independent of each other under differing time schedules.

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3) RDO/SP agrees that assistance should be arranged to help PVO local offices to establish or upgrade adequate accounting systems. However, this initiative should be the primary responsibility of PVO's concerned with their own systems; RDO/SP and USAID/Controller/Philippines would assist that initiative.

III. Recommendation No. 04: AID Recognition as Grantor:

USAID/RDO/SP generally agrees with the spirit and recommendation of this section. However, the language for RDO/SP's marking requirements special provision (quoted on page 26 of the draft audit report) was drawn from the procurement language in AID Handbook 1. Perhaps more specific language on marking requirements should be contained therein.

IV. Compliance and Internal Control

The discussion in this section of the draft audit report accurately reflects USAID/RDO/SP views. More detail on those views, as well as more detailed USAID views on other sections of the audit, are contained in USAID's December 12, 1986 memorandum to Mr. Aubrey Mills entitled "Record of Audit Findings (RAFs) re: Audit of PVO Co-Financing Project".

APPENDIX 2

List of Recommendations

	Page
Recommendation No. 1	4

We recommend that any new funding under the Private and Voluntary Organization Project by the Regional Development Office for the South Pacific be only to activities that are concentrated technically or geographically and have a demonstrable economic development focus.

Recommendation No. 2	12

We recommend that the Regional Development Office for the South Pacific:

a. provide specific guidance to grantees as to A.I.D.'s financial management requirements and

b. require audits of local offices of grantees every two years.

Recommendation No. 3	12

We recommend that the Controller/Philippines arrange for assistance to local offices of Private and Voluntary Organizations in establishing adequate accounting systems.

Recommendation No. 4	16

We recommend that the Regional Development Office for the South Pacific provide more specific guidance to grantees as to marking of A.I.D. funded commodities and structures and recognition of A.I.D. funding in other ways.

APPENDIX 3

Report Distribution

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