PD-AA[illegible]-107

AN: 5[illegible]0

5190327

5700203

5190265

519[illegible]

5190287

5190216

5190336

AUDIT OF
SALVADORAN FOUNDATION FOR ECONOMIC
AND SOCIAL DEVELOPMENT

Audit Report No. 1-519-88-11
January 25, 1988

U.S. MAILING ADDRESS:
RIG/T
APO MIAMI 34022

AGENCY FOR INTERNATIONAL DEVELOPMENT

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

TELEPHONES:
32-9987
also 32-3120 EXT. 2701-2703

January 25, 1988

MEMORANDUM

TO: D/USAID/El Salvador, Henry H. Bassford

Coinage N. Gothard

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

SUBJECT: Audit of Salvadoran Foundation for Economic and Social Development

The Office of the Regional Inspector General for Audit/Tegucigalpa has completed its audit of the Salvadoran Foundation for Economic and Social Development.

The draft audit report was submitted to you for comment and your comments are attached to the report. The report contains four recommendations. Recommendation Nos. 2, 3 and 4 are considered resolved and may be closed upon completion of planned or promised actions. Recommendation No. 1 is unresolved. Please advise me within 30 days of any additional actions taken to implement Recommendations 2, 3 and 4, and further information you might want us to consider on Recommendation No. 1.

I appreciate the cooperation and courtesy extended to my staff during the audit.

EXECUTIVE SUMMARY

The Salvadoran Foundation for Economic and Social Development was created in 1983 by a group of about 100 Salvadoran business leaders as a private Salvadoran "think tank". The organization was established to develop alternative solutions to governmental intervention in response to El Salvador's economic, political and social problems. It was legally established in August 1983 as a private non-profit organization and has received A.I.D. assistance since late 1983. As of September 30, 1987, USAID El Salvador had authorized approximately $75 million for the Foundation's establishment and for the A.I.D.-approved activities that it administers. Of this amount $61.5 million had been obligated; accrued and actual expenditures amounted to $10.5 million. Nearly all of these funds have been authorized under seven cooperative agreements, as amended, during the period September 1984 to October 1987. Besides financing the Foundation's direct operations, funds authorized by these agreements financed the activities under the Foundation's eight programs.

At the request of USAID/El Salvador, the Inspector General for Audit/Tegucigalpa, Honduras conducted a program results audit of the Salvadoran Foundation for Economic and Social Development during the period July 13, 1987 to October 15, 1987. Specifically, the audit objectives were to determine if: (1) A.I.D. funded activities were achieving their planned objectives, (2) A.I.D. funds were adequately accounted for, and (3) project activities were being implemented in compliance with A.I.D. regulations and project agreements.

The audit showed that (1) four of the eight A.I.D.-funded Foundation programs were behind schedule because of implementation delays and their impact on achieving overall program objectives was uncertain; (2) the Foundation had adequate financial controls and accounting systems over A.I.D. funds; and (3) some A.I.D.-funded activities were not in compliance with A.I.D. regulations or project agreements.

Nevertheless, the audit found that the Foundation, during its brief three-year existence, had developed into a responsive organization with highly capable and dedicated management staff; contributed to strengthening private sector business associations; increased the Government of El Salvador's awareness of alternatives to its economic policies; stimulated interest and investment in non-traditional products; and provided financial and technical assistance to businesses and entrepreneurs which might not otherwise have been provided.

Specific problems observed included: required contributions from program beneficiaries not always being used for project purposes or in accordance with A.I.D. allowable cost provisions; the Foundation not actively seeking increases in contributions from project beneficiaries; the actual impact of project accomplishments being uncertain; and program activities not being independently evaluated to assess their cost effectiveness.

The audit findings were not totally unexpected given the Foundation's rapid organizational growth, its initial unfamiliarity with A.I.D.

requirements and procedures, the country's civil conflict, the destructive 1986 earthquake, and other obstacles impeding private sector development.

There was no assurance that required contributions from project beneficiaries were being used for project purposes or in accordance with the allowable costs which were stated by the standard provisions of the cooperative agreements between A.I.D. and the Foundation. Certain of the A.I.D.-funded programs required that recipients of A.I.D. financial assistance contribute a minimum of 25 percent of the total costs of the proposed activity to the Salvadoran Foundation for Economic and Social Development. These programs, however, do not specify how these funds are to be used. The Foundation considered these contributions to be their "own" funds and had commingled them with the other non-A.I.D. donations that it had received. However, since these "donations" were directly linked and prerequisite to receiving A.I.D. funding, their use, in our opinion, should be restricted for project purposes and subject to A.I.D.'s standard rules on allowable expenditures as stated in the cooperative agreements. Restricting the use of these mandatory contributions in this manner would result in less direct A.I.D. funds being required for project purposes. This could be substantial. The Foundation has estimated it would generate nearly $7 million by 1992 from mandatory contributions. The report recommends that USAID/El Salvador either obtain a Foundation agreement to restrict the use of these contributions for project purposes or obtain a formal legal opinion why the use of these monies should not be restricted.

The Mission stated it believed that mandatory contributions should be used in a manner consistent with the overall goals and objectives of the Foundation. However, it did not believe it was in A.I.D.'s interest to restrict the contributions to specific projects or programs. The Inspector General's Office maintained that mandatory contributions from A.I.D.-financed projects should be used for activities consistent with A.I.D.-funded project purposes and A.I.D.'s standard rules on allowable expenditures. The full text of the Mission's comments is attached as Appendix 1.

The Salvadoran Foundation for Economic and Social Development had not always encouraged program beneficiaries to share in activity costs beyond the minimum 25 percent required under certain of the A.I.D.-funded programs. Implicit in the cooperative agreements, just as in the Foreign Assistance Act requirement on counterpart contributions, is the intent that project beneficiaries be encouraged to contribute as much as possible toward the cost of activities from which they benefit. The Foundation had not established a policy or any criteria designed to maximize the amount of contributions from project beneficiaries. As a result, the potential income from this source was greatly reduced, causing greater reliance on A.I.D. resources. This report recommends that the Foundation establish a more aggressive policy on obtaining contributions.

The Mission agreed and had encouraged the Foundation to pursue a more aggressive contribution policy. The recommendation can be closed upon receipt of written evidence that the Foundation has established such a policy.

The actual effect of project activities on generating jobs, foreign exchange and other accomplishments was uncertain. The audit found that reported jobs, foreign exchange and other accomplishments generated by two of the eight programs were not properly classified or accurately reported. In addition, the audit found that important program accomplishment data may have been improperly erased from computer memory by the program contract manager. A.I.D. Handbook guidance requires that Missions establish monitoring and evaluation information systems to accurately measure the effect of project activities. Neither USAID/El Salvador nor the Salvadoran Foundation for Economic and Social Development had established adequate criteria or a system for measuring project accomplishments. As a result, one could not accurately assess the cost benefits or impact of project activities. The report recommends that the Mission and the Foundation establish uniform criteria and a system for measuring and reporting project accomplishments. The Mission agreed there was a need to establish uniform criteria and a system for measuring and reporting project accomplishments. The recommendations can be closed upon evidence that such criteria and system have been established.

None of the A.I.D.-funded activities administered by the Salvadoran Foundation for Economic and Social Development had been independently evaulated to determine its impact on achieving planned objectives or its cost-effectiveness. As provided by A.I.D. Handbook 3, Chapter 12, independent evaluations are necessary to make objective and rational decisions about projects. Several cooperative agreements also required that evaluations be performed prior to the time of our audit. Evaluations had not been previously scheduled because, according to the Mission, it did not want to also burden the Foundation by having an evaluation performed simultaneously with the Inspector General's audit, which was expected earlier, and also because of the major earthquake in October 1986, which interrupted both the Foundation's and the Mission's operations for an extended period. As a result of not performing independent evaluations, the Mission had less reliable information to judge the performance of project activities and to determine if they were cost-effective. The report recommends that the Mission establish a plan and timetable to evaluate program activities. The Mission agreed that evaluations were needed and had started the process to evaluate some of the Foundation's programs. The recommendation can be closed upon evidence that an evaluation plan and timetable to evaluate the Foundation's programs has been established.

Office of the Inspector General

AUDIT OF
SALVADORAN FOUNDATION FOR ECONOMIC
AND SOCIAL DEVELOPMENT

TABLE OF CONTENTS

AUDIT OF
SALVADORAN FOUNDATION FOR ECONOMIC
AND SOCIAL DEVELOPMENT

PART I - INTRODUCTION

A. Background

El Salvador's economy has declined during the past decade as a result of civil unrest and depressed international prices for agricultural commodities. During the period 1960 to 1978, El Salvador's Gross Domestic Product expanded by an average of 5.4 percent per year, primarily as a result of new investment and exports of major traditional agricultural products - coffee, cotton and sugar. After 1978, however, the worldwide recession reduced international prices for agricultural commodities and the growing civil conflict resulted in the destruction of crops and infrastructure. From 1978 to 1983, El Salvador's per capita Gross Domestic Product and exports both decreased by approximately 35 percent, while unemployment and underemployment rose to nearly 40 percent.

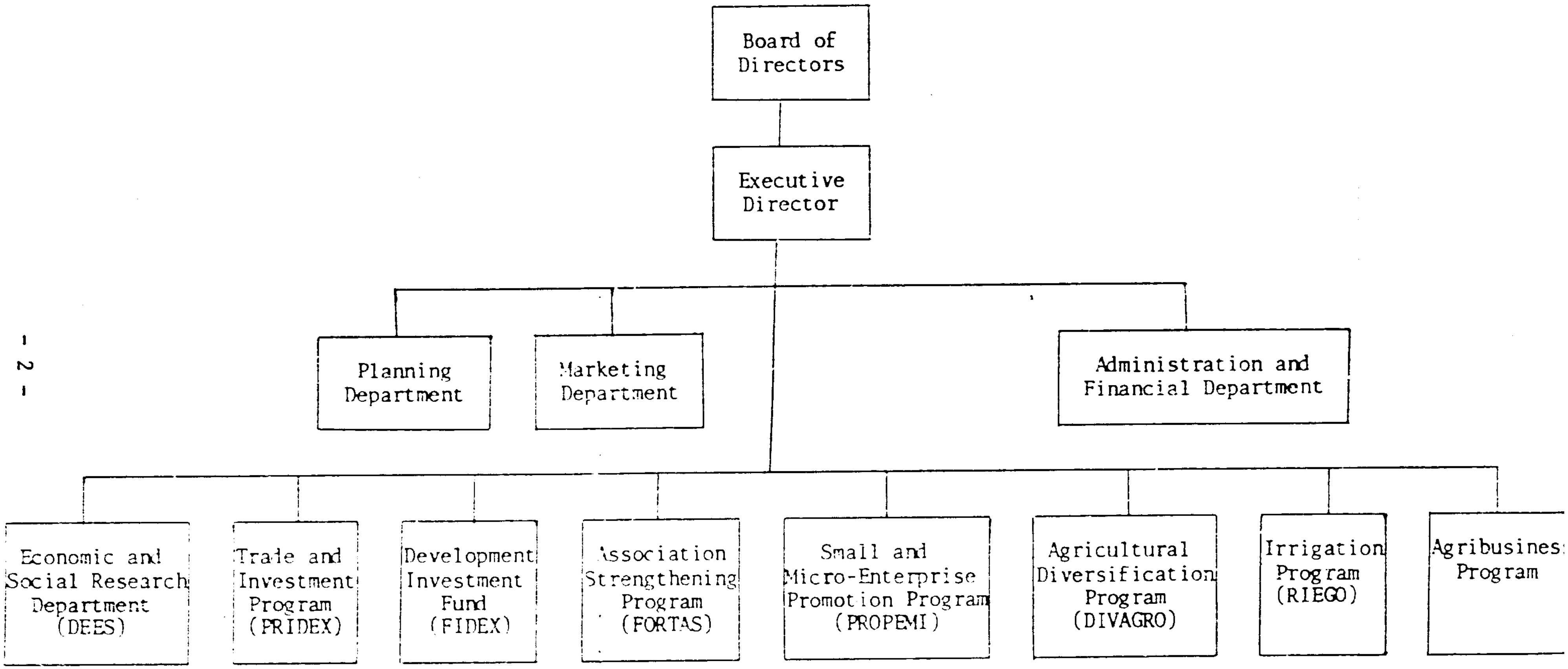
USAID/El Salvador has initiated a number of projects aimed at improving the country's economic situation. Besides implementing projects through the Government of El Salvador, the Mission has also relied recently on the private sector to implement its projects. One private organization that the Mission has used to implement several projects is the Salvadoran Foundation for Economic and Social Development (commonly known by its Spanish acronym, FUSADES).

The Salvadoran Foundation for Economic and Social Development was created in 1983 by a group of about 100 Salvadoran business leaders as a private Salvadoran "think tank." The organization was established to develop alternative solutions to governmental intervention in response to El Salvador's economic, political and social problems. It was legally established in August 1983 as a private non-profit organization and has received A.I.D. assistance since late 1983.

As of September 30, 1987 USAID El Salvador had authorized approximately $75 million for the Foundation's establishment and for the A.I.D. approved activities that it administers. Of this amount, $61.5 million had been obligated; accrued and actual expenditures amounted to $10.5 million. Nearly all of these funds were authorized under seven cooperative agreements, as amended, during the period September 1984 to October 1987. (See Exhibit 1 for a listing of the agreements.)

Besides financing the Foundation's direct operations, funds authorized by these agreements financed activities under the Foundation's eight programs as shown in the following general organizational diagram with their Spanish acronyms. (See Exhibit 2 for more information on the eight program activities.)

Organization Chart of FUSADES' Major Activities 1/



1/ The Foundation was in the process of reorganizing its organizational structure to more efficiently manage its programs by consolidating similar functional activities.

The Foundation had a total paid professional and support staff of 107 to manage its activities, representing an annual salary cost of about $1.1 million. Besides its paid staff, Foundation policies and guidance was provided by its 23-member Board of Directors, a 9-member Executive Committee, and by the members making up the 11 commissions and committees established to oversee and approve specific program activities. For the most part, these individuals received no compensation for their time and services on these various bodies. As of December 31, 1986 Foundation membership totaled 226 individuals.

The Foundation had received funds from other sources such as voluntary business and individual contributions, mandatory contributions from program beneficiaires, loan reflows, and from fees charged for seminars, training and publications. However, the total amount obtained from these sources was negligible when compared with direct A.I.D. funding which, as of December 31, 1986, accounted for 96 percent of the Foundation's operations.

A.I.D. monitoring responsibilities for FUSADES were generally split between the Offices of Private Enterprise, Rural Development and the Controller.

B. Audit Objectives and Scope

At the request of USAID/El Salvador, the Inspector General for Audit/Tegucigalpa, conducted a program results audit of the Salvadoran Foundation for Economic and Social Development (FUSADES) during the period July 13, 1987 to October 14, 1987. Specifically, the audit objectives were to determine if: (1) A.I.D. funded activities were achieving their planned objectives, (2) A.I.D. funds were adequately accounted for, and (3) project activities were being implemented in compliance with A.I.D. regulations and project agreements.

To accomplish these objectives, project files, records and other pertinent information were reviewed, and a total of 35 officials at USAID/El Salvador and at the Foundation were interviewed. In addition, field visits were made to a total of 22 beneficiaries of A.I.D.-funded assistance under the PRIDEX, FORTAS, PROPEMI, DIVAGRO, and RIEGO programs. These were the only programs with measurable activity as of June 30, 1987, which was the audit's cut-off date for assessing program accomplishments.

As of September 30, 1987, $10.5 million had been disbursed under the seven cooperative agreements between A.I.D. and FUSADES. The agreements did not generally require counterpart contributions from FUSADES, although project beneficiaries under some programs were required to contribute a minimum of 25 percent of project costs. These "counterpart" funds were not audited, although how they are used is a topic of discussion in this report. Other than normal annual financial audits, none of FUSADES' activities had been independently evaluated or audited before.

Our review of internal controls and compliance was limited to the findings reported. The audit was made in accordance with generally accepted government auditing standards.

AUDIT OF
SALVADORAN FOUNDATION FOR ECONOMIC
AND SOCIAL DEVELOPMENT

PART II - RESULTS OF AUDIT

The audit showed that (1) four of the eight planned programs were behind schedule because of implementation delays and their impact on achieving overall program objectives was uncertain; (2) the Foundation had adequate financial controls and accounting systems over A.I.D. funds; and (3) some A.I.D.-funded activities were not in compliance with A.I.D. regulations or project agreements.

Nevertheless, the Foundation, during its brief three-year existence, had developed into a responsive organization with capable and dedicated management staff; contributed to strengthening private sector business associations; increased the Government of El Salvador's awareness of alternatives to its economic policies; stimulated interest and investment in non-traditional products; and provided financial and technical assistance to businesses and entrepreneurs which might not otherwise have been available.

Specific problems observed included: required contributions from program beneficiaries were not always being used for project purposes or in accordance with A.I.D. allowable cost provisions; the Foundation was not actively seeking increases in contributions from project beneficiaries; the actual impact of project accomplishments was viewed as uncertain; and program activities were not being independently evaluated to assess their cost-effectiveness.

The audit findings were not totally unexpected given the Foundation's rapid organizational growth, its initial unfamiliarity with A.I.D. requirements and procedures, the country's civil conflict, the destructive 1986 earthquake, and other obstacles impeding private sector development.

The report recommends that USAID/El Salvador obtain an opinion from A.I.D.'s General Counsel on the appropriate uses of project beneficiary contributions; have the Foundation establish a more aggressive policy in obtaining contributions; establish uniform criteria and a system for measuring and reporting project accomplishments; and establish a plan and timetable to evaluate program activities. The report also contains a number of other observations which require management's attention.

A. Findings and Recommendations

1. Use of Project Beneficiary Contributions Should Be Restricted to Project Purposes

There was no assurance that required contributions from project beneficiaries were being used for project purposes or in accordance with the allowable costs which were stated by the standard provisions of the cooperative agreements between A.I.D. and FUSADES. Certain of the A.I.D.-funded programs required that recipients of A.I.D. financial assistance contribute a minimum of 25 percent of the total costs of the proposed activity to the Salvadoran Foundation for Economic and Social Development. These programs, however, do not specify how these funds are to be used. The Foundation considered these contributions to be their "own" funds and had commingled them with the other non-A.I.D. donations that it had received. However, since these "donations" were directly linked and prerequisite to receiving A.I.D. funding, their use, in our opinion, should be restricted for project purposes and subject to A.I.D.'s standard rules on allowable expenditures as stated in the cooperative agreements. Restricting the use of these mandatory contributions in this manner would result in less direct A.I.D. funds being required for project purposes. This could be substantial. The Foundation has estimated it would generate nearly $7 million by 1992 from mandatory contributions.

Recommendation No. 1

We recommend that USAID/El Salvador obtain FUSADES' agreement to use beneficiary contributions for project purposes only or obtain a formal Agency General Counsel legal opinion showing why the use of these monies should not be restricted.

Discussion

There was no assurance that required contributions from project beneficiaries were being used for general project purposes and/or in accordance with general A.I.D. policies. Certain of the A.I.D.-funded programs required that recipients of A.I.D. financial assistance contribute a minimum of 25 percent of the total costs of the proposed activity to the Salvadoran Foundation for Economic and Social Development. These programs, however, do not specify how these funds are to be used. These mandatory contributions were deposited into a single account with other non-A.I.D. donations and were considered by the Foundation to be its "own" funds without restriction on their use, even though these contributions were directly linked and prerequisite to receiving A.I.D. assistance.

Based on Foundation reports, about $200,000 had already been contributed in this manner and another $122,000 was identified as owed to the Foundation as of June 1987. During the next five and one-half years the Foundation estimated that an additional $6.8 million would be donated by recipients of A.I.D.-funded activities. The Foundation has used its "own" funds, which include these mandatory contributions, to pay for operating costs which were not authorized under the cooperative agreements or consistent with A.I.D. policies. For example, the Foundation had used these funds for entertainment expenses, including business lunches, and for the purchase of land.

Reimbursement of these types of expenses would not be allowable under grants and contracts financed by the U.S. Government. The standard provisions to the Cooperative Agreements provide that the grantee shall be reimbursed for costs incurred in carrying out the purposes of the grant which are determined to be reasonable, allocable, and eligible in accordance with, among other criteria, the cost principles contained in OMB circular A-122 entitled "Cost Principles for Nonprofit Organizations." These principles state that entertainment expenses, including lunches, are not an allowable cost. It is also not A.I.D. policy to acquire land with appropriated funds. In our opinion, contributions to the Foundation from project beneficiaries as a condition to receiving A.I.D.-funded assistance should be subject to the same allowable cost provisions and A.I.D. policies that govern the use of appropriated funds because these funds are directly linked to the provision of A.I.D. assistance.

Furthermore, unless a donation is required to be used for specific purposes, it would constitute general support for the Foundation, in effect an endowment. Therefore, allowing unrestricted use of these contributions could be construed as tacit agreement by A.I.D. to indirectly augment the Foundation's endowment without obtaining the necessary Congressional consent. According to A.I.D.'s Regional Legal Advisor (RLA), A.I.D. is prohibited from making contributions to endowments unless specifically authorized by the Congress. The RLA stated that, in her opinion, USAID/El Salvador was indirectly contributing to the Foundation's endowment by not objecting to the requirement that project beneficiaries donate funds to augument Foundation's endowment as a condition to receiving A.I.D. assistance. The RLA stated that, to her knowledge, A.I.D.'s General Counsel had not specifically addressed whether or not this indirect financing scheme was consistent with Congressional intent or whether these funds were subject to allowable-cost limitations as defined in the standard provisions to the cooperative agreements. In her opinion, it might be appropriate to restrict the use of these funds for specific project purposes.

Mission officials stated that the cooperative agreement which first identified the financing scheme was authorized by AID/Washington. As a result, they believe the Office of General Counsel would have reviewed and cleared the financing scheme. In addition, Mission officials said other Missions have projects with similar financing schemes. USAID officials stated that they considered these funds to be the Foundation's, without restrictions, and had never considered requesting a specific General Counsel opinion on this matter.

As a result of not restricting the use of project beneficiary contributions, there was no assurance that these contributions would be used for project purposes and/or in accordance with United States allowable-cost provisions for nonprofit organizations. Restricting the use of these mandatory contributions in this manner would better ensure their proper use and would result in less direct A.I.D. funds being required for project purposes. This could be substantial. The Foundation has estimated it would generate nearly $7 million by 1992 from mandatory contributions.

Management Comments

In its written comments, the Mission stated it did not have the same concerns as the auditors with respect to usage of beneficiary contributions or the potential "appearance of kickbacks" such unrestricted usage creates. The Mission stated that it believes such funds should be used in a manner consistent with the overall goals and objectives of FUSADES and that the Foundation's bylaws prohibit use of FUSADES funds for such things as political campaign contributions, which was an initial concern of the Mission. In addition, the Mission stated that it would not be in A.I.D.'s interest to restrict the beneficiary contributions to specific projects or programs, because this would increase funding for programs that the Mission is trying to de-emphasize.

Office of Inspector General Comments

The Office of Inspector General disagrees with the Mission on the need to restrict the use of mandatory beneficiary contributions. We also continue to have a concern with the potential image problem unrestricted use of these monies creates but, having alerted A.I.D. officials of this issue in the draft report, have eliminated it from the final report at their request. In our opinion, mandatory contributions from beneficiaries of A.I.D. financed projects should be used for activities consistent with A.I.D.-funded project purposes and the cost principles contained in OMB circular A-122 entitled "Cost Principles for Nonprofit Organizations." Restricting the use of these funds will better ensure they are not used for inappropriate activities and could result in substantially less direct A.I.D. funds being required to implement project activities. This latter point is significant, given the United States Government desire to reduce federal spending. The significance of this finding and recommendation is also linked to the following discussion on encouraging the Foundation to increase beneficiaries' contributions to FUSADES-sponsored activities.

2. The Foundation Should Attempt to Obtain Greater Participation by Project Beneficiaries

The Salvadoran Foundation for Economic and Social Development had not always encouraged program beneficiaries to share in activity cost beyond the minimum 25 percent required under certain of its A.I.D.-funded programs. Implicit in the cooperative agreements, just as in the Foreign Assistance Act requirement on counterpart contributions, is the intent that project beneficiaries be encouraged to contribute as much as possible toward the cost of activities from which they benefit. The Foundation had not established a policy or any criteria designed to maximize the amount of contributions from project beneficiaries. As a result, the potential income from this source was greatly reduced, causing greater reliance on A.I.D. resources.

Recommendation No. 2

We recommend that USAID/El Salvador, in consultation with the Foundation, establish a more aggresive participatory funding policy which better recognizes the extent of assistance provided, the project beneficiaries' financial ability to pay, and the purposes of the project.

Discussion

The Salvadoran Foundation for Economic and Social Development had not always encouraged beneficiaries to share in activity costs beyond the minimum 25 percent required under certain of its A.I.D.-funded programs.

As of June 30, 1987 the Foundation had received about $200,000 in contributions from program beneficiaries. These contributions were generated under four programs - PRIDEX, FORTAS, DIVAGRO and RIEGO. These programs generally required that beneficiaries contribute a minimum of 25 percent of the total activity cost to the Foundation. Generally, those activities with easily identifiable costs such as contracted technical assistance and travel were subject to the 25 percent requirement. A fee was often charged to cover expenses of other activities, such as seminars, conferences, and publications. However, there was little evidence that program managers had encouraged beneficiaries to participate more fully. In some cases, especially in the larger enterprises, greater contributions may have been feasible. Program managers indicated that some enterprises assisted under the trade and investment promotion, agricultural diversification, and association strengthening activities were capable of greater financial participation in their projects.

Implicit in the cooperative agreements, just as in the Foreign Assistance Act Section 110 requirement on counterpart contributions, is the intent that project beneficiaries be encouraged to contribute as much as possible toward the cost of activities that are designed to benefit them.

Program managers stated that until recently, very little emphasis had been placed on obtaining greater contributions from project beneficiaries. They also stated that there had not been any attempt to differentiate by type or size of enterprise or financial capabilities in regard to obtaining contributions. A Foundation official stated that greater participation had not been actively sought during the programs' initial years because this action might have adversely impacted on the programs' appeal and their developmental effect. He stated that there were at least 13 cases where project beneficiaries under the FORTAS and PRIDEX programs had contributed over the 25 percent minimum. In one case, the contribution represented two-thirds of the total activity cost. The official also stated that serious consideration was being given to increasing the contribution requirement for travel under the PRIDEX program to 75 percent of the total cost.

As a result of not trying to maximize the amount of contributions from project beneficiaries, the programs had to continue to rely heavily on A.I.D. support.

However, Foundation management and USAID/El Salvador officials stated that different strategies had been discussed recently for the purpose of identifying ways to increase Foundation revenues. One strategy discussed was to obtain greater contributions from project beneficiaries. The Foundation had also recognized that long-term USAID assistance was not assured and that other sources of revenue should be developed. One Foundation official also stated that, in his opinion, the higher the beneficiary contribution to a project the greater its chance for success.

Management Comments

In its written comments, the Mission stated that as of December 14, 1987, contributions from other than A.I.D. funding sources amounted to $1.1 million or about 12 percent of total A.I.D. disbursements to the Foundation. The Mission stated that this amount could not be considered "negligible." The Mission stated that initially it had discouraged the Foundation from pursuing a more aggressive policy because of potential inconsistencies with the project's development objectives and the risk of having the Foundation viewed as out of reach of the average businessman. The Mission added, however, that it had encouraged the Foundation to pursue a more aggressive contribution policy. Therefore, the Mission requested that the recommendation be deleted.

Office of Inspector General Comments

The audit showed that the Foundation had not yet adopted an official policy to obtain greater contributions from project beneficiaries which better recognizes the extent of assistance provided, financial ability to pay, and the purpose of the project. The report recommendation can be closed upon receipt of written evidence that the Foundation has established such a policy.

3. USAID/El Salvador Needs to Establish a More Reliable System for Measuring And Reporting Project Accomplishments

The actual effect of project activities on generating jobs, foreign exchange and other accomplishments was uncertain. The audit found that reported jobs, foreign exchange and other accomplishments generated by two of the eight programs were not properly classified or accurately reported. In addition, the audit found that important program accomplishment data may have been improperly erased from computer memory by the program contract manager. A.I.D. Handbook guidance requires that Missions establish monitoring and evaluation information systems to accurately measure the effect of project activities. Neither USAID/El Salvador nor the Salvadoran Foundation for Economic and Social Development had established adequate criteria and a system for measuring project accomplishments. As a result, we could not accurately assess the cost-benefits or impact of project activities.

Recommendation No. 3

We recommend that USAID/El Salvador, in consultation with the Foundation:

a) establish uniform criteria and a system for measuring and reporting project accomplishments; and

b) determine whether or not information eliminated from the Trade and Investment Promotion computer record needs to be replaced and, if so, ensure that replacement costs are recovered from the management contract.

Discussion

Reported project accomplishments under at least two A.I.D.-funded programs administered by the Foundation were unreliable. The audit found that the effect of the trade and investment promotion activities on generating jobs and foreign exchange (two major program goals) was uncertain. In addition, the effect of agricultural diversification activities appeared overstated.

As of June 30, 1987 the Trade and Investment Promotion Program (PRIDEX) claimed its activities had generated 4,738 jobs and $12.4 million in foreign exchange earnings. However, program staff admitted that these amounts could not be substantiated. For example, they stated that program promotion executives often estimated jobs and foreign exchange generated instead of gathering actual data from clients. Also, reported jobs were overstated as seasonal jobs counted the same as full-time positions. A program manager stated, for example, that if a client hired 100 employees for a temporary period, laid them off and then rehired them during a subsequent temporary period, the program would claim the total 200 jobs as being generated by the program. Site visits to several of the program's clients confirmed that jobs reported were inaccurate. Besides including seasonal workers with full-time workers, it was noted that at one company 86 employees were counted as new jobs when in fact they were pre-existing jobs which were being maintained with program funds used to alleviate the company's cash flow problems.

In connection with the questioned accomplishments claimed under the PRIDEX program, the audit disclosed that the overall accomplishments claimed in the program's latest report did not reconcile with the report's detailed information. A comparison of the summary information with the detailed data showed a difference of 503 jobs and $1.8 million in foreign exchange earnings as shown below.

Summary of Differences in PRIDEX Program Results

Program Sectors	Jobs Generated			Dollars Generated ($000)		
	Claimed	Supported	Difference	Claimed	Supported	Difference
Apparel	1,376	1,159	(217)	$ 2,531	$ 1,090	$(1,441)
Agriculture	1,992	1,546	(446)	1,905	1,530	(375)
Industrial Handicrafts	780	774	(6)	2,610	2,638	28
Light Manufacturing	590	756	166	5,274	5,242	(32)
Total	4,738	4,235	(503)	$12,320	$10,500	$(1,820)

Program officials could not adequately explain the reasons for the differences in the information. The Foundation wanted to make it clear, however, that the subject data had been compiled while the program was managed by a contractor. Program officials were unable to reproduce the back-up information from computer storage, as this information had been erased by the contractor in August 1987 upon completion of the contract. USAID/El Salvador and Foundation officials were unaware of this situation, but immediately took action to investigate the matter and to determine if the erased data was necessary for program analysis purposes.

It also appeared that accomplishments under the Agricultural Diversification (DIVAGRO) program had been overstated. For example, in the June 1987 semiannual report on program activities it was implied that the program had established two new packing plants for cucumbers and melons during the first half of 1987. In reality, the program provided technical assistance to existing concerns to diversify their operations. USAID's Rural Development staff agreed that DIVAGRO had overstated its accomplishments and stated that the Mission and the Foundation needed to establish a system to measure the project's impact and to establish more realistic reporting criteria.

A Foundation official stated that DIVAGRO program accomplishments had recently been reviewed. He stated that its claimed quantitative results in generating foreign exchange and investments had been understated while claimed results in generating jobs had been slightly overstated. He also stated that some jobs claimed under DIVAGRO could also have been claimed under the PRIDEX program because these programs often work with the same clients.

A.I.D. Handbook 3 and AID/Washington guidance require that Missions establish monitoring and evaluation information systems to accurately measure and report the effect of project activities. Implicit in this guidance is the need to establish uniform criteria to ensure accurate classification and reporting of project accomplishments.

Our uncertainty about project impacts stems from the fact that accomplishments were not properly classified or accurately reported.

Neither USAID/El Salvador nor the Foundation had established adequate criteria or a system for measuring the impact of project accomplishments. Program outputs were being identified, but the impact of these outputs was, for the most part, not being measured or not being measured in a consistent manner. In all fairness to the PRIDEX and DIVAGRO programs, measuring and reporting the impact of project accomplishments appeared to be a problem with all Foundation-administered programs.

As a result of not establishing uniform criteria and a system for measuring project accomplishments, neither the Mission nor the Foundation could accurately assess the cost-benefits or impact of project activities.

Management Comments

Mission officials agreed there was a need to establish uniform criteria and a system for measuring and reporting project accomplishments under some of its programs. At the exit conference, Mission officials stated that A.I.D. had generally been remiss in establishing adequate criteria and systems to measure and report project accomplishments, especially in regard to measuring the impact of project activities on overall project goals and objectives. The Mission also stated that the Foundation would make a determination as to the fault and responsibility for the Trade and Investment Promotion computer memory loss and proceed accordingly.

Office of Inspector General Comments

Minor wording changes were made to the text based on the Mission's comments. The recommendation can be closed upon evidence that appropriate actions have been taken.

4. Program Activities Need To Be Evaluated

None of the A.I.D.-funded activities administered by the Salvadoran Foundation for Economic and Social Development had been independently evaulated to determine its impact on achieving planned objectives or its cost-effectiveness. As provided by A.I.D. Handbook 3, Chapter 12, independent evaluations are necessary to make objective and rational decisions about projects. Several cooperative agreements also required that evaluations be performed prior to the time of our audit. Evaluations had not been previously scheduled because, according to the Mission, it did not want to burden the Foundation by having an evaluation performed simultaneously with the Inspector General's audit, which was expected earlier, and also because of the major earthquake in October 1986, which interrupted both the Foundation's and the Mission's operations for an extended period. As a result of not performing independent evaluations, the Mission had less reliable information by which to judge the performance of project activities and to determine if they were cost-effective.

Recommendation No. 4

We recommend that USAID/El Salvador establish a plan and timetable to evaluate Foundation activities before any new A.I.D.-funded activities are approved.

Discussion

None of the A.I.D.-funded activities administered by the Salvadoran Foundation for Economic and Social Development had been independently evaluated to determine their impact on achieving planned objectives or their cost-effectiveness. Since September 1984, seven cooperative agreements covering eight programs had been executed with the Foundation. These seven agreements authorized nearly $74 million for program activities, some of which had been approved for more than two years at the time of our review. As of September 30, 1987, $10.5 million had been disbursed under the seven agreements.

Some program activities had been amended to increase their funding and to extend their project assistance completion dates without the benefit of independent evaluations. For example, funding for the Trade and Investment Promotion, Economic Studies, Agricultural Diversification and Association Strengthening activities was increased and their programs extended without full knowledge of the activities' success in achieving planned objectives.

Mission officials stated that it was not entirely true that these activities had not been assessed. They stated, for example, that the Trade and Investment Promotion activities had been partially assessed by outside consultants in conjuction with preparing a project paper amendment; the Department of Economic Studies activities were partially reviewed by two outside consultants in conjuction with studies on the strategy and organization of the Economic Studies Department and the feasibility and design of a proposed statistical system; the Association

Strengtening activities had undergone a Mission in-house review; and an analysis of the Foundation had been conducted by an AID/Washington team in the preparation of a new agribusiness project paper. In addition, the Mission stated that a two-person team from AID/Washington had just completed a two week review of FUSADES' organizational structure and activities for the purpose of determining its ability to administer additional programs. The Mission stated that although these studies and assessments were not referred to as evaluations, they did provide useful program information which the Mission had considered in making program decisions.

A.I.D. Handbook 3, Chapter 12 provides general guidance on evaluations. As stated in section 12B3, the purpose of evaluation is to provide an objective and rational basis for making decisions about current and future projects, programs, policies and procedures. In addition, the cooperative agreements covering all the program activities, with the exception of the FORTAS and DIVAGRO programs, required that independent evaluations be performed within two years of the signing of the cooperative agreements. Project agreement No. 519-0316, which covers association strengthening activities, did not require an independent evaluation, but instead required a final program staff report after the first year and was to include an analysis of the impact of activities under the program. Similarly, Cooperative Agreement No. 519-0265, which covers the DIVAGRO program, did not require an independent evaluation, but instead required semiannual in-house reviews of program activities. Neither of these two internal assessments provided the benefits of an objective evaluation.

USAID/El Salvador stated that specific program evaluations had been considered, but evaluation plans were postponed because of other events. They stated that the Mission did not want to over-burden the Foundation by having an evaluation performed simultaneously with the Inspector General's audit, which was originally scheduled for late 1986, and because of the major October 1986 earthquake which interrupted both the Foundation's and the Mission's operations for an extended period. The Mission stated further that it was currently processing a bid for an evaluation of the RIEGO program in September 1987 and that it planned to arrange evaluations of the PRIDEX and PROPEMI programs in the future.

As a result of not obtaining independent evaluations of program activities, USAID/El Salvador had less reliable information to fully assess the impact of project activities on achieving project objectives and this large program's cost-effectiveness.

Management Comments

Mission officials stated that it was in the Mission's and Foundation's best interest to evaluate the programs to determine their impact on achieving planned objectives and their cost-effectiveness. The Mission stated that it had started the process to evaluate many of the Foundation's programs. Evaluations of the PROPEMI and PRIDEX programs would start in the second quarter of 1988.

Office of Inspector General Comments

The recommendation will be closed upon evidence that an evaluation plan and timetable has been established to evaluate the Foundation's programs.

B. Compliance and Internal Control

1. Compliance

The audit disclosed five compliance exceptions. First, USAID/El Salvador had not arranged for independent program evaluations as required by A.I.D. guidance and certain of the cooperative agreements (Finding No. 4). Second, USAID advanced more funds to the Foundation than authorized by A.I.D. regulations (see following section). Third, the Foundation had earned interest on grant funds in violation of the cooperative agreement (see following section). Fourth, the Foundation practiced age discrimination in its employment policies which is inconsistent with the Age Discrimination Act of 1975 (see following section). Fifth, some project-funded vehicles were permanently assigned to Foundation executives and therefore not available for project implementation purposes (see following section).

Other than the conditions cited, tested items were in compliance with applicable laws and regulations and nothing came to our attention that would indicate that untested items were not in compliance.

2. Internal Control

The audit disclosed one internal control weakness in that neither the Foundation nor USAID/El Salvador had established adequate systems for measuring and reporting program accomplishments (Finding No. 3).

With the above exception, no other control weaknesses came to our attention.

C. Other Pertinent Matters

During the audit several other issues warranting management's attention were identified. First, the audit showed that the Controller's Office has not itself performed a detailed assessment of the Foundation's financial capabilities or periodically spot-checked documentation supporting expense vouchers even though A.I.D. funding of the Foundation had increased dramatically. A.I.D. Handbook guidance and provisions of the Federal Manager's Financial Integrity Act require that Missions assure themselves that borrowers/grantees have adequate management capabilities and financial controls to ensure the proper accountability and use of A.I.D. project funds. Because of staff limitations, and other priority matters, the Controller's Office had relied on annual audited financial statements to monitor the Foundation's financial activities. The current audit showed that the Foundation was adhering to the operating manuals established for it by Price Waterhouse and found no evidence that A.I.D. funds were not being adequately accounted for. However, we do not believe that the Controller's office should rely primarily on periodic financial statements to assure itself of the Foundation's management capabilities and financial controls, especially since these statements do not provide adequate details on A.I.D. funds.

As part of the current audit, a desk review of the Foundation's last financial statements (as of December 31, 1985 and 1986) was performed. This review disclosed that although the audited financial report followed generally accepted auditing standards, it did not follow the expanded scope of work required by the General Accounting Office's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision). The audit report also disclosed the following matters that, for USAID purposes, could be an indication of unallowable costs and/or credits to project costs: (1) severance compensation had been paid annually to the Foundation's employees, and (2) at least part of USAID funds were generating interest income on short-term deposits (see the final Other Pertinent Matter). Additionally, there was no detailed information about the source and uses of USAID funds, nor comparisons with budgeted amounts.

The Controller's office would have better information to assess the Foundation's financial management if it required that the annual financial statements follow the General Accounting office standards and contain detailed information about the source and uses of USAID funds. The Mission stated that the General Accounting Office standards were only required if A.I.D. were to directly employ or contract the external auditing firm, but, since the Foundation contracted the auditing firm, the standards were not required. In our opinion, since A.I.D. finances 96 percent of the Foundation's Operations, including the last annual financial audit, it can require that the audit report follow General Accounting Office standards and be expanded to provide more detailed information about the source and uses of USAID funds. Regarding the severance pay issue, the Mission agreed it was a valid questions and had taken appropriate steps to ensure that it was legal under Salvadorean law.

Second, our review of the RIEGO program revealed a potential conflict-of-interest situation. As the program currently operates, commercial irrigation equipment suppliers are responsible for identifying potential participants. However, they must also assume 20 percent of the risk for loans made to beneficiaries, which had led to higher prices for the equipment. Mission management agreed that certain adjustments were needed in this aspect of the program and had begun to take steps to effect them at the time our review ended.

Third, it was noted that the Foundation was buying dollars from unauthorized sources to replenish the U.S. dollar account for advances which were not fully liquidated. The audit did not determine the extent of this practice or amounts involved; however, a recent purchase of $2,383 was made which cost the Foundation $262. This practice is not consistent with either El Salvador's or the United States' economic policies or ethical practices. The Mission stated that the Foundation's policies were being amended to stop this practice.

Fourth, it was noted that the Foundation's literature for external distribution rarely disclosed the source of program funds. Foundation pamphlets and annual reports generally did not indicate that the U.S. government was supporting the Foundation and its programs. No one that we spoke with at the Mission or at the Foundation could explain why the United States was not recognized as the Foundation's major supporter in Foundation literature, although they felt the origin of the Foundation's funding was common knowledge. The Mission stated it was simply preferable to maintain a low profile in certain elements of A.I.D. activities.

Fifth, it was noted that the Foundation discriminates on the basis of age in its employment practices. The audit did not determine the extent that this had happened, but identified 5 recent position openings which required that candidates be between the ages of 25 to 35. In accordance with the Age Discrimination act of 1975, U.S. funds cannot be used to support organizations that practice age discrimination. The Mission stated that foreign Private Voluntary Organizations were not subject to the Act's requirements. However, they agreed age discrimination was inconsistent with A.I.D. policy and took action to correct the situation.

Sixth, it came to our attention that the Foundation had not established a reserve for bad debts in its accounting system for loans made under the PROPEMI program. As a result, the original amount available under the program for loans could be reduced. There is no provision that a portion of the loan reflows be reserved for bad debts. This should be established to better ensure that the program's original loan amount is maintained. The Mission agreed and stated that steps would be taken to establish a reserve fund.

Seventh, it was noted that several top managers were incorporating as businesses to reduce the amount of income tax liability. The propriety of this apparent tax avoidance scheme needs to be determined. If such a practice is illegal under El Salvador tax laws, it should be quickly stopped. A.I.D. cannot afford to be accused of funding an organization which is not abiding by the laws of the country. This is a particularly sensitive issue, given the bad publicity that certain A.I.D. supported public agencies have recently received. The Mission agreed and has taken appropriate corrective actions.

Eighth, some of the eight A.I.D.-purchased vehicles were not being used for project purposes. The audit found that three of the vehicles were permanently assigned to Foundation executives and therefore not available for project implementation purposes. USAID needs to ensure that A.I.D. funded resources are used for project purposes and in accordance with the cooperative agreement provisions. The Mission stated it had taken steps to ensure that the three program vehicles assigned to Foundation managers have been reassigned.

Ninth, the audit disclosed that USAID/El Salvador had not promptly liquidated project advances. As of July 1987, $300,000 in advances made to the Foundation had remained outstanding for six months. In accordance with A.I.D. regulations, advances should not remain outstanding for more than 30 days, or not to exceed 90 days if the Mission had made a formal determination to this effect. Mission officials could not fully explain why this situation occurred, but indicated it may have been a USAID Controller error. As a result, unnecessary U.S. Government interest costs of $9,000 may have been incurred while advances remained outstanding. This matter was brought to the Mission's attention during the audit and the Mission took immediate action to correct the situation. For this reason, there was no need for further recommendations.

Finally, the Foundation had earned interest on its dollar account in the United States. The cooperative agreement and subsequent project implementation letters establishing this account prohibited the earning of interest. Foundation officials stated that interest was not earned on the principal account, but rather on time certificate of deposits which were required to guarantee letters of credit for certain procurements in the United States. This interest had been identified in the annual financial statements; however, no action had been taken to return these funds to USAID/El Salvador. As of October 1987, the Foundation reported that $2,166 in interest had been earned on these time deposits. After this matter was brought to the Mission's attention, immediate action was taken to recover the interest earned. As a result, no further action was recommended.

AUDIT OF
SALVADORAN FOUNDATION FOR ECONOMIC
AND SOCIAL DEVELOPMENT

PART III - EXHIBITS AND APPENDICES

Summary of A.I.D./FUSADES
Project Agreements as of September 30, 1987

Agreements	Date Signed	Current PACD	Amount Authorized	Amount Obligated	Amount Expended	Amount of Pipeline	Activities
Industrial Stabilization & Recovery Project No. 519-0287 (FUSADES, DEES, PRIDEX, FORTAS)	9/24/84	9/30/89	$26,900,000	$26,900,000	$6,380,369	$20,519,631	-FUSADES Administration -Department of Economic and Social Studies -Trade and Investment Promotion Program (Includes Credit Program) -Strengthening Private Enterprise Associations
Agricultural Diversification Program No. 519-0265 (DIVAGRO)	1/29/85	7/31/88	3,837,000	3,837,000	1,727,478	2,109,522	-Agricultural Diversification Program that Promotes Non-Traditional Agricultural Goods
Association Strengthening Activities Project No. 519-0316 (FORTAS, DEES)	7/19/85	12/31/87	1,945,000	1,945,000	699,962	1,245,038	-Strengthening Private Enterprise Associations -Department of Economic and Social Studies -Entrepreneurs of Educational Development Eastern Development Coordination Committee
Water Management Project No. 519-0303 (RIEGO)	8/27/85	8/30/90	$13,450,900	$13,450,900	$ 761,493	$12,689,407	-Irrigation Program that Promotes the Cultivation of Non-Traditional Crops for Export that Utilize Irrigation (Includes Credit Program)
Urban Small Business Project No. 519-0304 (PROPEMI)	8/29/85	9/30/88	3,000,000	3,000,000	902,052	2,097,948	-Small and Micro-Enterprise Promotion Program (Includes Credit Program)
Private Sector Initiatives Project No. 519-0336 (FORTAS, DEES)	8/31/87 1/	1/1/91	4,700,000	2,250,000	- o -	2,250,000	-Continuation of Activities under Project No. 519-0316 -Strengthening Private Enterprise Associations -Department of Economic and Social Studies
Agribusiness Project No. 519-0327	9/29/87	9/30/92	20,000,000	10,116,000	- o -	10,116,000	-Agricultural Program that Promotes Export of Non-Traditional Agricultural Goods (Includes Credit Program)
Totals			$73,832,900	$61,498,900	$10,471,354	$51,027,546	

1/ Agreement effective date is January 1, 1988.

EXHIBIT 1

FOUNDATION PROGRAM SUMMARIES

ECONOMIC AND SOCIAL RESEARCH PROGRAM (DEES)

Background

Economic and Social Research Program (DEES) activities have always been considered the principal reason for the Foundation's existence. USAID/El Salvador has actively supported these research activities by fully financing them under Cooperative Agreement Project No. 519-0287 which was approved on September 24, 1984.

This financial support enabled DEES to undertake studies required to develop the conceptual and analytical basis for proposing recommendations to the Government of El Salvador on policies and actions which are supportive of economic reactivation, trade, investment and export development. The studies were also intended to support the implementation of PRIDEX and FORTAS activities.

The program is coordinated and managed by 13 professional and support staff (at the time of the audit four more economist positions were being advertised). Their salaries, office equipment and materials were covered under project 519-0287, but no specific budget line item had been established. Instead, program funding was combined with two other Foundation-administered activities, PRIDEX and Foundation administration. As a result, USAID/El Salvador's Controller's Office does not separately account for the program, which makes it difficult to determine the specific amounts authorized, obligated and disbursed. As of September 30, 1987, the three combined activities had been authorized and obligated $26.7 million of which $6.2 million had been disbursed. 1/

The initial project assistance completion date under agreement No. 519-0287 was September 30, 1987, but had been extended once to September 30, 1989.

1/ On July 21, 1987, another cooperative agreement project No. 519-0316 (FORTAS Program) was amended to include $345,961 for the DEES program until December 31, 1987. On August 31, 1987, A.I.D. signed another Cooperative Agreement (Project No. 519-0336) with the Foundation to provide continuing support to FORTAS and DEES through December 31, 1990. The Agreement authorized $1.7 million for FORTAS and $3 million for DEES, but does not take effect until January 1, 1988.

Program Accomplishments

DEES had published several major studies. One of the most important studies was "The Need for a New Economic Model for El Salvador" published in October 1985. The main points of the proposal were suggestions on how to increase employment and exportable production. Six major studies were published during 1986. Among the most significant were: "The State of Our Economy," "Critical Analysis of Fiscal Policy" and "Strategy in the Face of Crisis: Reconstruction and Reactivation." The Department also issues a periodic bulletin which addresses current economic and social aspects of El Salvador.

Around 2,500 copies of DEES' studies and bulletins are distributed. They are distributed to local congressmen, government officials, Foundation members and other individuals and organizations that the Foundation considers would find the publications useful. The impact of these publications had not been measured.

TRADE AND INVESTMENT PROMOTION PROGRAM (PRIDEX)

Background

Trade and Investment Promotion Program (PRIDEX) activities were authorized under Cooperative Agreement No. 516-0287 which was signed on September 24, 1984. The objectives of the program were to generate employment, foreign exchange and new investment in the country through the expansion of non-traditional exports. To accomplish these objectives, the program sought to identify potential investors and exporters and provide them with access to product and industry-specific information and technical assistance. Activities financed by the program included short-term and long-term technical assistance, invitational and observational trips to and from El Salvador, stipend support for training and other activities.

The Salvadoran Foundation for Economic and Social Development (FUSADES) contracted with Arthur Young and Company to manage the program for the first two years of operation. Under this contract, Arthur Young established offices in San Salvador and New York. Two subcontractors were used to facilitate promotion activities in the United States. As of July 1987, program activities were managed by a professional and support staff of 19, including 6 Arthur Young contract staff. In August 1987, the management contract ended and was not extended. At the time of the audit, program management was being transferred to FUSADES.

Program funding was combined under agreement No. 519-0287 with two other FUSADES administered activities, economic studies and FUSADES administration. As a result, USAID/El Salvador's Controller's Office does not separately account for the program, which makes it difficult to determine the specific amounts authorized, obligated and disbursed. As of September 30, 1987, the three combined activities had been authorized and obligated $26.7 million, of which $6.2 million had been disbursed.

The initial project assistance completion date under Agreement No. 519-0287 was September 30, 1987, but had been extended once to September 30, 1989.

Program Accomplishments

According to PRIDEX records, as of June 30, 1987 the program had provided financial assistance to 68 companies and individuals. The program also reported that it provided informal assistance to over 100 other companies and individuals.

The program is behind schedule in achieving its revised planned objectives as shown below.

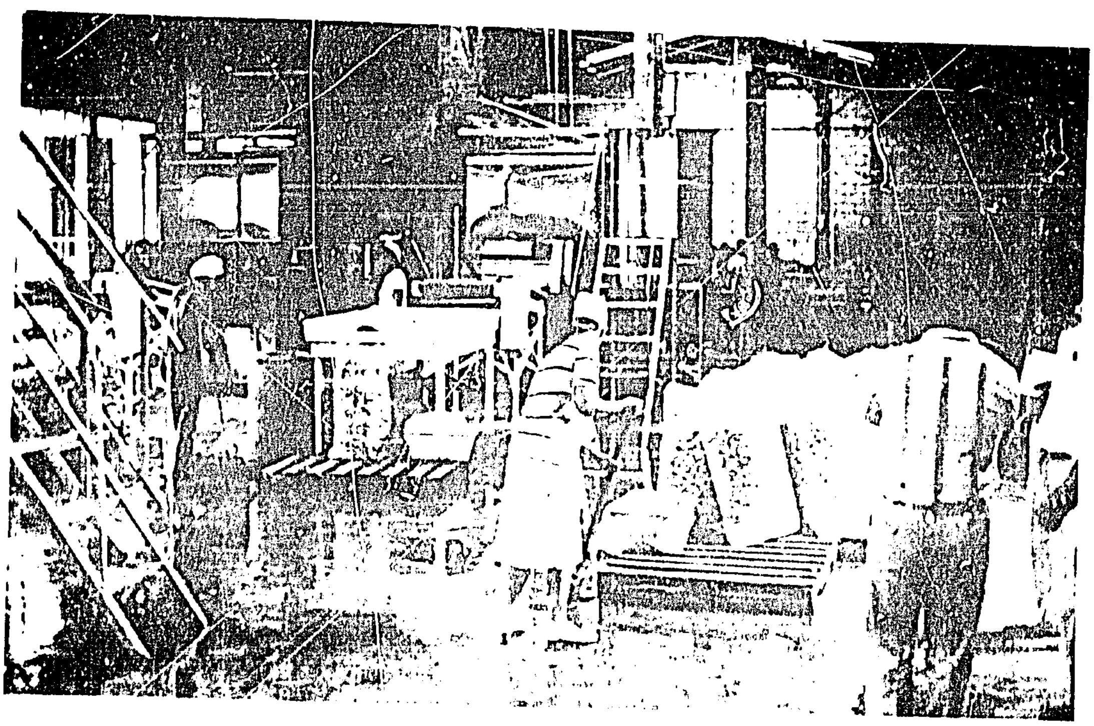
Targets Versus Actual Objectives Accomplishments

Objectives	Original Targets for 1986-1987	Revised Targets for 1986-1987	Actual Outputs for 1985-June 1987	Percentage Actual/ Revised Targets
Jobs	11,500	6,100	4,738	78%
Foreign Exchange ($000)	$34,100	$19,700	$12,370	63%

The only reason given by the Arthur Young contracting team for not achieving the planned objectives was that they were "totally unrealistic." As discussed on page 17 of the report, the audit found that the program's accomplishment reports were unreliable.

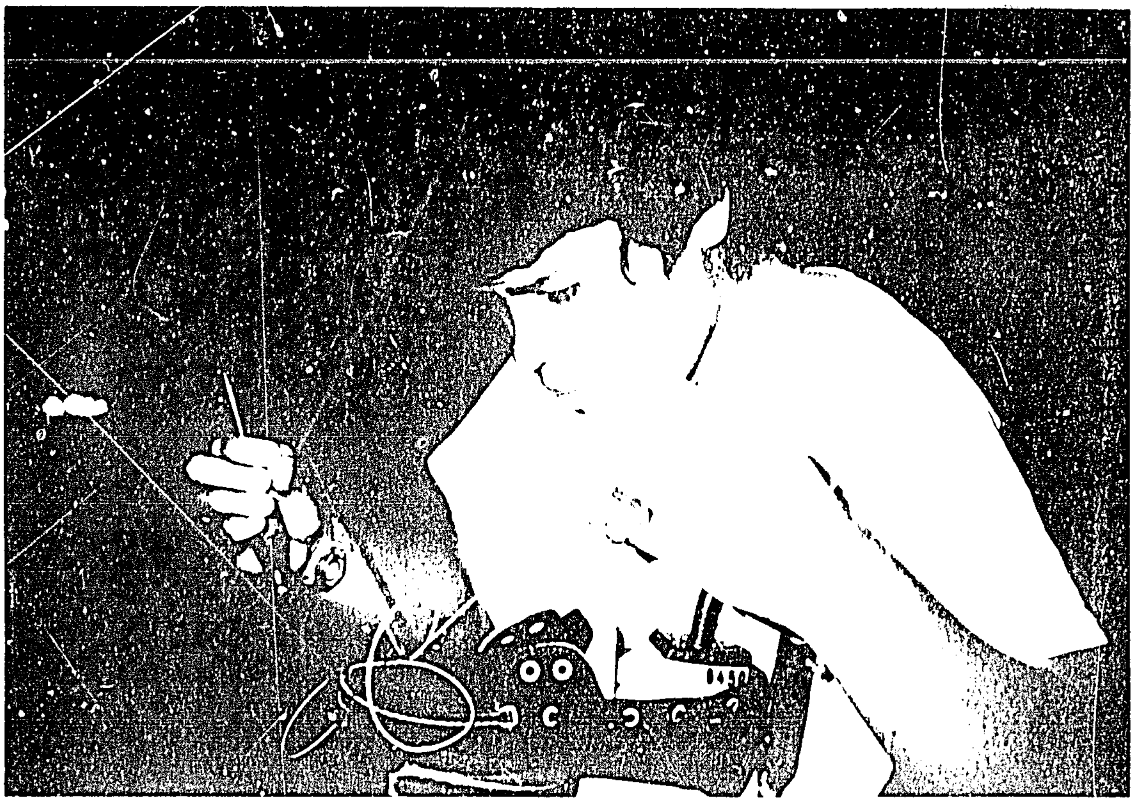
Illustrative examples of
Enterprises Assisted Under the PRIDEX Program

Fabric Handicrafts

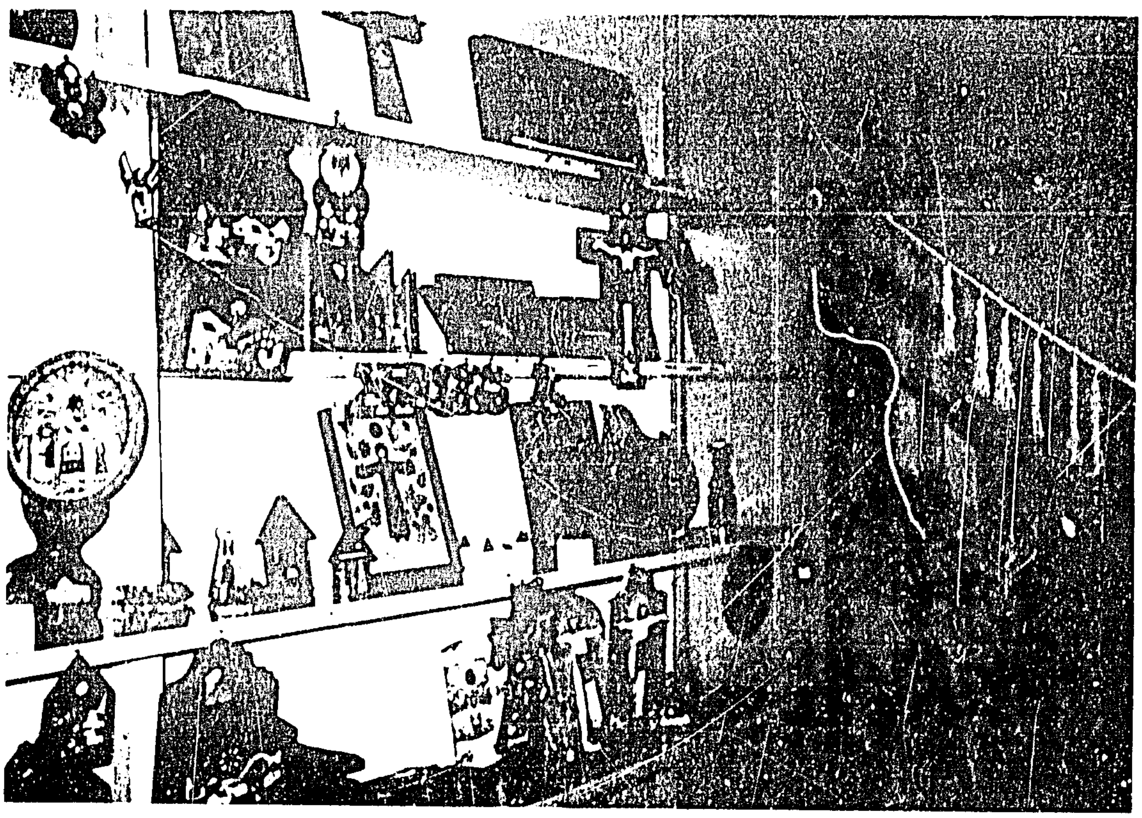


Snack Fools

Garment Factory



Shoe Manufacturing



Wool Handicraft

INVESTMENT FUND PROGRAM (FIDEX)

Background

The Investment Fund Program (FIDEX) was authorized on August 29, 1986, by amendment number three to Cooperative Agreement No. 519-0287.

The project amendment provided $15 million for an Investment Fund and $600,000 to cover the Investment Fund's administration costs. This activity was designed to make available investment credit and equity support to domestic and foreign investors for the purpose of stimulating the establishment of new and expanded "maquila" (assembly work such as contract sewing, electronics, data entry, etc.) operations and light manufacturing/assembly enterprises in El Salvador exporting to markets outside of the Central American Common Market. It is anticipated that the Credit Fund will finance projects identified and developed under the PRIDEX program.

The Investment Fund, however, had not yet been established. Its establishment had taken longer than expected because of the unique problems in establishing an off-shore fund and because of delays experienced in obtaining the necessary A.I.D. approvals. At the end of the audit, it appeared that the trust fund would be established with Citibank in the Bahamas, although changes were still being made to the trust document.

As of September 30, 1987, $15.6 million had been authorized and obligated and $2,633 had been disbursed. The project assistance completion date was September 30, 1989. The not-yet-fully established program was managed by one executive and one secretary. A credit analyst was in the process of being hired.

Program Accomplishments

No credit had yet been provided under the Investment Fund. As a result, this program had not yet had any impact on stimulating investments in El Salvador.

ASSOCIATION STRENGTHENING PROGRAM (FORTAS)

Background

Association Strengthening Program (FORTAS) activities were authorized and financed under two Cooperative Agreements, Project Nos. 519-0287 and 519-0316, which were approved on September 24, 1984 and July 19, 1985 respectively. The program's purpose was to strengthen the ability of private sector business associations to better serve their members. Specifically, the program was to assist associations to provide their members important information, technical advice and general guidance needed to maintain and increase the member's operations and to establish the basis for exporting their member's products.

The program financed a variety of activities designed to strengthen the associations including seminars, training, technical assistance and observational trips outside the country. Project Agreement No. 519-0287 authorized assistance to associations already involved with export activities, while Project Agreement No. 519-0316 authorized assistance to associations not related directly to exports. Agreement No. 519-0287 did not establish any cumulative limit on the amount of funds that could be used to assist the associations, but Agreement No. 519-0316 limits the total cumulative assistance to any one association to $20,000, unless waived by USAID. As of July 1987, FORTAS had six professional and support staff to carry out its activities.

As of September 30, 1987 a total of $2.2 million had been authorized and obligated under the two agreements. Of this amount $884,575 had been disbursed. 1/

The initial project assistance completion date under Agreement No. 519-0287 was September 30, 1987, but had been extended once to September 30, 1989. The initial project assistance completion date under Agreement No. 519-0316 was July 31, 1986, but had been extended three times to December 31, 1987.

1/ Included in the FORTAS authorization was $475,000 for a private sector education foundation (Private Foundation for Educational Development - FEPADE) and $300,000 for a special project to assist El Salvador's eastern region through the Eastern Development Coordination Committee (COMCORDE). On August 31, 1987 A.I.D. signed another Cooperative Agreement (Project No. 519-0336) with FUSADES to provide continuing support to FORTAS through December 31, 1990. The Agreement authorized $1.7 million for FORTAS, but does not take effect until January 1, 1988.

Program Accomplishments

According to FORTAS' records, as of June 30, 1987 the program had provided and/or committed financial assistance totaling $781,135 to 30 associations. These funds financed a range of activities which the audit classified into six categories. These categories and general descriptions are:

(1) Personal Training	Activities aimed at enhancing staff knowledge and skills such as computer courses.
(2) Strengthening Free Enterprise	Forums and courses aimed at reinforcing free enterprise objectives.
(3) Institutional Development	Activities aimed at strengthening the general internal management of the association.
(4) Observational Travel	Trips outside the country for association staff and members. Purpose of trips could encompass elements of other categories.
(5) Assistance to Associations	Activities aimed at resolving specific problems faced by the association and its members.
(6) Special Activities	Support for FEPADE

A breakdown of assistance by these categories follows.

Proj No 519-	1	2	3	4	5	6	Total
0287	$54,041	$ 1,319	$ 88,654	$40,476	$19,758	$ - o -	$204,248
0316	15,886	87,171	111,862	31,861	17,707	312,400	576,887
Total	$69,927	$88,490	$200,516	$72,337	$37,465	$312,400	$781,135

The impact of these activities on strenghtening the associations had not been measured.

SMALL AND MICRO-ENTERPRISES PROGRAM (PROPEMI)

Background

In July 1984, the Salvadoran Foundation for Economic and Social Development proposed to USAID/El Salvador the establishment of a program to assist small-scale entrepreneurs. This proposal culminated in the August 29, 1985 signing of Cooperative Agreement No. 519-0304 which established the Small and Micro-Enterprises Program (PROPEMI). The objectives of the program were to "increase the profitability of, and promote the expansion of small and micro-enterprises in the area of San Salvador, thereby generating employment and fostering economic growth." To accomplish these objectives, the program provides credit and technical assistance to small-scale businesses.

The program conditions the approval of credit upon the entrepreneurs' acceptance of a five-week training program. This training program is aimed at strengthening entrepreneurs' management and accounting capabilities. Loans made under the program were generally in the range of $200 to $4,000 at 15 percent interest for up to 2 years. A maximum grace period of four months on the payment of principal was also common.

As of September 30, 1987 $3 million had been authorized and obligated and $902,052 disbursed. As of July 1987 PROPEMI had 29 professional and support staff to implement its activities. The project assistance completion date is September 30, 1988.

Project Accomplishments

According to PROPEMI records, as of June 30, 1987 the program had provided financial and/or technical assistance to 807 small enterprises in the San Salvador area. However, the program was behind in achieving its planned targets as shown below.

Targets Versus Accomplishments

Objectives	Targets for 1986-1987	Actual Outputs 1/	Percentage Actual/ Target
Loans	761	251	33%
Trainees	1,133	807	71%
New Employment	761	325	43%

1/ As of June 30, 1987.

Program managers claimed the lower-than-planned outputs were partially due to the October 1986 earthquake which affected economic activity and resulted in the availability of government-sponsored disaster relief assistance.

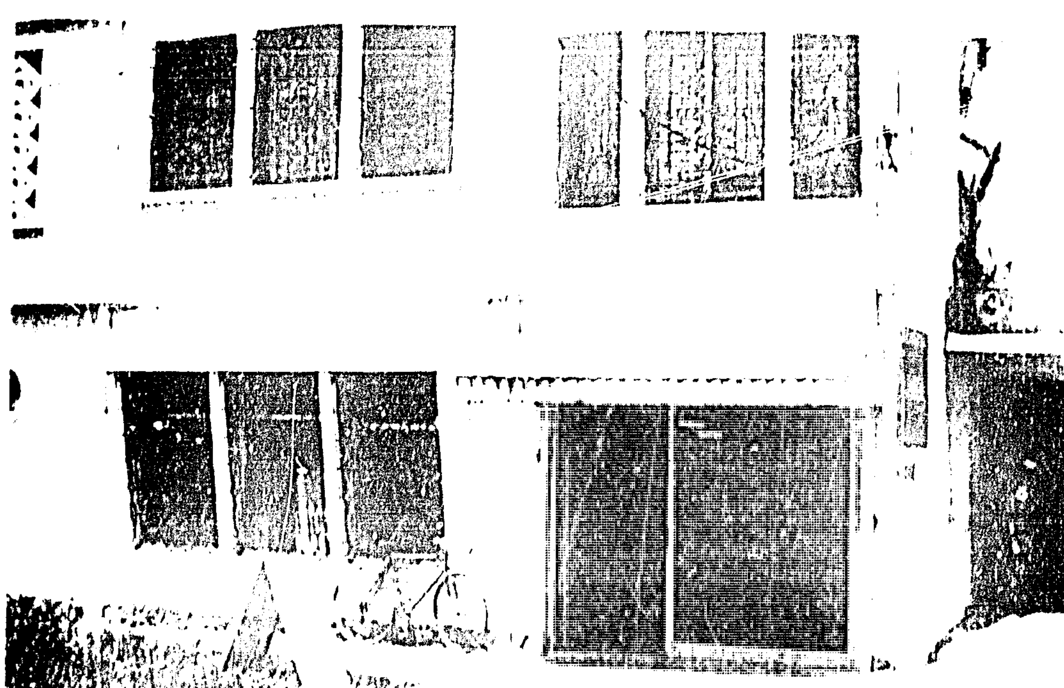
As of June 30, 1987, 225 of the 251 approved loans, totaling $295,930, had been disbursed. Of this amount, $231,765 was still outstanding, and $3,475 (1.5%) of this was considered delinquent over 30 days.

Illustrative Examples of
Enterprises Assisted Under the PROPEMI Program

Vehicle Repair Shop

Barber Shop

Cabinet Making Shop



Tailor Garment Shop

AGRICULTURAL DIVERSIFICATION PROGRAM (DIVAGRO)

Background

Agricultural Diversification Program (DIVAGRO) activities were authorized by Cooperative Agreement Project No. 519-0265, dated January 29, 1985, for the purpose of supporting the activities started under the Government of El Salvador's agrarian reform program. Specifically, the DIVAGRO program sought to expand private sector investment in non-traditional agribusiness enterprises by financing technical assistance, training, feasibility and marketing studies, an agricultural diversification data bank, and research activities on behalf of farmers, farm cooperatives, packing plants and other agricultural export related endeavors.

As of September 30, 1987, $3.8 million had been authorized and obligated. Of this amount $1.7 million had been disbursed. As of July 1987, the program was managed by five professional and support staff. In addition, the program had contracted the long-term assistance of four Chile Foundation (agricultural institution) advisors.

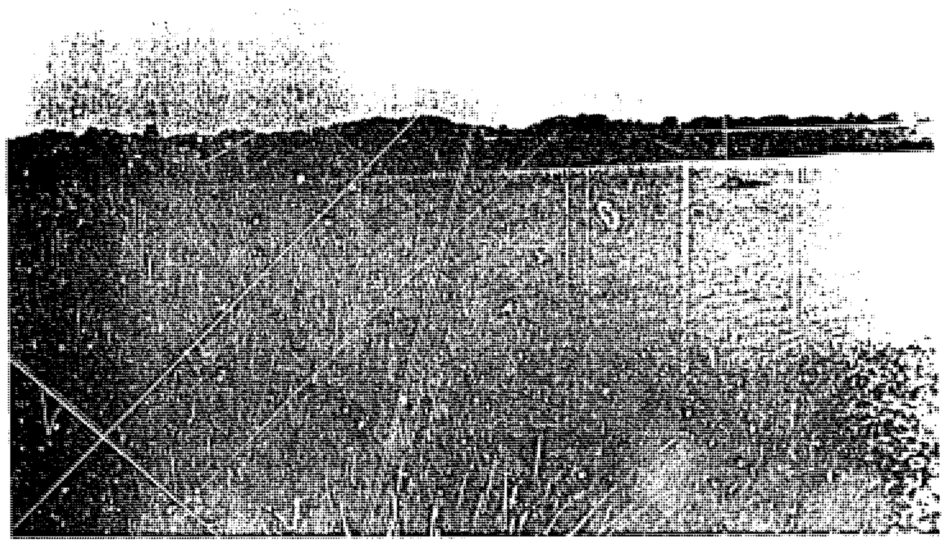
The initial project assistance completion date was December 31, 1986, but had been extended once to July 31, 1988.

Program Accomplishments

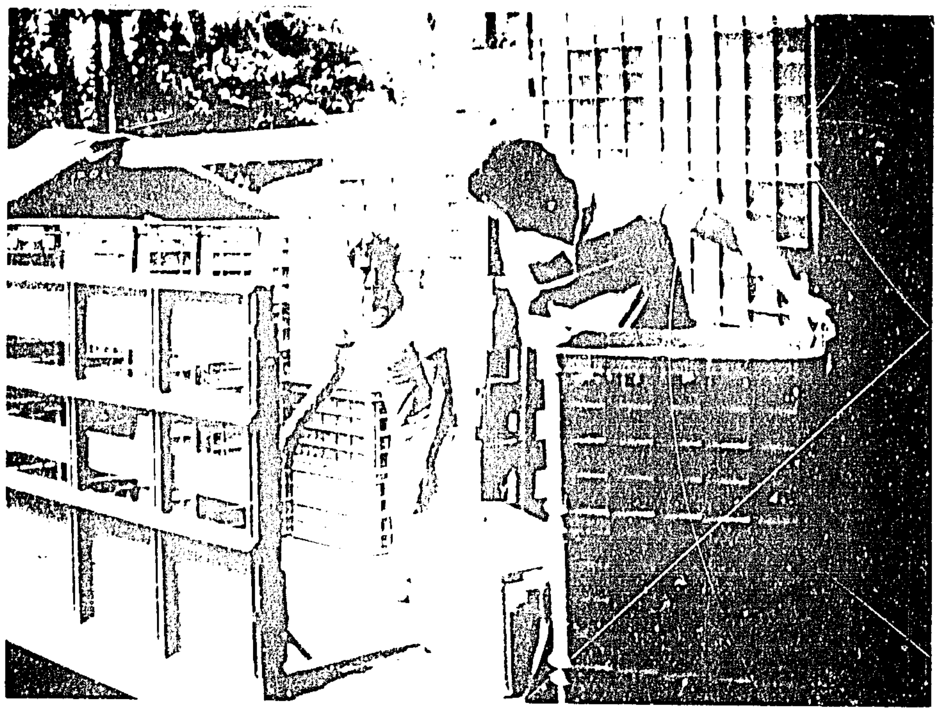
As of June 30, 1987, 20 companies had received technical assistance and feasibility studies had been financed for 12 other enterprises on production of shrimp, Tilapia fish, dairy products, melons and watermelons, vegetables, flowers, ornamental plants, and other crops. In addition, the program financed observation trips for 68 entrepreneurs and program staff to different countries to participate in conferences, fairs, promote their products, and observe first-hand other production, processing and marketing techniques. Furthermore, 342 individuals had visited and learned first-hand about the program's three research experimental farm plots.

According to program reports, these activities had resulted in 120,456 person-work-days and $2.2 million in foreign exchange. As mentioned in the body of this report, some of the program's claims had been exaggerated.

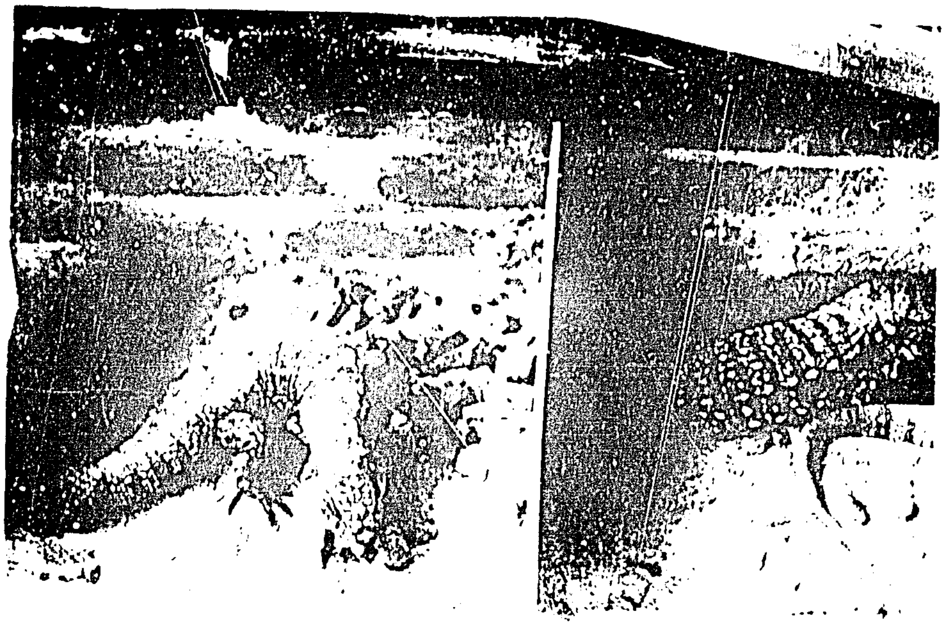
Illustrative Examples of
DIVAGRO Assisted Activities

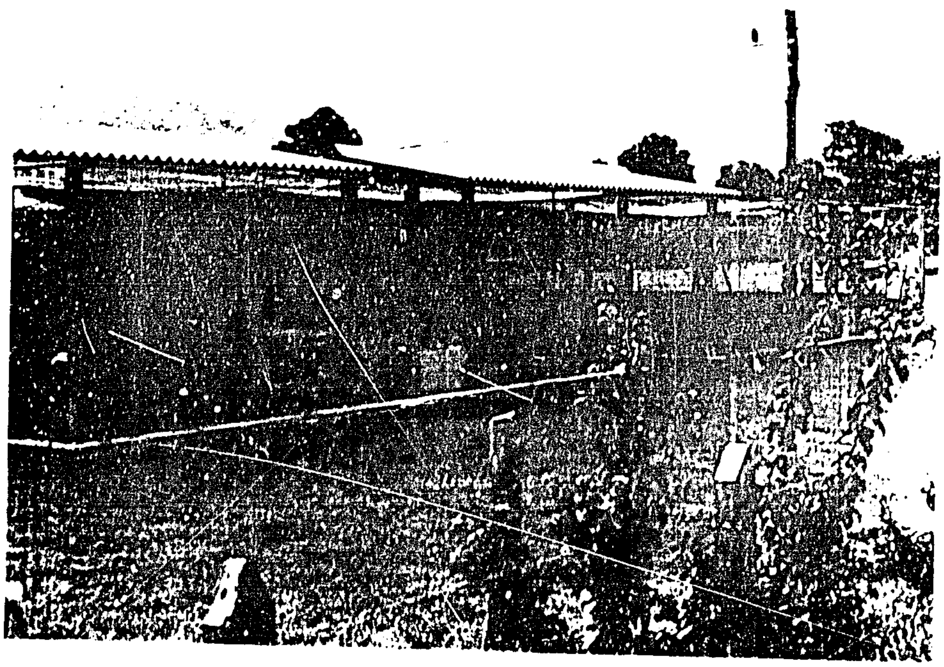


Shrimp Farming

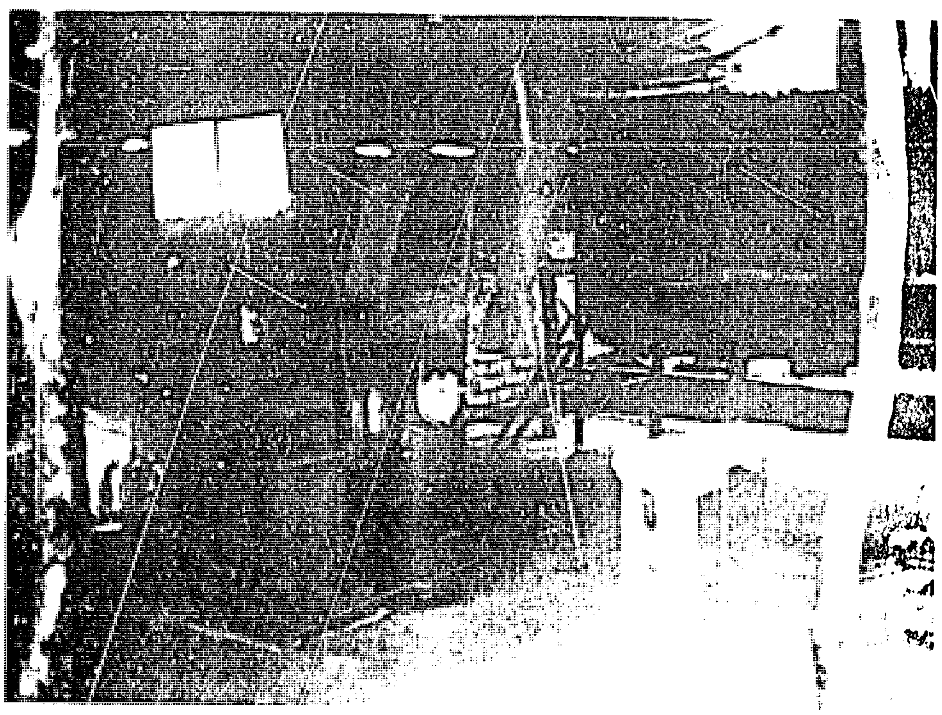


Increase In Vegetable Packing Plant Production





Captive Lizard Breeding Project



Marigold Flower Farm and Processing Plant

WATER MANAGEMENT PROGRAM (RIEGO)

Background

Water Management Program (RIEGO) activities were authorized under Cooperative Agreement Project No. 519-0303 which was approved on August 27, 1985. The program's purpose was to promote through the private sector diversified, irrigated farming with the objective of increasing non-traditional exports, jobs and foreign exchange 1/. Specifically, the program sought to establish a private sector irrigation association to manage the program's technical assistance and $10 million credit fund activities. These activities were aimed at farmers, packers, processors and exporters of labor-intensive, irrigated, non-traditional crops.

The cooperative agreement envisioned that the irrigation association would be established within three months. However, this activity took nearly two years because of the diversified membership requirements established by the agreement. Once the new Irrigation Association (CORPREX) was established on June 1, 1987, additional delays were experienced in interpreting and putting into practice the complex agreement requirements. Numerous program design problems have been identified by program and A.I.D. management which needed to be corrected. As of September 30, 1987, $13.5 million had been authorized and obligated and $761,493 expended. The program was managed by seven professional and support staff.

The initial project assistance completion date was extended once to August 30, 1990.

Program Accomplishments

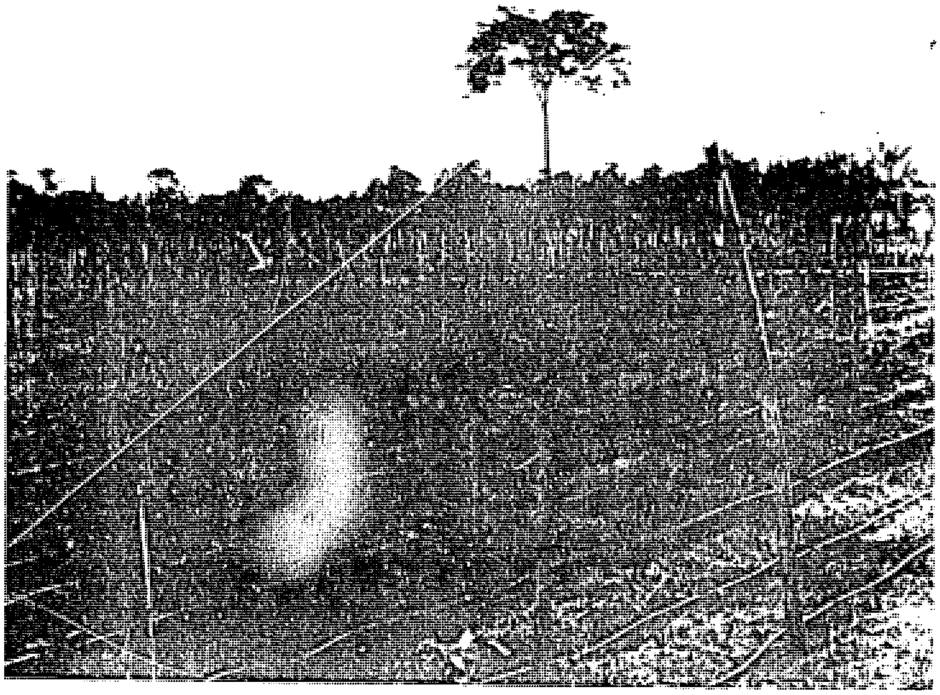
Program implementation was behind scheduled. As of June 30, 1987 only four irrigation projects had been approved and funds disbursed. However, eleven other projects were in the loan approval pipeline with three expected to be funded soon. The total funding for these 15 projects represented $4.7 million. The loans made to date ranged from about $10,000 to $73,500 at 15 percent interest for 1 to 7 years.

In addition to the loan activities, the program had also financed travel for 28 potential irrigation users and program staff to Honduras and the United States to observe irrigation practices and learn about its benefits.

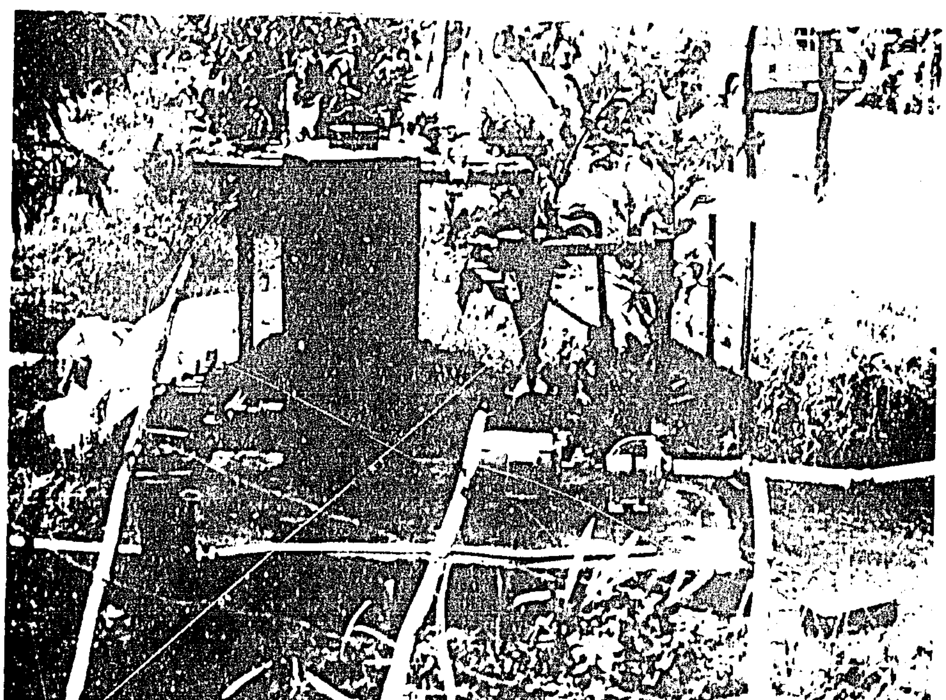
The impact of these activities on increasing exports, jobs and foreign exchange earnings had not been determined.

1/ The cooperative agreement also authorized financial assistance to the Government of El Salvador to promote irrigation-related activities through the public sector.

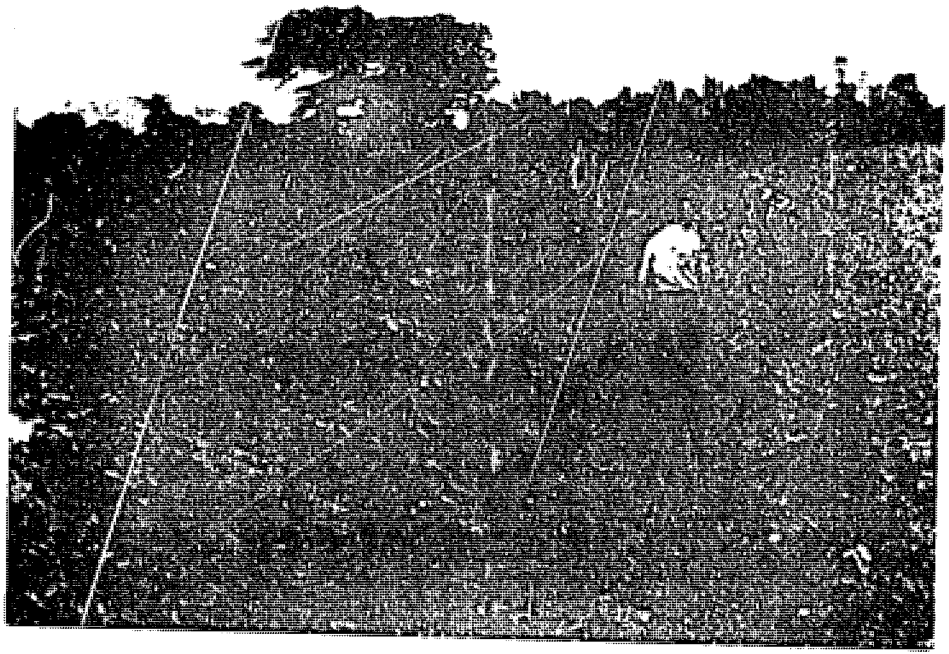
Illustrative Examples of
RIEGO Program Assisted Activities



Drip Irrigation Lines at Tomato Farm



Water Pump and Related Equipment
at Tomato Farm



Expansion of Rose Farm with
Drip Irrigation Technology

AGRIBUSINESS DEVELOPMENT PROGRAM

Background

This is the newest program that USAID/El Salvador will implement through the Salvadoran Foundation for Economic and Social Development (FUSADES). Agribusiness Development Program activities were authorized under cooperative agreement No. 519-0327 which was signed on September 29, 1987. The objective of the program is to increase the production and export of non-traditional agricultural products with the goal of increasing employment and foreign exchange earnings. The program will assist Salvadoran and foreign investors and producer associations to establish and expand Salvadoran business activities related to the production and export of non-traditional agricultural products. The program will provide short and long-term United States and local currency financing, technical assistance and training.

As of September 30, 1987, $20 million had been authorized, of which $10.1 million had been obligated. The project assistance completion date is September 30, 1992.

Project Accomplishments

There had not been any measurable activity under this new program.

UNITED STATES GOVERNMENT

memorandum

APPENDIX 1
Page 1 of 10

DATE: December 14, 1987

REPLY TO ATTN OF: Henry H. Bassford, ~~DIR~~ for

SUBJECT: Mission Comments on Draft Audit Report on Salvadoran Foundation for Economic and Social Development (FUSADES)

TO: Coinage Gothard, RIG, Tegucigalpa

The following comments and suggested revisions to the Draft Audit Report are based on Mission and FUSADES review of the report and its recommendations. Specific quotes from the draft report are underlined and/or in quotation marks.

Before passing on to specific findings, we would like to comment on the overall tone of the report. We would like to see some tonal changes in the language of the final report. An audit report should be objective and present a concise and accurate description of valid findings. We feel that for the most part the auditors have done that. At times, however, the draft report's objective and subtantive narrative drifts off course into a subjective, almost journalistic tone.

We mention this because some of the language in the report is unacceptable for a professionally written document with prospects for as wide a distribution as the document in question. Words and phrases such as: sort of, worse yet, "kickbacks", coercion, had not always, etc., are misleading or too subjective. Subjective, inaccurate, ambiguous language, as well as clearly undocumented allegations, have no place in a serious audit of any institution. For instance, the draft report states (page ii of the Executive Summary) "The audit findings should be understood in the context of the political pressure on USAID/El Salvador to obligate substantial economic and development assistance funds...." What political pressure? The Mission feels no such pressure. This was an erroneous conclusion reached by the auditors. In another paragraph referring to the need for an independent evaluation, (page v of the Executive Summary) the auditors state that, "the major earthquake of....interupted both the Foundation's and the Mission's operations for several weeks." Several weeks? We have yet to recover completely from the effects of the earthquake. Many of FUSADE'S clients have similar problems. Thus, a misleading impression of the obstacles faced by both the Mission and FUSADES on a daily basis is given, and the earthquake is not even mentioned as a part of the context.

In some cases the auditor's determination of the effect of a finding was merely an exercise in speculation of possible future events. Quoting from the Office of Inspector General, Policy and Procedures Handbook, chapter 5 page 3, "The effect describes what resulted from the condition." For example, the effect presented in finding No. 1 (bottom of page 8 of the report), "This could result in an additional cost of about $7 million in direct AID funds to implement project activities." The auditors offer no evidence to support this figure; they offer no objective proof to back up this assertion. How, then, can this statement be set forth as one of the key attributes of this finding?

The Executive Summary of the draft report does not present the Mission's comments. Statements that are fully developed in the body of the report may, when pulled out of context and placed in the Executive Summary, be misleading. Since many readers will only read the Executive Summary, Mission feels that the Summary should present a balanced view. For example, the Executive Summary (page iv) states "In addition, the audit found that program accomplishment data may have been improperly erased from computer memory." The auditors do not mention who was at fault. This leaves the reader with the impression that either the Mission or FUSADES was negligent. The discussion section under finding No 3 (page 19) clarifies who was at fault: "The Foundation wanted to make it clear, however, that the subject data had been compiled while the program was managed by a contractor (Arthur Young and Company). Program officials were unable to reproduce the back-up information from computer storage, as this information had been eraced by the contractor in August 1987 upon completion of the contract."

Another point we would like to bring to the auditor's attention concerns the way in which the Mission's comments are portrayed in the draft report. Throughout the body of the report, under the heading "Management Comments," the Mission's comments are sometimes oversimplified, misinterpreted or misquoted. The Mission would prefer that its comments be presented verbatim and in their entirety, not taken out of context.

Mission feels that the audit contains a sufficient number of valid findings and recommendations to render it a good management tool with respect to showing the Mission and FUSADES where we need to make some mid-course changes in the program, and indeed to correct the deficiencies that the audit pointed out. We would request that the auditors do some serious editing to the draft in order to eliminate all ambiguities from the final report.

EXECUTIVE SUMMARY, page i and Background, page 2

"The Salvadoran Foundation for Economic and Social Development was created in 1983 by a group of about 100 Salvadoran business leaders as a sort of think tank for public policy."

FUSADES was not established with AID assistance, nor as a "sort of think tank". The organization was funded privately and established in 1983 as a private Salvadoran think tank, and was functioning as such when AID stepped in in 1984. AID tapped into a good, ongoing organization. We suggest that the words "sort of" be deleted. The phrase suggests that FUSADES was loosely organized, which was not the case. Furthermore, it sets a negative tone that could prejudice the reader from the onset.

EXECUTIVE SUMMARY, page ii and RESULTS OF AUDIT, page 6

(1) "...planned activities were behind schedule because of implementation delays and their impact on achieving overall program objectives was uncertain."

How many of the planned activities were behind? Was it all of them? A high percentage of them? The wording of this statement implies that all of FUSADES programs were lagging behind. We request that the auditors be more specific in their wording of this finding. If the statement is derived from a sampling of FUSADES activities, then it would be helpful to specify how many activities were examined, and, of the total, how many or what percentage of the activities sampled were behind schedule. With regard to impact on achieving program objectives, use of the word "uncertain" is unfair and not substantiated. The FUSADES programs have achieved real, verifiable results, some of which are remarkable, given FUSADES' youth as an organization and the conditions in El Salvador.

Finding No. 1 p. 9

"There was no assurance that required contributions from project beneficiaries were being used for general project purposes and/or in accordance with general AID policies." (EXECUTIVE SUMMARY, p ii: "Specifically, the audit showed that required contributions from program beneficiaries were not always used for project purposes or in accordance with AID allowable cost provisions....")

18

Mission notes that FUSADES was never required to use contributions from program beneficiaries for project purposes. Specifically, in the original Cooperative Agreement (0287) between A.I.D. and FUSADES, there was no mention made of restrictions on the counterpart contributions. On the contrary, FUSADES was permitted to use these counterpart funds for its own purposes. The draft audit report further states, on p.10, paragraph 1, that contributions from beneficiaries "should be subject to the same allowable cost provisions and A.I.D. policies that govern the use of appropriated funds..." However, the auditors cite no basis for this statement. The Handbooks and Standard Provisions for Non-U.S., Non-Governmental Grantees do not address this issue. The Mission's point is that there was no negligence or inappropriate behavior on the part of FUSADES or the Mission with respect to this issue; the auditors simply have a different point of view.

The RLA was consulted by phone about paragraph 2, p. 10, and she stated that the paragraph is an inaccurate portrayal of her conversation with the auditors. Congressional intent and the indirect financing scheme are the only issues which, to her knowledge, the General Counsel had not addressed. With regard to restricting use of funds, the RLA stated that there are pro's and con's, and that building FUSADES as an institution may be a proper foreign aid objective. Moreover, the RLA stated that there were advantages and disadvantages to restricting the use of these funds for project or program purposes. We discussed the possibility of amending the Cooperative Agreement with FUSADES to clarify the use of these funds, either to contribute to project purposes, or program income to be used for purposes consistent with FUSADES' goals and objectives (perhaps as spelled out in its charter). Finally, <u>the RLA stated that, in her opinion, it is clear that beneficiary contributions are not subject to the same restrictions as USG funds.</u> The Mission has requested that the RLA put this opinion in writing.

A final comment on the language in the middle of page 11. It is inflammatory, unsubstantiated and puzzling. Why are unrestricted beneficiaries' contributions coercive? Also, the use of the word "kickbacks" implies that illicit benefits are being generated. This is an innuendo. The auditors give no examples, offer no proof. The lack of accuracy insinuates guilt where none is established by fact.

The Management Comments to Finding No. 1 (p. 12, paragraph 1) are not an accurate reflection of what was discussed with the auditors at the exit conference. The Mission does not have the same concerns as the auditors with respect to usage of beneficiary contributions. The Mission stated that it believes such funds should be used in a manner consistent with the overall goals and objectives of FUSADES. The foundation's bylaws prohibit use of FUSADES funds for such things as political campaign contributions.

Also, it would not be in AID's interest to restrict the beneficiary contributions to specific projects or programs, because this would increase funding for programs that the Mission is trying to de-emphasize.

Finding No. 2, p. 13

"Implicit in the cooperative agreements, just as in the Foreign Assistance Act requirement on counterpart contributions, is the intent that project beneficiaries be encouraged to contribute as much as possible toward the cost of activities that are designed to benefit them".

A cooperative agreement is a legal document, and as such, nothing that is not spelled out clearly can be upheld, or considered legally or morally binding. Nevertheless, even though not all of the subagreements required the recipients to contribute a minimum of 25 percent of the activity costs, FUSADES attempted at times to obtain the maximum possible. In numerous instances recipient contributions have exceeded 25 percent, and in some cases they have exceeded 65 percent.

As of December 14, 1987, FUSADES contributions from other than the A.I.D. funding sources amounts to a total colon equivalent of US$ 1,122,800. This represents 12.2 percent of total AID disbursements to the Foundation, which amounted to $9,176,226 as of November 30, 1987. This amount cannot be considered "negligible".

It should be noted here that the Mission initially discouraged FUSADES from pursuing a more aggressive policy because of potential inconsistencies with the projects' development objectives and the risk of having FUSADES viewed as out of the reach of the average businessman. With our encouragement, FUSADES is now pursuing a more aggressive policy. We request that the recommendation be deleted.

Finding No. 3, p. 17
Executive Summary

"We recommend that USAID/El Salvador, in consultation with the Foundation: a) establish uniform criteria and a system for measuring and reporting project accomplishments; and b) determine whether or not information eliminated from the Trade and Investment Promotion computer record needs to be replaced and, if it does, ensure that replacement costs are recovered from the Arthur Young management contract."

While we are in complete agreement with this recommendation, the write-up, especially in the Executive Summary, is somewhat misleading. A verifiable tracking system and accurate reporting requirements will be improved. However, many programs do have appropriate reporting systems in place, and, although there could be improvements by establishing uniform methodologies, verifiable results are being achieved. With respect to part b, the Arthur Young contract has not been fully liquidated. FUSADES will make a determination as to fault and responsibility for data loss and proceed accordingly.

FUSADES points out that the Foundation status report that was based on the Arthur Young data constituted only one report of a number of status reports submitted by the Foundation on all of its programs. The wording of the report suggests the problem is bigger than it actually is.

Finding No. 4

"We recommend that USAID/El Salvador establish a plan and timetable to evaluate Foundation program activities before any new AID funded activities are approved."

We agree with this recommendation and have started the process to evaluate many of the programs under FUSADES, starting with PROPEMI and PRIDEX in the second quarter of 1988. The RIEGO program has been evaluated. The Mission feels that independent program evaluations are in FUSADES' and AID's best interests. However, the Mission notes that it has complied with AID's Evaluation Handbook. The Evaluation Handbook (page 20) discusses the pros and cons of outside evaluations, but does not require them.

Recommendation No. 5.

We request that this finding be rewritten or deleted. The text as currently written is misleading and inaccurate; i.e. "USAID/El Salvador had not fully established ...the adequacy of financial activities". To implement what is written "fully establish" is to place an unrealistic burden on a Mission; and moreover, what is written is inaccurate: "that no evidence was in the Controller's Office that the Controller had adequately assessed the Foundation's management capabilities, internal controls, or accounting procedures before obligating funds..." On the contrary, prior to the Mission's granting the Foundation PVO status, the Mission, as required by Handbook 3, reviewed for certification the management and financial capabilities of the Foundation. This determination was based upon certified accounting statements prepared by Peat, Marwick, Mitchell & Co. (PMM). PMM has issued an unqualified opinion every year since FUSADES was organized in 1983.

The audit report states that FUSADES' annual financial statements do not comply with GAO financial reporting standards. While this is an accurate statement, we question if the GAO standards apply. Our reading of the "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision) of the Comptroller General of the United States indicates that private institutions' external auditors are not required to comply with GAO standards in their normal course of making determinations as to the degree or quality of an entity's meeting generally accepted accounting principles. If AID were to directly employ or contract the external auditing firm, we do not disagree that the standards would apply; but such is not the case - these are FUSADES' auditors.

We take strong exception to the implication that the Controller, by relying on US AICPA affiliate unqualified audit statements, may be out of compliance with the Financial Manager's Integrity Act. A very strong emphasis is currently underway by both FM and the RIG in relying more and more on non-Federal auditors reviewing our work to satisfy the FMIA requirements. This Mission has a very good reputation in using US AICPA affiliates in many of our projects. In the present instance, two of the very best in El Salvador--Price Waterhouse and Peat, Marwick, Mitchell--have worked with FUSADES.

Another quote from the draft is related to illustrate that some additional audit work is still necessary to reflect the perceived negative effects on operations. To say "that several Foundation-administered activities were not being separately accounted for by the USAID/Controller because they had not been separately budgeted in the cooperative agreement." appears to us inadequate. What is the implication? What is the negative effect? When FUSADES submits their financial expense reports, they do so in conformity with the Agreement and attach a very detailed breakdown by each component. These are retained by the USAID Controller. The report is presented in a different format, but one which is consistent with the obligation as planned by the project designers.

In light of the above, the statement, "As a result of these weaknesses, the Mission is reported as having inadequate assurances that $75 million . . . would be adequately accounted for and used in accordance with project agreement provisions", is an overstatement. What percentage of Mission accepted costs were found to be unallowable? What sample size supports such a statement? This allegation on the $75 million is without foundation, given that less than $10 million has been disbursed.

Recommendation No. 5 is not adequately supported by the audit. To illustrate:

Recommendation No. 5, Part a	"We recommend that USAID/El Salvador a) schedule a non-federal audit of the Foundation's financial management capabilities;"

Part a) would require the Mission to schedule a non-Federal audit of the Foundation's financial management capabilities. We have it. The Mission directly contracted Price Waterhouse in February 1986 to prepare five management operations manuals, with the assistance of USAID/El Salvador. These manuals were completed in June 1986. Significant work by the Foundation, the Private Sector Division and the Controller's Office went into these manuals before acceptance. FUSADES requested PMM to perform an operational audit of the Foundation's implementation of their new manuals. PMM's findings are currently being implemented. Attached is PMM's management letter, dated August 20, 1987.

Recommendation No. 5, Part b — "... require that the annual audited financial reports provide more detailed information on each Foundation program and comply with General Accounting Standard;"

Part b) is not consistent with the GAO Standards. GAO standards must be followed by Federal auditors for audits of Federal organizations, programs, activities, functions, and funds received by contractors, nonprofit organizations, and other external organizations. In addition, legislation further states that Inspectors General should insure that any work performed by non-Federal auditors of Federal organizations, programs, activities and functions complies with these standards. Thus, we would have no problem in requiring the application of GAO Standards if AID were to contract for a non-Federal audit. However, these standards do not apply to a private entity's external auditors. Refer to Chapter 1 of the GAO Standards.

Recommendation No. 5, Part c — "... ensure that Project No 519-0287 activities related to Foundation administration, PRIDEX and DEES are separately budgeted and account for;"

PRIDEX and DEES, with values of roughly $3 and $1 million respectively, are accounted for and reported separately by the Foundation. Mission guidance is found in Chapter 13, Controller Guidebook; it is contemplated that "each project obligating document generally sets forth a financial plan or budget detailed to the major elements of a project." It is against this single budget that all project costs are limited to and charged. The attached supporting detail supplied by the Grantee monthly provides the initial basis needed for any analysis required for the Mission's proper determination of costs. Examples of monthly detailed expense reports are attached.

Recommendation No. 5, Part d

"... determine if severance payments to employees who continue their employment with the Foundation are being made in accordance with Salvadoran law and AID's standard rules on allowable expenditures and, if not, recover those amounts incorrectly paid."

Severance pay is considered a valid question and has been questioned by the Mission previously. Mission has been provided with two legal opinions that confirm that the payment of severance pay, as formally established by FUSADES AID approved policies, is in full accordance with Salvadoran law. In addition, our review of OMB Circular A-122 indicates severance pay, under present circumstances, is an allowable cost. We do not consider this issue to be a problem. The legal opinions are attached.

NOTE: The Mission requested this audit from the RIG as a management tool in and of itself to add to our previously established assurances of FUSADES' financial management capability. The audit implies we had no assurances of FUSADES' capability before we obligated funds. This was not accurate. The audit recommends a non-Federal audit of FUSADES' management capability. We have a management letter from a US AICPA affiliated auditing firm addressing the specific issue. Managerially speaking, something is lacking here. Are we attacking the real cause of the cited deficiency properly? Would a funds accountability audit by a non-Federal auditor be the better course of action? If so, would it be cost-beneficial? Did the RIG find material weaknesses in FUSADES' accounting to warrant such an action at this time? What period of time should the audit cover? Could the RIG assist in assuring the non-Federal funds accountability audit's quality, assuming the Mission could find the necessary financial resources? Could the task be accomplished within the next six months? As answers to these questions require resolution, is this section really applicable? Does the audit seriously suffer by deletion of this section?

One additional item not heretofore mentioned is "USAID funds were generating interest on long-term deposits." Please change to short-term deposits. Also, please note that FUSADES has paid the U.S. Treasury all interest earned as of September 30, 1987. Copy of FUSADES check attached.

Other Pertinent Matters:

"Second" - The Foundation did not consider that it was in violation of Salvadoran law when it bought dollars on the on the "extra-bank" market. There is no recognized black market per se in El Salvador. However, Mission and FUSADES prefers not to have even the hint of impropriety attached to the Foundation. Therefore, FUSADES policies are being amended to stop the practice.

"Third" - The origin of funding for FUSADES printed material is common knowledge. However, we ask the auditors to consider the country's situation, specifically as it relates to "Yanqui" influence. It is simply preferable to maintain a low profile in certain elements of our activities. Moreover, the independence of FUSADES judgement could be called into question, as well as the AID position on sensitive policy issues.

"Fourth" - The audit contends that the Foundation practiced age discrimination in its employment practices which is inconsistent with the Age Discrimination Act of 1975. According to the Standard Provisions for Non-U.S., Nongovernmental Grantees, Page 9, Article 8, entitled Nondiscrimination in Federally Assisted Programs (Nov. 84) "No person in the United States, consistent with the laws of the United States, shall be excluded from participation in the benefits of, or be otherwise subjected to discrimination under any program or activity funded by this grant on the basis of race, color, national origin, age, handicap, or sex." There is nothing ambiguous in the above statement. It clearly does not refer to soverign foreign countries. However, a breakdown of FUSADES employees will show that there has been no discrimination on any basis. The total employee roster numbers 113, of these 52 are women, a number of them holding executive level positions; employees over age 35 total 39 and 5 are under age 25. FUSADES also does not practice a forced retirement at age 65 policy. In any event, FUSADES has agreed to stop references to age in its employment advertising.

"Fifth" - The Foundation has not established a reserve for bad debts in its PROPEMI program. We feel that this is a good finding. PROPEMI will take steps to establish a reserve fund. FUSADES points out that this was not taken into consideration before because PROPEMI's bad debt rate is 1% of the total loan portfolio.

"Sixth" - Whether the scheme has propriety or not, the Mission disagrees with the practice, and has advised FUSADES that, where there is an established employer-employee relationship, incorporation to reduce one's income tax is not acceptable to AID, and payments to such corporations will not be considered as allowable project costs. We agree with the audit that this is a particularly sensitive issue, and have begun to take corrective actions, i.e. that FUSADES has been formally notified that such costs will not be allowed, that financial analysts will begin to examine each corporation to test for the employee-employer relationship, that FUSADES manuals will be amended to reflect this audit observation and the Mission's position, and that an independent legal opinion will be contracted.

"Seventh" - AID has taken steps to insure that the three program vehicles assigned to FUSADES managers have been reassigned.

List of Report Recommendations

Recommendation No. 1

We recommend that USAID/El Salvador obtain FUSADES' agreement to use beneficiary contributions for project purposes only or obtain a formal Agency General Counsel legal opinion showing why the use of these monies should not be restricted.

Recommendation No. 2

We recommend that USAID/El Salvador, in consultation with the Foundation, establish a more aggresive participatory funding policy which better recognizes the extent of assistance provided, the project beneficiaries' financial ability to pay, and the purposes of the project.

Recommendation No. 3

We recommend that USAID/El Salvador, in consultation with the Foundation:

a) establish uniform criteria and a system for measuring and reporting project accomplishments; and

b) determine whether or not information eliminated from the Trade and Investment Promotion computer record needs to be replaced and, if so, ensure that replacement costs are recovered from the management contract.

Recommendation No. 4

We recommend that USAID/El Salvador establish a plan and timetable to evaluate Foundation activities before any new A.I.D.-funded activities are approved.

APPENDIX 3

REPORT DISTRIBUTION

	No. of Copies
Director, USAID/El Salvador	5
AA/LAC/EN	2
LAC/CAP	1
LAC/DR	1
LAC/DP	1
LAC/CONT	1
LAC/GC	1
LAC RLAs	1
GAO Panama Branch	1
AA/M	2
S&T/AGR	1
S&T/PO	1
PRE/PPR	1
PRE/I	1
GC	1
LEG	1
M/FM/ASD	3
PPC/CDIE	3
AA/XA	2
XA/PR	1
IG	1
AIG/A	1
IG/PPO	2
IG/PSA	1
IG/LC	1
IG/EMS/C&R	12
IG/I	1
RIG/I/T	1
Other RIG/As	1