AUDIT OF A.I.D. ASSISTANCE TO THE GOVERNMENT OF EL SALVADOR FOR EARTHQUAKE RELIEF, REHABILITATION AND RECONSTRUCTION DURING FISCAL YEAR 1987

AUDIT REPORT NO. 1-519-88-12
April 14, 1988

AGENCY FOR INTERNATIONAL DEVELOPMENT

S. MAILING ADDRESS
RIG/T
APO MIAMI 34022

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

TELEPHONES
32-9947
[illegible]

April 14, 1988

MEMORANDUM

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

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

SUBJECT: Audit of A.I.D. Assistance to the Government of El Salvador for Earthquake Relief, Rehabilitation and Reconstruction During Fiscal Year 1987

The Office of the Regional Inspector General for Audit/Tegucigalpa has completed its audit of A.I.D. assistance to the Government of El Salvador for Earthquake Relief, Rehabilitation and Reconstruction During Fiscal Year 1987. Five copies of the audit report are enclosed for your action.

The draft audit report was submitted to you for comment and your comments are attached to the report. The report contains five recommendations. Recommendation No. 5 is considered closed and requires no further action. Recommendations 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 Nos. 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.

Encl. A/S

EXECUTIVE SUMMARY

On October 10, 1986, a major earthquake struck San Salvador, the capital of El Salvador, killing or injuring over 21,000 people and damaging infrastructure such as hospitals, housing, roads, schools, and utilities. Despite severe damage to the Embassy and A.I.D. complexes, the Mission in El Salvador responded quickly, and the U.S. Government ultimately committed itself to provide $137 million in assistance during fiscal year 1987.

The omnibus Continuing Resolution for fiscal year 1988 contained a provision requiring the Office of the Inspector General, A.I.D., to provide a detailed accounting, no later than April 15, 1988, to the Committees on Appropriations of the uses of funds made available to El Salvador during fiscal year 1987 for earthquake relief, rehabilitation and reconstruction. In response, the Regional Inspector General for Audit, Tegucigalpa performed this limited-scope program results and financial/compliance audit of funds obligated, advanced and expended by USAID/El Salvador for earthquake relief, rehabilitation and reconstruction during fiscal year 1987. This will be supplemented by a detailed financial/compliance audit currently being conducted by Price Waterhouse in El Salvador. That report is scheduled to be completed in July 1988.

The objective of our program results audit was to selectively verify accomplishments under the Emergency Shelter Support Project as of April 30, 1987 and under the Earthquake Recovery Program which ended on January 20, 1988. The objectives of our financial/compliance audit, which covered International Disaster Assistance expenses liquidated by USAID/El Salvador as of September 30, 1987 were to determine: (1) whether A.I.D. obligations, advances and expenditures were properly accounted for by USAID/El Salvador and the Government of El Salvador, and (2) whether the funds expended were supported by adequate documentation and were used in accordance with established eligibility and procurement criteria.

USAID/El Salvador had effectively managed U.S. Government resources made available to El Salvador for earthquake relief, rehabilitation and reconstruction during fiscal year 1987. The United States responded quickly to the earthquake with substantial quantities of food and emergency relief supplies (worth $3,502,600). USAID/El Salvador supported the relief effort with the services of its own direct-hire and contractor personnel. Effective controls were established by using A.I.D.-financed contractors to account for the receipt and distribution of relief supplies.

Emergency relief assistance was quickly followed by two USAID/El Salvador grants totaling $50,300,000. First, an Emergency Shelter Support project for $300,000 started on October 25, 1986 and terminated on April 30, 1987. And second, an Earthquake Recovery Program for $50 million began on November 21, 1986 and ended on January 20, 1988 (see Exhibits 1 and 2 for a detailed accounting).

In general, the objectives of these projects (to provide funds for temporary shelter, employment, slum rehabilitation, restoration of public services and loans for damaged homes and businesses) were successfully accomplished (see Appendices 4, 5 and 6). Under the Emergency Shelter Support project, between 3,780 and 5,040 families received A.I.D.-financed building materials. Under the Earthquake Recovery Program, 897,206 person-days of work were generated in order to remove 114,608 cubic meters of rubble; 2,299 loans were made to micro or small businesses to repair or replace buildings, machinery, equipment, inventories and working capital; 36,124 families received A.I.D.-financed building materials for the construction or repair of temporary shelters; 26 small, medium-size and large infrastructure subprojects were completed in slum areas to help relocate families and to repair or reconstruct civil works such as retaining walls and drainage structures; 7,195 loans were made to repair or reconstruct houses; and 63 public service restoration activities were completed by 14 Government of El Salvador agencies.

Except as noted in the body of this report, we found that, in general, USAID/El Salvador had properly accounted for International Disaster Assistance expenses liquidated in fiscal year 1987; the funds expended were supported by adequate documentation and had been used in accordance with established eligibility and procurement criteria.

One objective was to disburse funds quickly in order to speed assistance to needy earthquake victims. As a result, some funds were not used in accordance with beneficiary eligibility criteria, particularly under two credit lines established under the Earthquake Recovery Program. Considering the speed with which these two projects were implemented, however, we found that they had been relatively well-managed. As implementation problems were identified, USAID/El Salvador moved quickly to correct them without curtailing unnecessarily the flow of A.I.D. assistance to earthquake victims.

The program's credit component was intended to assist low- and middle-income home owners and micro and small businesses affected by the October 10, 1986 earthquake. Loan amounts were to be commensurate with the amount of damages. An undetermined amount of funds were loaned to individuals who did not qualify for program benefits, were used for ineligible purposes and/or were approved without adequate support or justifying documentation. The Mission had identified some of these loans and was taking corrective actions. However, it had yet to identify the full extent of inappropriate uses of credit funds and take final corrective actions. Irregularities occurred because program criteria lacked specificity and because the lending institutions generally lacked the time and resources to verify fully beneficiary eligibility and proposed fund uses. These program weaknesses were generally corrected during program implementation and appear to have been avoided in the follow-on Earthquake Reconstruction Project. Nonetheless, because of these initial weaknesses, more program irregularities occurred than otherwise would have, thus reducing the availability of funds to the target group. We recommended the ineligible loans be identified and

resolved. The Mission concurred that the home and business credit lines needed to be more fully examined; however, it was undecided as to the most cost-effective approach to achieving this objective. The recommendation remains open.

Neither USAID/El Salvador nor the Government of El Salvador had current information on the status of earthquake recovery loan reflows. Program guidelines required participating financial institutions to establish a special section to manage and recover loans and to report quarterly on the amount of loan balances and recoveries. The institutions had not complied with these requirements because, apparently, they were not fully aware of them and/or lacked the resources to comply with them. Furthermore, until our audit, the cognizant Salvadoran implementing agency had not routinely requested information on reflows. As a result, important information on participating institutions' loan recovery performance, delinquencies, and existing balances remained unknown. The lack of such information impeded effective management of the credit program. We recommended that it be collected on a regular basis. The Mission agreed and had already taken action to implement the recommendation.

The Government of El Salvador's portion of home and business loan reflows had not yet been deposited into a special account nor had their uses been determined. As of our audit, the reflows amounted to nearly $2.7 million. After deducting the institution's share of the interest earned on the loans, the amount available for deposit was nearly $2.2 million. Program guidelines required the financial institutions to deposit loan reflows (principal and two percent interest) into a special account at the Central Bank within 180 days of collection. The program envisioned that these reflows would be used for similar credit activities. No deposits had been made because: (1) the Secretariat for External Financing had only just recently established an account for the reflows; (2) the Secretariat and USAID/El Salvador had not yet formally established plans on how all these funds would be used, and, (3) neither the Secretariat nor the USAID had expected significant reflows during the first year. As a result, a substantial amount of loan reflows had been retained by the participating institutions and had not been made available for similar credit activities. We recommended that the reflows be deposited promptly and that plans be developed for their use. The Mission agreed and had already taken steps to comply with the recommendation.

Finally, we found that appropriated U.S. dollars may have been obligated or used for activities associated with the earthquake contrary to project and legislative requirements. Also, the separate accounting records mantained by USAID/El Salvador for $36,957 in funds obligated under the Office of Foreign Disaster Assistance and Ambassador's Relief grants were incomplete.

In response to the draft audit report USAID/El Salvador (the Mission) made the following statement:

The draft audit report as written still contains a few inaccuracies, faulty cause-effect relationships and conclusions reached which are inaccurate and misleading to the uninformed reader. The Mission's comments contained herein are directed at correcting those technical errors and conclusions. The Mission commends the spirit of collaboration on the part of RIG/A/T in assisting the Mission to achieve its goals, and accurately portraying a detailed accounting as mandated by Congress.

The benefits of the experience in the preceeding phases of the $50 million earthquake reconstruction process, rescue, relief and recovery and the constructive recommendations of this audit have enabled the Mission to begin the $75 million reconstruction phase with a better understanding of the institutional capacity of the agencies involved and has permitted the refinement of the procedures used in the highly successful previous efforts which are now concluded.

In preparing this audit report, we considered USAID/El Salvador's comments, which are contained in Appendix II.

Office of the Inspector General

AUDIT OF A.I.D. ASSISTANCE
TO THE GOVERNMENT OF EL SALVADOR
FOR EARTHQUAKE RELIEF,
REHABILITATION AND RECONSTRUCTION
DURING FISCAL YEAR 1987

TABLE OF CONTENTS

		Page
PART I	- INTRODUCTION	1
	A. Background	1
	B. Audit Objectives and Scope	4
PART II	- RESULTS OF AUDIT	7
	A. Findings and Recommendations	9
	1. Inappropriate Credit Line Disbursements Need to Be Resolved	9
	2. More Information Is Needed to Better Manage Credit Line Reflows	14
	3. Credit Line Reflows Need to Be Deposited into a Special Program Account and Their Uses Determined	17
	4. Appropriated U.S. Dollars May Have Been Obligated or Used for Activities Associated with the Earthquake Relief Effort Contrary to Authorized Project or Legislative Requirements	21
	5. Accounting Records for the Office of Foreign Disaster Assistance and Ambassador's Relief Grants Needed to Be Updated	25
	B. Compliance and Internal Controls	28
	1. Compliance	28
	2. Internal Controls	28
	C. Other Pertinent Matters	29
PART III	- EXHIBITS AND APPENDICES	
	A. EXHIBITS	
	1. Earthquake Recovery Program (519-0331) USAID/El Salvador Financial Statements as of September 30, 1987	

2. Earthquake Recovery Program (519-0331) SETEFE Financial Statements as of September 30, 1987

3. Accounting for Other A.I.D. Funds or Commodities Obligated or Used for Activities Associated with the Earthquake during Fiscal Year 1987

4. Analysis of Audit Coverage of U.S. Government Assistance Provided to El Salvador in Response to the Earthquake during Fiscal Year 1987

B. APPENDICES

1. Photographs of Damage Caused by the Earthquake of October 10, 1986

2. Accomplishments of OFDA Emergency Relief Program

3. Accomplishments of PL 480 Title II Emergency Food Distribution Program

4. Accomplishments of El Salvador Earthquake Recovery Program (Project No. 519-0331)

5. Accomplishments of Emergency Shelter Support (Project No. 519-0330)

6. Photographs of Facilities Repaired or Reconstructed with Funds Provided under the El Salvador Earthquake Recovery Program (Project No. 519-0331)

7. Accounting for International Disaster Assistance Funds Made Available to USAID/El Salvador during Fiscal Year 1987

8. Eligibility of Expenditures for International Disaster Assistance Funds Made Available to USAID/El Salvador during Fiscal Year 1987

9. Acceptability of Procurement Transactions for El Salvador Earthquake Recovery Program (Project No. 519-0331) and Temporary Shelter Support (Project No. 519-0330)

10. Summary of Inelegible Credit Disbursements Under the El Salvador Earthquake Recovery Program (Project No. 519-0331)

11. Mission Comments

12. List of Report Recommendations

13. Report Distribution

AUDIT OF A.I.D. ASSISTANCE TO THE GOVERNMENT OF EL SALVADOR FOR EARTHQUAKE RELIEF, REHABILITATION AND RECONSTRUCTION DURING FISCAL YEAR 1987

PART I - INTRODUCTION

A. Background

At 11:49 a.m. on October 10, 1986, a major earthquake that lasted 6 seconds and measured 5.4 on the Richter scale struck San Salvador, the capital city of El Salvador. Despite its brevity, the earthquake caused significant damage because of its location directly beneath the city, its shallow depth and its unusually high accelerations (vertical movements). Approximately one third of San Salvador's 1.5 million inhabitants were affected by the earthquake. About 1,100 people died, 20,000 were injured and 250,000 to 300,000 suffered serious damage to their homes.

The quake caused massive damage to infrastructure, particularly in a twenty-square-block downtown area (see Appendix 1 for photographs of earthquake damage). Damage has been estimated at up to $2 billion. The housing, particularly low income housing, suffered severe damage resulting in loss of shelter for thousands of families. About 23,000 units were destroyed and 30,000 severely damaged. Damage to schools was extensive. Approximately 2,000 of the city's classrooms were destroyed or seriously damaged. Five hospitals, nine health units and numerous private clinics were severely damaged. The damage to the road network in the metropolitan area was considerable. Vital public services were curtailed because of the damages to telephone, electrical and water systems. The flow of government services was interrupted as 176 major buildings (both private and public) were destroyed. The commercial sector suffered heavy losses resulting from total to partial destruction of buildings, equipment and inventories.

The earthquake also affected USAID/El Salvador operations. Because of damages to the U.S. Embassy and A.I.D. office buildings, USAID/El Salvador temporarily had to move its offices for up to six weeks to its guest house and private homes without telephone service. Much of the radio and telex equipment in the U.S. Embassy was damaged, making communications with Washington difficult. The Mission computer system was damaged and many records were not accessible. A.I.D. and Embassy officials began working long days -- up to 18 hours or more, six to seven days a week -- to compensate for the lack of facilities and to assist in the relief effort.

In response to the earthquake, the U.S. Government, through A.I.D., committed itself to provide nearly $137 million for El Salvador in fiscal year 1987 as follows:

Type of Assistance	Amount
Emergency Relief	$ 2,900,000
PL 480 Title II Commodities	902,600
Earthquake Recovery Program	50,000,000
Earthquake Reconstruction Project	75,000,000
A.I.D/GOES Programed Local Currencies	2,239,768
Other A.I.D. Projects and Activities	5,775,930
	$136,818,298

A.I.D.'s Office of Foreign Disaster Assistance (OFDA) financed $2.9 million in emergency relief assistance during the first two weeks following the earthquake as detailed below:

October 12, 1986 - the U.S. Ambassador authorized $25,000 for the local purchase of relief supplies by USAID/El Salvador.

October 15, 1986 - A.I.D. authorized $25,000 (Project No. 519-0330) for the local purchase of food, cooking utensils, emergency relief supplies and equipment by USAID/El Salvador.

October 23, 1986 - USAID/El Salvador granted $300,000 (Project No. 519-0330 for Emergency Shelter Support) to the Municipality of San Salvador for the purchase and delivery of corrugated roofing, lumber and nails to 5,240 families who needed temporary shelter.

OFDA also provided $2,550,000 in commodities (such as tents and blankets), transportation services and personnel to support the Government of El Salvador (GOES) relief effort.

In addition to the foregoing, PL 480 Title II commodities stored in El Salvador and Guatemala valued at $902,600 were used in a GOES emergency food distribution program. The U.S. Government agreed to replace these commodities.

On November 21, 1986 A.I.D. granted the GOES $50 million for the El Salvador Earthquake Recovery Program (Project No. 519-0331) from International Disaster Assistance funds specifically appropriated on October 18, 1986 by the U.S. Congress. The purpose of the project was to assist the GOES in meeting basic human needs and reviving economic activity in the areas severely affected by the earthquake. The official GOES representative for the project was the Ministry of Planning. The Ministry, through its Technical Secretariat for External Financing (SETEFE), was responsible for controlling disbursements and accounting for program funds. The project was to be completed by November 20, 1987 but was extended to January 20, 1988. As of September 30, 1987 the program's budget and expenditures consisted of the following (see Exhibits 1 and 2 for more details):

Component	Budget	Expenditures a/
1) Employment Generation/Rubble Removal	$ 2,200,000	$ -
2) Micro/Small Business Credit	10,000,000	5,992,434
3) Temporary Shelter	4,460,000	3,709,879
4) Slum Rehabilitation	3,340,000	-
5) Home Repair/Reconstruction Credit	21,562,078	13,606,399
6) Restoration of Public Services	8,437,922	178,444
	$50,000,000	$23,487,156

a/ Expenditures are defined as A.I.D. direct payments or reimbursement for, or liquidation of advances against payments made for, items received, services rendered, expenses incurred, assets acquired and construction performed before October 1, 1987.

On January 5, 1987 USAID/El Salvador contracted Lopez Salgado and Company (affiliated with Price Waterhouse) for a cumulative cost of $291,157 to provide management consulting and monitoring services for the implementation of the $50 million Earthquake Recovery Program.

On September 24, 1987, A.I.D. granted the GOES $75 million for an Earthquake Reconstruction Project (No. 519-0353). Its purpose is to assist the government and private sector of El Salvador to reconstruct and rehabilitate housing, vital social infrastructure and businesses as well as to restore basic services to persons, particularly those of lower income, affected by the October 10, 1986 earthquake. The project is to be completed by September 30, 1990.

Additionally, $2,239,768 from A.I.D./GOES jointly programed local currencies and $5,775,930 from other USAID/El Salvador projects and accounts were obligated or used for activities associated with the earthquake. For example, many A.I.D. contractors whose work was interrupted by the earthquake were directed to support the emergency relief effort, temporarily postponing contract goals. Included in the $5,775,930 cited above is $421,409 in commodities that were procured under the Public Services Restoration Project (519-0279) to repair damages caused by the earthquake.

In March 1987 A.I.D.'s Regional Inspector General for Audit in Tegucigalpa (RIG/A/T) recommended that a public accounting firm be contracted to make a non-Federal audit under IG supervision of the $50 million Earthquake Recovery Program to assess the financial integrity of the program's various components as they were completed. On January 22, 1988 USAID/El Salvador contracted Price Waterhouse for the non-Federal financial/compliance audit of the program. The estimated completion date of this audit is July 22, 1988.

B. Audit Objectives and Scope

The omnibus Continuing Resolution for fiscal year 1988 (which was approved on December 22, 1987) contained a provision requiring the Office of the Inspector General, A.I.D., to provide a detailed accounting, no later than April 15, 1988, to the Committees on Appropriations of the uses of funds made available to El Salvador during fiscal year 1987 for earthquake relief, rehabilitation and reconstruction.

The Regional Inspector General for Audit, Tegucigalpa performed a limited-scope program results and financial/compliance audit of funds obligated, advanced and expended by USAID/El Salvador for earthquake relief, rehabilitation and reconstruction. Our audit scope was limited to the audit objectives and A.I.D.-financed activities stated in this report in order to satisfy the congressionally mandated audit request before the reporting deadline.

The objective of our program results audit was to selectively verify accomplishments under the Emergency Shelter Support Project (519-0330) as of April 30, 1987 and under the Earthquake Recovery Program (Project 519-0331) as of January 20, 1988.

Our financial/compliance audit covered International Disaster Assistance funds obligated, advanced and expended by USAID/El Salvador as of September 30, 1987. This effort is being supplemented by a non-Federal (CPA) audit of the Earthquake Recovery Program to be completed in July 1988, under the supervision of our staff. Obligations audited were $50,336,957, advances were $44,758,725 and expenditures were $23,742,736, as follows:

Activity	Obligations	Advances	Expenditures
Ambassador's Relief Grant (OFDA funds)	$ 11,970	$ -	$ 2,185
OFDA Local Purchases (Project 519-0330)	24,987	-	-
Emergency Shelter Support (OFDA funds, Project 519-0330)	300,000	300,000	253,395
Earthquake Recovery Program (Project 519-0331)	50,000,000	44,458,725	23,487,156
	$50,336,957	$44,758,725	$23,742,736

The objectives of our financial/compliance audit were to determine: (1) whether A.I.D. obligations, advances and expenditures were properly accounted for by USAID/El Salvador and the GOES, and (2) whether the funds expended were supported by adequate documentation and were used in accordance with established eligibility and procurement criteria. We did

not audit the use of A.I.D. advances outstanding as of September 30, 1987 ($24,900,497) because they had not been liquidated and recorded by USAID/El Salvador as expenditures. We did, however, selectively verify, as part of our program results audit, activities accomplished with project funds, which would include any funds advanced and used by the GOES and other Salvadoran institutions but not yet liquidated by USAID/El Salvador.

Most of the expenditures under the Earthquake Recovery Program ($20,011,372) had been previously reviewed by Price Waterhouse in 1987 under a program monitoring contract separately financed by USAID/El Salvador. Our audit relied on the work performed by Price Waterhouse after making appropriate tests to verify the accuracy of their work.

Our financial/compliance audit also covered $11,468,298 in additional funds or commodities that were obligated or used for activities associated with the earthquake as summarized below and detailed in Exhibit 5.

Activities	Amount
International Disaster Assistance Funds accounted for by OFDA for emergency relief	$ 2,570,000
PL 480 Title II commodities used in the emergency food distribution program	902,600
A.I.D./GOES jointly programed local currencies	2,239,768
USAID/El Salvador activities funded with previously appropriated U.S. dollars	5,775,930
	$11,468,298

However, our audit coverage for the $11,468,298 was mainly limited to a description of how the funds and commodities were reportedly used. In addition, we sought to determine whether the funds were obligated or used in a manner consistent with project and legislative requirements.

We did not audit the $75 million Earthquake Reconstruction Project (519-0333) obligated on September 24, 1987, because no funds had been expended thereunder as of the cut-off date of our financial/compliance audit (September 30, 1987).

In Exhibit 4, we summarize our audit coverage of the nearly $137 million in activities financed by the U.S. Government for El Salvador in fiscal year 1987 in response to the earthquake. This exhibit also shows at what point in the body of the report each activity is discussed.

Best Available Copy

To accomplish our objectives, we reviewed records and interviewed officials of USAID/El Salvador, the GOES, the Municipality of San Salvador, A.I.D. contractors and selected financial institutions. USAID/El Salvador financed a separate contract with the auditing firm of Price Waterhouse so they could assist us with our audit. To verify accomplishments, we selectively reviewed records, interviewed beneficiaries, and inspected commodities and facilities financed with A.I.D. funds. To determine the accuracy of selected expenditure review reports prepared by Price Waterhouse under its monitoring contract with USAID/El Salvador, we traced selected findings to their workpapers and verified them with visits to respective financial institutions and beneficiaries cited in the reports and workpapers of Price Waterhouse. Audit field work was conducted from January 19, 1988 to March 15, 1988. Our review of internal controls and compliance was limited to the findings in this report. The audit was performed in accordance with generally accepted government auditing standards.

Best Available Copy

AUDIT OF A.I.D. ASSISTANCE
TO THE GOVERNMENT OF EL SALVADOR
FOR EARTHQUAKE RELIEF,
REHABILITATION AND RECONSTRUCTION
DURING FISCAL YEAR 1987

PART II - RESULTS OF AUDIT

USAID/El Salvador had effectively managed U.S. Government resources made available to El Salvador for earthquake relief, rehabilitation and reconstruction during fiscal year 1987.

A.I.D. responded quickly to the earthquake of October 10, 1986 with substantial quantities of emergency relief supplies and food (worth $3,502,600). USAID/El Salvador supported the relief effort with the services of its direct-hire and contractor personnel. Effective controls were established by using an A.I.D.-financed contractor to account for the receipt and distribution of emergency relief supplies (see Appendices 2 and 3).

Emergency relief was quickly followed by two USAID/El Salvador grants for $50,300,000. An Emergency Shelter Support project for $300,000 was started on October 23, 1986 and finished on April 30, 1987. An Earthquake Recovery Program for $50 million began on November 21, 1986 and ended on January 20, 1988.

The objectives of these projects (to provide funds for temporary shelter, employment, slum rehabilitation, restoration of public services and credit to repair damaged homes and businesses) were in general successfully accomplished (see Appendices 4, 5 and 6). Under the Emergency Shelter Support project, between 3,780 and 5,040 families received A.I.D.-financed building materials. Under the Earthquake Recovery Program, 897,206 person-days of work were generated to remove 114,608 cubic meters of rubble; 2,299 loans were made to micro or small businesses to repair or replace buildings, machinery, equipment, inventories and working capital; 36,124 families received A.I.D.-financed building materials for the construction or repair of temporary shelters; 26 small, medium-size and large infrastructure subprojects were completed in slum areas to relocate families and to repair or reconstruct civil works such as retaining walls and drainage structures; 7,195 loans were made to repair or reconstruct houses; and 65 public service restoration activities were completed by 14 Government of El Salvador (GOES) agencies. One objective of the project was to disburse funds quickly to speed assistance to needy earthquake victims. As a result, some funds were not used in accordance with established eligibility criteria, particularly under the credit components of the Earthquake Recovery Program.

Considering the speed with which these two projects were implemented, they were well-managed. USAID/El Salvador wisely employed two institutional contractors funded separately from these projects to monitor the receipt and distribution of commodities, disbursements, and

procurement transactions. As implementation problems were identified, USAID/El Salvador responded quickly to resolve the problems. Without the assistance of these contractors, it is unlikely that the projects could have been implemented as effectively as they were.

Except as noted in the body of this report, we found that, in general, USAID/El Salvador had properly accounted for the International Disaster Assistance funds obligated in fiscal year 1987 ($50,336,957); also, the funds expended ($23,742,736) were supported with adequate documentation and generally used in accordance with established eligibility and procurement criteria (see Appendices 6, 7, 8 and 9).

Our audit disclosed an undetermined amount of ineligible expenditures under the credit components of the Earthquake Recovery Program (see Finding No. 1). In addition, our review disclosed that the management of credit reflows under the Earthquake Recovery Program can be improved (see Findings No. 2 and 3), and that appropriated U.S. dollars may have been obligated or used for activities associated with the earthquake contrary to project and legislative requirements (see Finding No. 4). Finally, we found that the separate accounting records mantained by USAID/El Salvador for $30,957 in funds obligated under the OFDA and Ambassador's Relief grants were not complete (see Finding No. 5).

Our report recommends that ineligible loans be identified and resolved, management of credit reflows be improved, a legal opinion be obtained to determine whether funds were obligated or used contrary to requirements, and accounting records be updated.

A. Findings and Recommendations

1. Inappropriate Credit Line Disbursements Need to Be Resolved

The program's credit component was intended to assist low- and middle-income home owners and micro and small businesses affected by the October 10, 1986 earthquake. Loan amounts were to be commensurate with the amount of damages. An undetermined amount of credit component funds were loaned to individuals who did not qualify for program benefits, were used for ineligible purposes and/or were approved without adequate support or justifying documentation. The Mission had identified some of these loans and was taking corrective actions on them. However, it had yet to identify the full extent of inappropriate uses of credit funds or take final corrective actions. Irregularities occurred because program criteria lacked specificity and because the lending institutions generally lacked the time and resources to fully verify applicants' eligibility and proposed fund uses. These program weaknesses were generally corrected during program implementation and appear to have been avoided in the follow-on Earthquake Reconstruction Project. Nonetheless, because of these initial weaknesses, more program irregularities occurred than otherwise would have, thus reducing the availability of funds to the target group.

Recommendation No. 1

We recommend that USAID/El Salvador, in consultation with the Government of El Salvador, establish and implement a plan to:

a. identify as many ineligible home and business loans by institution as may be cost-effective, and

b. obtain restitution or substitution of eligible loans for such ineligible disbursements.

Discussion

The Secretariat for External Financing (SETEFE) within the Ministry of Planning was responsible, together with the financial institutions, for implementing the earthquake recovery program's credit components. The project agreement required SETEFE to develop a complete description of activities to be carried out prior to A.I.D.'s disbursement of program funds. A description of credit activities was prepared and accepted by A.I.D. on December 8, 1986. The program agreement and these guidelines required, among other things, that home credit assistance be restricted to applicants who (1) were in the low-to-middle-income bracket; (2) owned, or rented and planned to purchase, the damaged property; and (3) suffered physical damage to their property as a result of the October 10, 1986 earthquake. The program agreement and guidelines required, among other things, that business credit assistance be targeted to micro (assets of less than $20,000) and small (assets between $20,000 and $100,000) businesses which were damaged by the earthquake.

In addition, program guidelines required that home loans be limited to repair and reconstruction of homes and awarded in amounts commensurate with damages but not to exceed $4,000. Similarly, business loans were to be used to reconstruct and repair buildings; repair machinery, equipment and tools; and replace inventory and working capital commensurate with damages incurred but not to exceed $15,000. Implicit in the guidelines was an understanding that participating financial institutions themselves would ensure, through site inspections, documentation requirements or a combination thereof, that loan funds were actually required and properly used.

The Earthquake Recovery Program's credit line component was successful in quickly disbursing most of the $33.4 million budgeted for home and business recovery assistance. The majority of the loans were approved and contracted within six months of the program's November 1986 starting date. At the program's end in January 1988, 7,195 home loans representing $20.9 million and 2,299 business loans representing $9 million had been awarded. Of these amounts, $20.6 million and $8.9 million had been disbursed for home and business loans, respectively. In total, 18 financial institutions were involved in administering the credit program. They included 10 banks, 7 savings and loan associations, and 1 credit agency.

It appears that, for the most part, the credit funds went to eligible recipients and were used for the program's intended purposes: to repair physical damages and to recover other losses incurred as a result of the October 10, 1986 earthquake. However, the success of the program, as measured in terms of the amounts of money disbursed and individuals assisted in a short period of time, was not without its costs.

An undetermined amount of credit funds were loaned to individuals who did not qualify for program assistance, were used for ineligible purposes and/or were approved without adequate support or justifying documentation. The Mission was aware of some of these improper disbursements and was taking action to resolve them. However, the full extent of funds not used in accordance with program eligibility criteria had not been fully quantified or resolved by the Mission. We estimate that at least $4 million, or 13 percent, of the total home and business credit disbursements may have been made to ineligible borrowers and/or for ineligible purposes. This estimate is based on the cumulative findings of various formal and informal reviews which are summarized in Appendix 10.

Inappropriate credit line disbursements can be attributed to various factors, including inadequate loan processing and monitoring by the participating financial institutions. In fairness to the institutions, however, neither the criteria used to determine program eligibility and loan amounts nor the institutions' management capabilities to administer credit activities were adequately established by A.I.D. or the GOES at the program's outset. Program guidance and directions to the financial institutions lacked specificity and in certain instances were misleading. For example, although the discussion attached as a cover to

the detailed credit guidelines prepared by SETEFE indicated that the financial institutions were required to perform physical inspections to verify damages and end-uses of funds, the detailed guidelines themselves did not specifically require this action. Furthermore, the institutions were verbally instructed by the government that 100 percent physical inspections would not be required because of the urgency to disburse funds. Also, while program guidelines restricted home program assistance to individuals in the low- and middle-income brackets, these brackets were never precisely defined, leaving the final decision with the institutions. Furthermore, credit managers at some of the institutions visited stated that they had not received the guidelines or had received them only after some loan disbursements had already been made.

In addition, the institutions were generally not prepared to adequately handle the program's large volume of credit applications. In this regard, some institutions, especially banks, reportedly lacked the necessary resources to fully verify applicant eligibility and proposed fund uses in the relatively short time anticipated under the program. As a result, some of the financial institutions received temporary financial assistance outside the program's original design to assist in administering their earthquake recovery loan portfolios. Seven banks received the equivalent of $7,600 from Economic Support Fund local currency generations in order to hire temporary staff to help process housing loans.

Program weaknesses, to a certain extent, were corrected during program implementation and appear to have been generally avoided in the follow-on Earthquake Reconstruction Project (No. 519-0333). For example, home credit under the follow-on program will only be administered by savings and loan associations, whose performance was found to be better than the banks under the recovery program. One exception, however, is that the reconstruction program, like the recovery program, did not fully take into account the possibility of earthquake insurance. The availability and possible possesion of earthquake insurance by the program's target group could affect the demand estimates for reconstruction funding.

As a result of not adequately establishing credit criteria or reviewing participating institutions' loan processing capabilities, more irregularities occured than otherwise would have, thus reducing the availability of credit funds to the program's intended target group. Fortunately, the potential adverse effect of these program weaknesses was minimized by the quick and decisive actions taken by the Mission to have Price Waterhouse (PW) monitor the program and to suspend advances to the financial institutions for up to seven weeks until they had implemented specific improvements in their loan processing operations. These efforts resulted in a better managed program and subsequently fewer abuses.

By the time all contracted loans are funded, the credit program will have disbursed $30 million, or 90 percent of the component's revised budget amount. Better defined guidelines and directions at the program's outset would have ensured that more credit funds reached the target group,

although it may have taken longer. Given the number of ineligible and questionable loans found by Price Waterhouse, the banks, the Mission and the current audit (see Appendix 10), and the fact that advances had to be halted to correct deficiencies, one must question whether a more slowly implemented program, especially the home and business loan programs, would not have been advisable. The Mission has continuously worked on resolving the ineligible loans identified by Price Waterhouse. It now needs to focus its attention on identifying the full extent of ineligible credit disbursements and to obtain commensurate restitution or substitution of eligible loans from the GOES and/or the financial institutions. We believe the following proposed plan may be the most cost-effective means of resolving the outstanding ineligible loan issue.

- First, USAID/El Salvador in consultation with the GOES should decide on the specific criteria that will be used to measure program compliance.

- Second, have Price Waterhouse, during its ongoing audit, select a statistically valid sample of all loans disbursed under the program, by institution and by loan program. The results of this sample should be projectable to the universe of loans and value in regard to the following three categories (a) number of unqualified recipients, (b) loans exceeding actual damages, and (c) loans used for ineligible purposes.

- Third, for each category determine the number and value of ineligible loans that the institutions and Price Waterhouse agree upon. For those in disagreement, have the government and USAID jointly agree on their disposition. For the total in each category, extrapolate the findings to the universe.

- Fourth, for the projected amount, have the institutions repay the determined amounts to the same account used for program reflows and/or substitute new eligible loans as verified by the Mission. An acceptable alternative would be to have the Government of El Salvador repay the portion that the institutions would not agree to from its Economic Support Fund local currency resources.

- Fifth, credit should be given for the amount that the institutions have already repaid or substituted for earlier ineligible loans.

Less cost-effective would be determining restitution on an actual basis, which would require a review of all loan awards. This may be necessary if determining restitution on a sample basis is not acceptable to the institutions and/or the GOES. In this situation, however, the Mission should assess the significance of the new PW statistical sample findings by financial institution before initiating a review of all loan awards. If not significant, it may be more cost-effective to recover only the ineligible disbursements identified in the new sample.

Best Available Copy

In addition, the Mission needs to ensure that the deficiencies identified in the earthquake recovery program's credit component, including unclear and/or insufficiently detailed guidelines, incomplete and/or late distribution of the guidelines, and inadequate consideration of the existence of earthquake insurance, are avoided in the follow-on earthquake reconstruction project.

Management Comments

The Mission concurred that the home and business credit lines needed to be more fully examined; however, they did not concur with the Office of the Inspector General (IG) estimate that $4 million, or 13 percent, of the total home and business credit disbursements may have been ineligible. They generally did not believe adequate information had been collected to date by PW or others to establish an accurate estimate. In addition, the Mission did not concur with the recommendation that all ineligible loans be identified. They consider this recommendation premature and not cost-beneficial. The Mission stated that the ongoing non-Federal audit was designed to determine the degree of ineligible loans and suggested that the results of this effort be the basis for establishing a cost-effective plan to recover ineligible disbursements.

Office of Inspector General Comments

The Office of the Inspector General agrees with the Mission on the need to establish a plan which is cost-effective. This has always been the IG's intent. Wording changes have been made in the text and recommendations to clarify this point. Additional wording changes have been made in the text to clarify other points, including the basis for the IG's $4 million estimate. Unlike the Mission, the IG considers this a conservative figure and fully supported by documentation as described in Appendix 10.

2. More Information Is Needed to Better Manage Credit Line Reflows

Neither USAID/El Salvador nor the Government of El Salvador had current information on the status of earthquake recovery credit reflows. Program guidelines required participating financial institutions to establish a special section to manage and recover loans and to report quarterly on the amount of loan balances and recoveries. The institutions had not complied with these requirements because, apparently, they were not fully aware of them and/or lacked the resources to comply with them, and because SETEFE, until our audit, had not routinely requested information on reflows. As a result, important information on the institutions' loan recovery performance, delinquencies and existing balances remained unknown. The lack of such information impeded effective management of the credit program.

Recommendation No. 2

We recommend that USAID/El Salvador obtain from the 18 participating financial institutions, through the Government of El Salvador Secretariat for External Financing, reports on the status of their earthquake program loan balances, delinquencies and reflows on a quarterly basis.

Discussion

Neither USAID/El Salvador nor the earthquake recovery program's implementing agency, the Secretariat for External Financing (SETEFE), had current information on the status of home and business loan reflows including amounts delinquent and total amounts repaid. This information was important to, among other things, determine how effective the institutions were in recovering the loans, to gauge the rate and amount of delinquencies, and to plan the use of these reflows. Deviations in the participating financial institutions' loan collection procedures, including their failure to report the status of reimbursements to SETEFE, was mentioned in PW's August 31, 1987 report. Yet, as of our audit, corrective actions had not been taken by SETEFE or the Mission.

As part of the audit, in early February 1988 we requested SETEFE to provide us with information on recoveries and delinquencies. SETEFE had to specifically request this information from each of the 18 participating institutions because it had not been regularly reported as required. The responses summarized below showed that, of the approximately $3.1 million due as of January 31, 1988, 87 percent had been recovered and 13 percent was considered at least 30 days delinquent.

Summary of Loan Recoveries
and Delinquencies a/

Status	Home Repair	Business Repair	Total Home and Business	Percentage of Total
Recovered	$1,683,112	$ 973,515	$ 2,656,627	87%
Delinquent	188,257	209,082	397,339	13%
Amounts Due	$1,871,369	$1,182,597	$ 3,053,966	100%

a/ Includes information provided by 17 of the 18 institutions as of January 31, 1988. See Finding No. 3 for more details on recoveries.

Credit component guidelines required financial institutions to establish a special section to manage and recover loans and to report quarterly to SETEFE on the credit balances and amounts recovered.

The institutions had not complied with the reporting requirements because they apparently were not aware of them and because they lacked the necessary resources. Price Waterhouse stated in its monitoring reports that the financial institutions, especially the banks, had not assigned personnel to the supervision and recovery of loan funds. A SETEFE official stated that the institutions had limited resources and therefore had not established special sections to manage the loans. This was considered a factor in explaining why the institutions did not have readily available current information on loan reflows. The official also stated that SETEFE had not specifically required the institutions to report quarterly on the status of loan reflows.

As a result of not being aware of the status of loan reflows, neither SETEFE nor the Mission knew whether or not the institutions were adequately recovering and managing loan reflows, nor the amount of funds that were available for use within the credit program or other similar activities.

Program guidelines required the participating financial institutions to report the status of credit reflows on a quarterly basis. Neither SETEFE nor USAID/El Salvador had required compliance with this requirement. As a result, program managers had inadequate knowledge of the institutions' reflow experience and whether or not the institutions were effectively managing this activity.

Management Comments

The Mission fully agreed with the recommendation and provided evidence that SETEFE had already taken action to implement it. The Mission objected to certain parts of the discussion that left the impression that the Mission was not aware of the status of reflows.

Office of Inspector General Comments

Minor wording changes were made to clarify the text. The recommendation appears to be resolved, i.e., appropriate corrective actions have been taken, and can be closed upon evidence that the 18 participating financial institutions have submitted the first of the required periodic reports.

3. Credit Line Reflows Need to Be Deposited Into a Special Program Account and Their Uses Determined

The government of El Salvador's portion of credit reflows had not yet been deposited into a special account nor had their uses been determined. As of our audit, these reflows amounted to nearly $2.7 million. After deducting participating financial institutions' share of the interest earned on the loans, the amount available for deposit was nearly $2.2 million. Program guidelines required the financial institutions to deposit loan reflows (principal and two percent interest) into a special account in the Central Bank within 180 days of collection. The program envisioned that these reflows would be used for similar credit line activities. No deposits had been made because: (1) SETEFE had only just recently established an account for the reflows; (2) SETEFE and USAID/El Salvador had not yet formally established plans on how all these funds would be used; and (3) because neither SETEFE nor the USAID Mission expected significant reflows during the first year. As a result, a substantial amount of loan reflows had been retained by the participating institutions and had not been made available for other similar credit activities.

Recommendation No. 3

We recommend that USAID/El Salvador:

a. obtain evidence from the Ministry of Planning demonstrating that participating institutions are depositing the Government of El Salvador's portion of the reflows into the corresponding special account, and

b. formulate, in consultation with the Ministry of Planning, a plan as to how these funds will be used, as intended by the program agreement.

Discussion

At the time of our audit, none of the home and business loan reflows had been deposited into a special account in the Central Bank. Neither the earthquake recovery program's implementing agency, SETEFE, nor USAID/El Salvador knew exactly how much the financial institutions had recovered from their earthquake recovery loan portfolios because, as discussed in the previous finding, this information was not being reported quarterly as required.

The principal was loaned at five percent interest. Three percent of this was kept by the lending institution; the principal and remaining two percent interest was to be deposited and used for similar credit activities.

On our behalf, SETEFE requested this information from each of the 18 participating financial institutions in early February 1988. By March 11, 1988 information had been received from 17 of the 18 institutions. The incomplete information showed that, as of January 31, 1988, $2.7 million had been recovered, of which nearly $2.2 million or 81 percent, was being held on behalf of SETEFE as shown in the following table:

Summary of Loan Recoveries to Be Deposited into the Special Account as of January 31, 1988 a/

Type of Loan	Total Recovered	Capital	Two Percent Interest	Available for Deposit	Three Percent Interest for the Institutions
Home	$1,683,112	$1,055,379	$260,935	$1,314,314	$368,798
Business	973,515	774,492	90,326	864,818	108,697
Total	$2,656,627	$1,827,871	$351,261	$2,179,132	$477,495 b/

a/ Information for one institution was not available.

b/ Does not include penalties collected by the institutions.

Information in SETEFE files indicated that similar information had been collected only once before. This information was as of the end of May 1987, and covered approximately the first six months of program implementation. It showed that $667,544 had been recovered and was available for program credit or other similar purposes.

Summary of Loan Recoveries Available for Deposit as of May 31, 1987 c/

Type of Loan	Available for SETEFE's Use d/	Two Percent Capital	Interest
Home	$473,032	$391,290	$ 81,742
Business	194,512	170,476	24,036
Total	$667,544	$561,766	$105,778

c/ Only information on SETEFE's portion of recoveries was available.

d/ A special account for deposit of these funds had not yet been established.

In July 1987, USAID/El Salvador authorized participating financial institutions to use the above recoveries to meet their unsatisfied demand for home loans. Project Implementation Letter No. 31 authorized this use but only to then existing reflows and not to those subsequently recovered. It was subsequently found, however, that these funds were not needed because the institutions were already at full capacity and/or were not

interested in increasing their portfolios. As a result, in October 1987 through implementation letter No. 44, A.I.D. rescinded the earlier requirement that these funds be used to meet the unsatisfied housing demand, leaving their use to be jointly agreed upon by SETEFE and A.I.D.

One institution told us that it had sent the Central Bank a check covering reflows but that it had been returned because the special account had not yet been established. The audit did not attempt to verify how the GOES's portion of these reflows was being maintained by the institutions. Most of the institutions we visited said they were not using these funds; however, two institutions stated that they had relouned such funds for various purposes at rates higher than the recovery program's five percent interest rate. Another stated it had used the funds to meet the Central Bank's reserve requirements. The program was not designed so that earthquake recovery credit reflows could be used for the economic benefit of the financial institutions, beyond their three percent share of interest earnings.

Program guidelines required the financial institutions to deposit the government's portion of the credit reflows (principal and two percent interest) into a special account in the Central Bank within 180 days of collection. Program credit implementation plans envisioned that these reflows would be used for similar credit activities as agreed to jointly by the GOES and USAID/El Salvador.

However, this aspect of the credit program had never been fully implemented. During the audit, SETEFE established a special account to deposit the reflows. However, the institutions had not been instructed to make deposits, and plans governing the use of all reflows had not been formalized by SETEFE and USAID/El Salvador. Neither SETEFE nor the USAID expected significant reflows during the first year. A USAID/El Salvador official confirmed that plans had not yet been formalized, but stated that they would be completed in the immediate future. Another USAID official said the tentative plan was to channel the home and business credit reflows into two other A.I.D.-funded programs, the National Low-Income Housing Fund and the Federation of Credit Institutions program 1/. We were advised that these two programs were aimed at assisting groups similar to those targeted under the earthquake recovery program's home and business credit components.

As a result of only recently establishing an account and not developing formal plans for the use of credit reflows, a substantial amount of funds was not available for similar assistance activities.

The Earthquake Recovery Program was designed so that a certain amount of program funds would be recovered and used for similar credit activities. The intended target groups had not fully benefited because SETEFE and USAID/El Salvador had not until recently established the account or the

---

1/ See RIG/A/Tegucigalpa Audit Report No. 1-519-88-05, dated December 23, 1987, for the results of our review of this program.

Best Available Copy

procedures necessary to implement this aspect of the earthquake recovery program. As a result, these reflows to date have only benefited the financial institutions which have apparently used some of these funds for their own economic gains.

Management Comments

The Mission accepted the recommendation as written and stated that steps have already been taken to comply with it. The Mission disagreed, however, with certain parts of the dicussion which they alleged made it seem that the Mission had not established formal plans for the use of reflows. It cited Project Implementation Letter No. 31 as evidence of a formal agreement for the use of credit reflows.

Office of Inspector General Comments

The discussion clearly recognizes the Mission's earlier effort to plan the use of reflows with Project Implementation Letter No. 31. The discussion also points out, however, that this particular plan only pertained to existing reflows as of July 1987 and not to subsequent reflows, and that even this limited plan was subsequently rescinded three months later. The report's point, therefore, is that the Mission had not established a comprehensive plan to use all reflows. The recommendation appears resolved and can be closed upon evidence that deposits have been made into the new reflow account and provision of a signed agreement or plan on the use of these reflows as intended by the program agreement.

1. Appropriated U.S. Dollars May Have Been Obligated or Used for Activities Associated with the Earthquake Relief Effort Contrary to Authorized Project or Legislative Requirements

USAID/El Salvador obligated or used $1,340,231 from development assistance and economic support funds to finance activities associated with earthquake relief. The use of these funds to support recovery efforts may have been contrary to project and legislative requirements and could also hamper the activities for which the funds were originally authorized. The Foreign Assistance Acts for fiscal years 1986 and 1987 and A.I.D. regulations establish procedures for modifying the authorized use of appropriated funds and for providing prior notification to the Congress of such changes. We found no evidence in USAID/El Salvador files that Congress had been notified of the obligation or use of development assistance and economic support funds for activities associated with earthquake relief. Because of differences between the Foreign Assistance Acts of 1986 and 1987 and the complexity of A.I.D. regulations, we were unable to determine whether Congressional Notifications were in fact required. For this reason, we believe the General Counsel, Bureau for Latin America and the Caribbean, A.I.D., should determine whether any corrective action was or still is required.

Recommendation No. 4

We recommend that USAID/El Salvador obtain a legal opinion from the General Counsel, Bureau for Latin America and the Caribbean, A.I.D., to determine whether development assistance and economic support funds obligated or used for activities associated with earthquake relief were employed in a manner consistent with authorized project or legislative requirements and take any corrective actions required by the legal opinion.

Discussion

Some appropriated U.S. dollars may have been obligated or used for activities associated with earthquake relief contrary to project and legislative requirements. Exhibit 3 (items D5 to D13) lists $1,340,231 in funds obligated or used in fiscal year 1987 for activities associated with the earthquake. These activities were financed with U.S. dollars from funds appropriated under the Foreign Assistance Act (FAA) for Development Assistance ($888,764) and Economic Support ($451,467). The use of these funds for earthquake recovery could hamper the activities for which the funds were originally authorized.

The FAAs 2/ for fiscal years 1986 and 1987 and A.I.D. regulations establish procedures for modifying the authorized use of appropriate funds and for providing prior notification to the Congress of such changes.

2/ Foreign Assistance Act amendments of 1986 and 1987 modified the Foreign Assistance Act of 1961, and were enacted by a continuing resolution.

The FAA for fiscal year 1986 appears to provide some flexibility in obligating funds for international disaster assistance. Part I, Chapter 9 - "International Disaster Assistance," Section 492 states:

> In addition to amounts otherwise available to carry out this chapter, up to $50,000,000 in any fiscal year may be obligated against appropriations under this part (other than this chapter) for use in providing assistance in accordance with the authorities and general policies of section 491. Amounts subsequently appropriated under this chapter with respect to a disaster may be used to reimburse any appropriation account against which obligations were incurred under this subsection with respect to that disaster.

This section may apply to the $888,764 of Development Assistance funds used for earthquake activities because they were appropriated under Part I of the FAA, which is the same Part under which International Disaster Assistance funds are appropriated. Section 492 probably would not apply to the $451,467 of Economic Support Funds (ESF) used for earthquake activities because ESF funds are appropriated under Part II of the FAA.

The FAA for fiscal year 1986 may also provide an exception for notifying Congress on program changes concerning programs of disaster relief and rehabilitation. Section 634A(a) "Notification of Program Changes" of the FAA states:

> None of the funds appropriated to carry out the purposes of this Act (except...programs of disaster relief and rehabilitation) may be obligated for any activities, programs, projects, types of material assistance, countries, or other operations not justified, or in excess of the amount justified, to the Congress for obligation under this Act...for any fiscal year unless... the Congress is ...notified fifteen days in advance of such obligation.

Congressional notification requirements were modified by Section 523 of the FAA for fiscal year 1987 3/. Section 523 was basically the same as Section 634A of the FAA for fiscal year 1986 but it no longer allowed an exception for programs of disaster relief and rehabilitation.

3/ Contained in a note to the "Legislation on Foreign Relations through 1986."

The FAA for fiscal year 1987 also added Section 514, as follows:

> None of the funds made available by this Act may be obligated under an appropriation account to which they were not appropriated without the written approval of the Appropriations Committees of both Houses of the Congress.

To provide guidance to implement Congressional notification requirements, A.I.D.'s LAC Bureau cabled its overseas offices on April 9, 1985 (STATE 106586) which stated in part:

> 2. A full Congressional Notification (CN) is required:
>
> (C) For activities which have been previously notified to the Congress,
>
> (1) When A.I.D. wishes to authorize an increase in life-of-project funding above the authorized level shown in the latest CN for the activity. However, projects authorized on a continuing basis for which LOP funding is identified in the CP as being continuing need not be notified for increases in LOP funding;
>
> (2) When the purpose or scope of the activity becomes substantially different from that indicated in the latest CN for that activity; or
>
> (3) When the funding source is different from that indicated in the latest CN for that activity, e.g. a shift between appropriation accounts or between grants and loans within an appropriation account.

We found no evidence in USAID/El Salvador files that the Congress was notified of the $1,340,231 in Development Assistance and Economic Support funds obligated or used for earthquake activities by USAID/El Salvador in fiscal year 1987. Considering the differing notification requirements contained in the FAA's for fiscal years 1986 and 1987 and in A.I.D. guidance, we were unable to determine whether the Congress should have been notified.

The use of funds for earthquake recovery activities was different from the original purposes of the projects authorized by the Congress. For example, funds authorized under the Public Services Restoration project (519-0279), were used to finance commodities of $421,409 to repair or replace facilities of the power company damaged by the earthquake even though the purpose of this project was "... to assist the Grantee to maintain and restore public services affected by the political conflict

in the country." Implementation Letter No. 19, dated August 30, 1984, provided equipment on hand could be temporarily used for an emergency due to a natural disaster. However, in our opinion the temporary use of equipment on hand is different from the direct procurement of equipment for a disaster.

Because of the complexities of this issue and other factors which may apply or of which we may not be aware, we believe the Assistant General Counsel for Latin America and the Caribbean, A.I.D., should determine whether any corrective action is required.

Management Comments

While USAID/El Salvador agreed with the recommended action, they believed the appropriate actions were taken (see page 9 of Appendix II for details of USAID/El Salvador comments).

Office of Inspector General Comments

Recommendation 4 can be closed as soon as a legal opinion is obtained and any required corrective actions are taken.

5. Accounting Records for the Office of Foreign Disaster Assistance and Ambassador's Relief Grants Needed to Be Updated

USAID/El Salvador maintained limited accounting records which did not fully account for the obligation and expenditure of funds made available for the OFDA operating grant ($25,000) and the Ambassador's Relief grant ($25,000). The accounting records and controls that should be maintained for these grants are set forth in A.I.D. Handbooks 8 and 19. USAID/El Salvador was responsible for maintaining the official accounting records for the OFDA grant, and A.I.D./Washington the records for the Ambassador's grant. We believe that USAID/El Salvador should maintain subsidary records for the Ambassador's grant to avoid overobligation or overexpenditure of funds, and to provide a basis for verifying the accuracy of the official records kept by A.I.D./Washington. USAID/El Salvador could not locate all of the supporting documentation for the obligations and expenditures recorded in the separate accounts for these grants. Also, some of the documentation had not been posted to the accounts. USAID/El Salvador did not originally record all of the transactions in its accounts because its computer system was damaged by the earthquake. After the computer system was restored in January 1987, the missing documentation was difficult to locate because the transactions had been processed along with other petty cash transactions. Separate accounting records should be kept current for each grant to avoid the overobligation or overexpenditure of funds.

Recommendation No. 5

USAID/El Salvador should:

a. update its separate accounting records for the Office of U.S. Foreign Disaster Assistance and the Ambassador's grants, and

b. advise A.I.D./Washington of the updated balances for obligations and expenditures.

Discussion

Accounting records were incomplete for two grants.

OFDA Grant (Project 519-0330)

Although USAID/El Salvador kept separate accounting records, it did not adequately account for obligations and expenditures made against a budget allowance of $25,000 provided by OFDA for relief expenses as required by A.I.D. Handbook 19. Chapter 1A-5 of the Handbook provides that the USAID Controller's Office will maintain budget allowance accounts for recording obligations and disbursements. Allowees are responsible for maintaining these accounts to avoid the overobligation or overexpenditure of funds allowed.

USAID El Salvador's "Project Financial Status Report" as of September 30, 1987 showed that the USAID had obligated $24,987 of the $25,000 budget allowance. USAID/El Salvador provided us with documents to support only $10,506 of the obligations recorded in the account. In addition, no disbursements (expenditures) had been recorded in the account as required by A.I.D. Handbook 19, even though the USAID/El Salvador Controller was able to provide us with $9,374 in payment vouchers. Apparently, all of the goods and services had been provided because the report showed that expenditures had been accrued for the full amount of the obligation ($24,987). Officials of the USAID/Controller's office said they plan to record the payment vouchers in the account as soon as they can be located. These vouchers were not originally recorded because the USAID computer system was damaged by the earthquake. After the computer system was restored in January 1987, the vouchers were difficult to locate because they had been processed along with other petty cash transactions.

Although a comprehensive separate account control was not maintained for this grant, it appears that the Controller's office adequately accounted for the receipt and expenditure of petty cash funds used for this grant as well as for other purposes. During the period immediately following the earthquake, USAID Controller personnel obtained $57,199 in petty cash funds to cover expenses for emergency relief. A record of the receipt and disbursement of these funds was maintained by Controller personnel. However, this record did not separately summarize the funds spent for the OFDA local purchases grant, the Ambassador's Relief Grant and USAID/El Salvador operating expenses.

In order to verify that funds were not overobligated or overexpended, we believe that USAID/El Salvador should locate the missing obligation documents and payment vouchers, and update its accounting records.

Ambassador's Relief Grant

USAID/El Salvador subsidiary accounting records for the $25,000 relief grant authorized by the U.S. Ambassador were not complete. A.I.D./Washington is responsible for keeping the official accounting records for this grant. However, we believe USAID/El Salvador should maintain subsidiary records in order to avoid the overobligation or overexpenditure of grant funds and to provide a basis to verify that copies of all obligating documents and advices of charge for expenditures were sent to A.I.D./Washington for recording in the official accounts.

A.I.D. Handbook 8, Chapter 4 provides that when a Chief of Mission has determined that a disaster exists, up to $25,000 in OFDA funds from the International Disaster Assistance account can be committed for emergency relief by advising A.I.D./Washington. The U.S. Mission is responsible for ensuring that total costs incurred do not exceed the $25,000. It also has to provide A.I.D./Washington with copies of obligating documents and advices of charge for expenditures. The official accounting records are kept in A.I.D./Washington.

USAID/El Salvador maintained separate manual accounting records for this grant but they were not complete and covered an eleven-day period only, from October 21 through 31, 1986. USAID/El Salvador had recorded $11,970 in obligations in its separate accounting records for this grant. They provided us with obligating documents to support $7,820 of the obligations shown in the records and additional documents for $1,956 that had not been posted in the records. Also, USAID/El Salvador had recorded $2,185 of expenditures in their separate accounting records for this grant. They provided us with payment vouchers to support $730 in expenditures shown in their records and additional vouchers for $234 not posted in the records. USAID/El Salvador had difficulty finding the payment vouchers for this grant because they were processed along with other petty cash transactions, and were not easily identifiable. In order to verify that funds were not overobligated or overexpended, we believe the missing documentation (obligating documents, payment vouchers and advices of charge) should be found and posted to the records. USAID/El Salvador records should then be reconciled with the official accounting records in A.I.D./Washington to determine whether any adjustments are needed in the official records.

Management Comments

USAID/El Salvador stated it had updated its accounting records for the OFDA relief grant and was awaiting an advice of charge from A.I.D./Washington to complete the accounting for this grant.

USAID/El Salvador also stated it took action for the Ambassador's relief grant by forwarding to A.I.D./Washington all information on obligations and an advice of charge for all disbursements made by USAID/El Salvador. The advice of charge was sent to A.I.D./Wahington on March 31, 1988.

Office of Inspector General Comments

USAID/El Salvador updated its accounting records as follows:

	Obligations	Expenditures
OFDA Grant		
Before audit	$24,987	$ -
After audit	$21,343	$15,259
Ambassador's Grant		
Before audit	$11,970	$2,185
After audit	$9,654	$9,654

Based on actions taken by USAID/El Salvador, Recommendation No. 5 is considered closed upon issuance of this audit report.

B. Compliance and Internal Controls

1. Compliance

Our review of compliance was limited to the findings presented in this report. We found the following six compliance deficiencies.

First, financial institutions did not comply with loan eligibility or use criteria as required by the Earthquake Recovery Program (see Finding No. 1).

Second, financial institutions did not report quarterly on loan delinquencies and recoveries as required by the Earthquake Recovery Program (see Finding No. 2).

Third, SETEFE had not established a special program account for loan reflows as required by the Earthquake Recovery Program (see Finding No. 3).

Fourth, appropriated U.S. dollars may have been obligated or used for activities associated with the earthquake contrary to project and legislative requirements (see Finding No. 4).

Fifth, USAID/El Salvador did not fully comply with the A.I.D. requirement to maintain accounting records for the OFDA grant (see Finding No. 5).

Sixth, SETEFE did not initially deposit A.I.D. funds received under the Earthquake Recovery Program in a separate bank account as required by the Grant Agreement (see Appendix 7).

2. Internal Controls

Our review of internal controls was limited to the findings presented in this report. We found two internal control deficiencies.

First, SETEFE initially advanced funds to financial institutions under the Earthquake Recovery Program prior to obtaining signed contracts governing the use of these funds (see Appendix 7).

Second, internal controls established for the Emergency Shelter Support Project did not operate effectively. As a result, the number of families who received building materials could not be precisely determined and accountability for materials distributed under the project may not have been adequate (see Appendix 5).

C. Other Pertinent Matters

During the audit, the following other pertinent matters came to our attention. First, we noted that the earthquake recovery program's credit component was not aimed at or restricted to assisting the most devastated areas of San Salvador. Instead, the program was generally open to all areas of the city on a first come, first served basis. The audit did not determine what percentage of credit funds was disbursed by area, but our limited work showed that assistance was widely scattered throughout the metropolitan area. It appears that the credit program would have had a greater impact in assisting the intended target groups--low- and middle-income home owners and micro and small business--if the most affected areas with the highest concentration of these groups had been designated and or identified by map delineation at the program's outset. In our opinion, these areas could have been identified based on the GOES' and the Mission's knowledge of these areas and target groups. The designated areas could have been expanded during program implementation based on experience and fund availability. As discussed in Finding No. 1, better defined criteria would have reduced the number of inappropriate loans. Similarly, specifically designated areas could have better ensured that program funds reached the target groups.

Second, some employees and clients of the financial institutions that administered the home credit program and some U.S. Mission national employees may have improperly received preferential treatment in obtaining credit assistance. Price Waterhouse identified, during its monitoring activities, those financial institution employees that received home credit assistance. Based on information provided by 12 of the 17 institutions, 516 employees received loans totaling about $1.4 million, or about 7 percent of total program disbursements. The recovery program did not prohibit these employees from receiving loans provided they met the eligibility criteria. One institution had approved loans to 271 of its employees, or 53 percent of the total number of employees identified by Price Waterhouse. Five institutions did not provide Price Waterhouse with employee loan information.

During its review of loan files and end-use checks, Price Waterhouse discovered that some employees in eight of the institutions had improperly received home loans. In these cases, it was found that the subject homes had not suffered earthquake damages and the funds were used for other purposes. Officials at the institution with the highest number of employee loans (271) stated that at the program's outset, loans were readily approved for its employees. When Price Waterhouse questioned the eligibility of a number of these loans, the institution's top management immediately investigated the situation and took corrective actions for those loans found ineligible. The institution hired two staff members to inspect involved employee homes for damages. The institution also required involved employees to report how they used the loan funds. However, only about 123, or 45 percent, responded. The institution and Price Waterhouse identified a total of 32 loans of the 271 which were not eligible. The institution transferred some of these loans to its commercial portfolio and required repayment on others. The institution reported to SEIEFE that it had substituted eligible new loans for these improper loans. The institution also stated that it had discharged some of the employees involved in these improper loans.

In addition to employees, the audit showed that clients of at least one of the institutions received preferential treatment over non-clients. The extent of this was not determined and, furthermore would probably be difficult to fully substantiate. However, this institution readily admitted that customers with existing mortgages had their loan applications processed before non-clients. The program did not preclude previous clients who were otherwise eligible from obtaining loans; however, the program was to provide equal treatment to members of the target group. By giving preference to existing clients the institution gave the appearance of protecting its existing mortgages.

One institution also gave preferential treatment to some Mission and U.S. Embassy local employees. The audit identified 44 local national employees who had their credit applications submitted as a group to the Mission's local bank which, according to Mission officials, was also where many of the employees had accounts. The program did not preclude local national employees, who were otherwise eligible, from obtaining loans. Of the 44 employees, 7 were determined ineligible by the institution. However, the remaining 37 received priority over an estimated 200 non-Mission applicants awaiting credit at the same financial institution. USAID/El Salvador and the Embassy financed the physical inspection reports for these individuals and others at a cost of $3,840. The Mission, in its written comments to the draft report, said it wanted "to go on record officially stating that no partiality was shown to Mission employees by USAID or the U.S. Embassy and that the Mission repeatedly told financial institutions to give Mission employees the same consideration as all other applicants."

These three potential conflict-of-interest situations might have been avoided by better planning and establishing more stringent criteria for the credit component.

Third, under the earthquake recovery program's credit component, 4/ the financial institutions are permitted to retain the government's portion of loan recoveries for up to 180 days. The rationale for allowing the institutions to maintain these funds for six months is unclear. We know of no reason why these funds could not be deposited into the special MIPLAN account on a monthly basis. The present arrangement appears to constitute a windfall for the institutions. A Mission official said he saw no reason why the funds could not be deposited monthly except for the fact that the 180-day term was a contractual arrangement. He speculated that the 180-day term was established because of the institutions' low margin on the home and business loans. Eight of the ten institutions we visited stated they were not aging the reflows and were willing to deposit the collected reflows whenever they were requested to do so. The more quickly these funds are deposited into the special account, the more quickly they can be used for higher priority development needs.

4/ See Finding No. 5 for discussion on credit reflows.

Fourth, as discussed in Finding No. 1, the existence of earthquake insurance was not considered in determining program eligibility and/or the amount of loan awards. We were told that the savings and loan associations generally required catastrophe insurance (including earthquake coverage) to cover at least the existing mortgage loan balance. The audit of the earthquake recovery program's credit component showed that some program recipients obtained, through a combination of insurance proceeds and loans, more funds than they needed to repair earthquake damages. It appears this situation could also occur under the follow-on earthquake reconstruction program (No. 519-0333). Credit applications under the new program should specifically require each applicant to identify whether the subject property is covered by earthquake insurance, and if so, to identify through documentation the amount received for damages. In these cases, loan amounts should only be approved for the difference between the estimated damages and insurance proceeds, not to exceed the program's maximum limit. Adherence to this policy may result in budgeted funds having a wider impact than originally anticipated.

Fifth, one of two financial institutions may have deposited funds advanced by USAID/El Salvador under the credit components of the Earthquake Recovery Program into interest-bearing accounts. Annex II of the Grant Agreement provides that any interest earnings on grant funds will be returned to A.I.D. We asked SETEFE to obtain information from the financial institutions involved, but no information had been provided as of the completion of our audit (March 15, 1988).

Sixth, USAID/El Salvador donated twenty-four 5,000-gallon water bladders worth $2,400 each to the National Water Company (ANDA) on March 25, 1987 from relief supplies left over after the earthquake. We could only find 18 water bladders and ANDA personnel did not know where the other 6 bladders were.

Seventh, it was not clear if the total number of duplicate home and business loans had been identified. The Salvadoran Bank Association (ABANSA) was responsible for identifying duplicate loans by matching loan applications submitted to it by the financial institutions. In ABANSA's latest report, dated March 24, 1987, we noted that participating institutions had received 9,623 home and 3,071 business loan applications. Price Waterhouse reported in its August 31, 1987 report that 10,609 home and 2,970 business applications had been received by the institutions. Price Waterhouse obtained its information directly from the institutions. It was unclear why Price Waterhouse reported fewer business loans than were reported by ABANSA five months earlier. More disturbing, however, is the possibility that ABANSA may not have had the universe of home loan applications in its computer memory at the time it performed its duplicate loan search. Price Waterhouse showed nearly 1,000 more home loan applications than reported by ABANSA. The differences in loan data reported by ABANSA and Price Waterhouse need to be examined during the follow-on Price Waterhouse audit. The Mission needs to assure itself that the duplicate loan search was based on the full loan universe at the time it was performed. If not ABANSA's data bank should be updated and another search performed.

AUDIT OF A.I.D. ASSISTANCE TO THE GOVERNMENT OF EL SALVADOR FOR EARTHQUAKE RELIEF, REHABILITATION AND RECONSTRUCTION DURING FISCAL YEAR 1987

PART III - EXHIBITS AND APPENDICES

EARTHQUAKE RECOVERY PROGRAM 519-0311

USAID/EL SALVADOR FINANCIAL STATEMENTS AS OF SEPTEMBER 30, 1987
In U.S. Dollars

COMPONENT NAME	OBLIGATIONS (1)	EXPENDITURES: LIQUIDATIONS (2)	EXPENDITURES: DIRECT AID EXPENDITURES (3)	EXPENDITURES: (2+3) TOTAL (4)	ACCRUALS (5)	(4+5) ACCRUED EXPENDITURES (6)
1- Employment Generation/Rubble Removal	2,200,000	0	0	0	1,940,000	1,940,000
2- Micro & Small Business Credit Line	10,000,000	5,992,434	0	5,992,434	4,007,566	10,000,000
3- Temporary Shelter	4,460,000	0	3,709,879	3,709,879	210,498	3,920,377
4- Slum Rehabilitation	3,340,000	0	0	0	0	0
5- Home Repair Credit Line	21,562,078	13,606,399	0	13,606,399	6,355,679	19,962,078
6- Public Services Restoration	8,437,922	0	178,444	178,444	6,510,385	6,689,329
PROGRAM TOTALS	50,000,000	19,598,833	3,888,323	23,487,156	19,024,128	42,511,784

COMPONENT NAME	DISBURSEMENTS: TOTAL ADVANCES (1)	DISBURSEMENTS: DIRECT AID PAYMENTS (2)	DISBURSEMENTS: (1+2) TOTAL (3)	ADVANCES: LIQUIDATED (1)	ADVANCES: OUTSTANDING (2)	(1+2) TOTAL (3)
1- Employment Generation/Rubble Removal	2,200,000	0	2,200,000	0	2,200,000	2,200,000
2- Micro & Small Business Credit Line	10,000,000	0	10,000,000	5,992,434	4,007,566	10,000,000
3- Temporary Shelter	270,484	3,709,879	3,980,363	0	270,484	270,484
4- Slum Rehabilitation	2,546,356	0	2,546,356	0	2,546,356	2,546,356
5- Home Repair Credit Line	21,562,078	0	21,562,078	13,606,399	7,955,679	21,562,078
6- Public Services Restoration	7,879,807	178,444	8,058,251	0	7,879,807	7,879,807
PROGRAM TOTALS	44,458,725	3,888,323	48,347,048	19,598,833	24,859,892	44,458,725

1/ Financial Statements were prepared by RIG/A/T auditors from the following sources: Columns 1, 4 and 5 of the schedule for OBLIGATIONS, EXPENDITURES AND ACCRUALS were taken from USAID EL SALVADOR'S "Project Financial Status Report" as of September 30, 1987. Columns 1 and 2 of the schedule for DISBURSEMENTS, and columns 1 and 2 of the schedule for ADVANCES were taken from USAID/El Salvador's Payment Vouchers.

EXHIBIT 2

EARTHQUAKE RECOVERY PROGRAM (519-0321)
SETEFE FINANCIAL STATEMENTS AS OF SEPTEMBER 30, 1987 1/
(In U.S. Dollars)

COMPONENT NAME	AMOUNT OBLIGATED	ADVANCES FROM AID	ADVANCES TO IMPLEMENTING AGENCIES	DETAILED FINANCIAL STATEMENTS
1 - Employment Generation/Rubble Removal	2,200,000	2,200,000	2,152,866	Exhibit 2-1
2 - Micro & Small Business Credit Line	10,000,000	10,000,000	9,280,000	Exhibit 2-2
3 - Temporary Shelter	4,460,000	270,484	196,376	Exhibit 2-3
4 - Slum Rehabilitation	3,340,000	2,546,336	1,210,266	Exhibit 2-4
5 - Home Repair Credit Line	21,562,078	21,562,078	18,840,089	Exhibit 2-2
6 - Public Services Restoration	8,437,922	7,879,807	5,836,471	Exhibit 2-5
	50,000,000	44,458,725	37,516,068	

1/ Financial statements were prepared by RIG/A/T auditors from SETEFE's "Financial Report" as of September 30, 1987.

EXHIBIT 2-1

DETAILED SETEFE FINANCIAL STATEMENT AS OF SEPTEMBER 30, 1987
EMPLOYMENT GENERATION/RUBBLE REMOVAL
(In U.S. Dollars)

RECEPIENT INSTITUTION	OBLIGATED	ADVANCES FROM AID	ADVANCES TO IMPLEMENTING AGENCIES
1 - CREM/SAN SALVADOR MAYOR'S OFFICE			
* Payrolls and purchases of tools	2,020,000	2,020,000	2,019,784
2 - MINISTRY OF PUBLIC WORKS			
* Rubble removal and transportation	179,444	179,444	132,526
3 - CREM/ORE			
* Tools transportation	556	556	556
COMPONENT TOTAL	2,200,000	2,200,000	2,152,866

DETAILED SETEFE FINANCIAL STATEMENTS AS OF SEPTEMBER 30, 1987
(In U.S. Dollars)

MICRO AND SMALL BUSINESS CREDIT LINE

PARTICIPATING FINANCIAL INSTITUTION	AMOUNT OBLIGATED	ADVANCES FROM AID	ADVANCES TO IMPLEMENTING AGENCIES
1 - BANCO HIPOTECARIO	1,052,600	1,052,600	1,052,600
2 - BANCO AGRICOLA	1,380,200	1,380,200	1,380,200
3 - BANCO CAPITALIZADOR	588,400	588,400	588,400
4 - BANCO CUSCATLAN	1,216,800	1,216,800	1,056,800
5 - BANCO DE CREDITO POPULAR	728,200	728,200	728,200
6 - BANCO SALVADORENO	1,725,800	1,725,800	1,565,800
7 - BANCO DE DESARROLLO E INVERSION	617,000	617,000	617,000
8 - BANCO FINANCIERO	406,400	406,400	335,400
9 - BANCO DE COMERCIO	1,095,619	1,095,619	1,226,600
10 -BANCO MERCANTIL	509,000	509,000	409,000
11 -FIGAPE	679,981	679,981	320,000
COMPONENT TOTAL	10,000,000	10,000,000	9,280,000

HOME REPAIR CREDIT LINE

PARTICIPATING FINANCIAL INSTITUTION	AMOUNT OBLIGATED	ADVANCES FROM AID	ADVANCES TO IMPLEMENTING AGENCIES
1 - BANCO HIPOTECARIO	2,780,000	2,780,000	2,780,000
2 - BANCO AGRICOLA	2,720,000	2,720,000	2,463,000
3 - BANCO CAPITALIZADOR	1,006,000	1,006,000	995,400
4 - BANCO CUSCATLAN	2,155,711	2,155,711	1,632,600
5 - BANCO DE CREDITO POPULAR	670,689	670,689	670,689
6 - BANCO SALVADORENO	2,614,000	2,614,000	2,497,800
7 - BANCO DE DESARROLLO E INVERSION	1,228,000	1,228,000	1,228,000
8 - BANCO FINANCIERO	279,200	279,200	273,000
9 - BANCO DE COMERCIO	1,061,000	1,061,000	688,200
10 -BANCO MERCANTIL	588,800	588,800	520,400
11 -APRISA	545,400	545,400	381,400
12 -CRECE	731,278	731,278	618,400
13 -CREDISA	1,435,600	1,435,600	1,124,200
14 -AHORROMET	906,400	906,400	636,200
15 -CASA	539,800	539,800	426,200
16 -CENTRAL DE AHORROS	899,600	899,600	758,000
17 _ATLACATL	1,400,600	1,400,600	1,146,600
COMPONENT TOTAL	21,562,078	21,562,078	18,840,089

DETAILED SETEFE FINANCIAL STATEMENT AS OF SEPTEMBER 30, 1987
TEMPORARY SHELTER
(In U.S. Dollars)

RECEPIENT INSTITUTION	AMOUNT OBLIGATED	ADVANCES FROM AID	ADVANCES TO IMPLEMENTING AGENCIES
1 - SAN SALVADOR MAYOR'S OFFICE			
+ Logistics, Distribution of Materials and census of earthquake victims	40,746	30,484	40,046
2 - CREM 1/			
+ Local purchases of wood, roofing sheets and nails.	200,000	200,000	156,329
3 - UNASSIGNED	509,376	40,000	0
	750,121	270,484	196,376
PLUS AID DIRECT PURCHASES: 1/			
+ Wood, roofing sheets and nails	3,709,879	0	0
COMPONENT TOTAL	4,460,000	270,484	196,376

1/ CREM figures were adjusted by RIG auditors to exclude a $412,539 Mission reimbursement to SETEFE which was erroneously presented in the SETEFE financial report as an advance. RIG auditors reclassified the amount obligated (budgeted) for this reimbursement as an AID direct purchase.

DETAILED SUB-PROJECT STATEMENT AS OF SEPTEMBER 30, 1987
... REHABILITATION
(U.S. Dollars)

SUB-COMPONENT / BENEFICIARY GROUP	AMOUNT OBLIGATED	ADVANCES FROM AID	ADVANCES TO IMPLEMENTING AGENCIES
1 - INFRASTRUCTURE REHABILITATION			
GROUP 1			
* Modelo 2	81,817	81,817	81,817
* Isidro Menendez	15,190	15,190	15,190
* Papini	10,707	10,707	10,707
* Corp Nuevo	38,582	38,582	38,582
GROUP 2			
* Adesco Sol	42,427	42,427	42,427
* Quinonez	106,989	106,989	106,989
GROUP 3			
* Minerva	54,852	54,852	54,852
* Corazon de Maria	145,515	145,515	131,670
GROUP 4			
* Altos de San Francisco	92,726	92,726	92,726
* Nicaragua	23,317	23,317	23,317
GROUP 5			
* 22 de Abril	39,857	39,857	39,857
* Sanchez	42,777	42,777	25,810
* Dario Gonzalez	9,139	9,139	9,139
GROUP 6			
* Canteras de Aragon	33,136	33,136	33,136
* El Granjero	31,102	31,102	31,102
GROUP 7			
* La Roca	64,000	64,000	0
* La Fosa	21,649	21,649	0
* Bambu 4	10,000	10,000	0
GROUP 8			
* Zone 2 Relocation	114,795	114,795	0
* Zone 3 Relocation	164,698	164,698	0

DETAILED SPTEFE FINANCIAL STATEMENT AS OF SEPTEMBER 30, 1987
SLUM REHABILITATION
(In U.S. Dollars)

SUB-COMPONENT/ BENEFICIARY GROUP	AMOUNT OBLIGATED	ADVANCES FROM AID	ADVANCES TO IMPLEMENTING AGENCIES
GROUP 9			
* Asuncion	7,088	7,088	0
* Santa Cecilia	3,352	3,352	0
* Fortaleza	100,435	100,435	0
* Don Bosco Concepcion	7,957	7,957	0
* Fernadesal	6,536	6,536	0
* Escuela Gonzalez	3,449	3,449	0
OTHER GROUPS			
* Iberia	150,000	150,000	0
* Nunez Arrue	3,530	3,530	0
CONTINGENCIES	285,046	285,046	52,026
2 - RELOCATION PROJECTS			
* 10 de Octubre	446,356	446,356	383,656
* La Selva	0	0	0
3 - SUPERVISION	49,727	49,727	37,264
4 - UNASSIGNED	1,133,644	340,000	0
COMPONENT TOTAL	3,340,000	2,546,356	1,210,266

DETAILED BUDGET FINANCIAL STATEMENT AS OF SEPTEMBER 30, 1987
PUBLIC SERVICES RESTORATION
(In U.S. Dollars)

RECEPIENT INSTITUTION/ACTIVITY	OBLIGATED	ADVANCES FROM AID	ADVANCES TO IMPLEMENTING AGENCIES
1 - MINISTRY OF HEALTH			
* BLOOM Hospital's temporary installation	500,000	500,000	400,000
* NEUMOLOGICO Hospital temporary installation	174,000	174,000	151,358
* NEUMOLOGICO: Consultants and Design	23,000	23,000	22,998
* MATERNITY: Consultants and design	17,000	17,000	17,000
* ROSALES Hospital: warehouse reconstruction	52,000	52,000	44,924
* ROSALES Hospital: emergency repairs	200,000	200,000	200,000
	966,000	966,000	836,279
2 - MINISTRY OF EDUCATION			
* School reconstruction & temporary classrooms	2,321,701	2,301,163	1,713,000
* Purchases of wood (AID direct payment)	178,444	0	0
* School Desks purchases (AID direct payment)	199,855	0	0
	2,700,000	2,301,163	1,713,000
3 - NATIONAL WATER AGENCY (ANDA)			
* Rehabilitation of water distribution system	1,200,000	1,200,000	1,200,000
4 - ELECTRICITY COMPANY (CEL)			
* Public lighting restoration, and others.	600,722	600,722	520,000
* Structural Steel (AID direct payment)	119,278	0	0
	720,000	600,722	520,000
5 - MUNICIPALITIES/CEL			
* Mejicanos Municipality	36,832	36,832	36,832
* Ayutuxtepeque market	20,240	20,240	20,240
* Cuscatancingo: Mayor's office and market	21,075	21,075	21,075
* Contingencies	21,800	21,800	21,800
* Unassigned	53	53	53
	100,000	100,000	100,000
6 - SOCIAL SECURITY INSTITUTE (ISSS)			
* Construction of 7 temporary structures	440,000	440,000	210,000
7 - MINISTRY OF AGRICULTURE AND LIVESTOCK (MAG)			
* Protection of conservationist infrastructure	15,000	15,000	15,000

DETAILED SETEFE FINANCIAL STATEMENT AS OF SEPTEMBER 30, 1987
PUBLIC SERVICES RESTORATION
(In U.S. Dollars)

RECIPIENT INSTITUTION/ACTIVITY	OBLIGATED	ADVANCES FROM A.I.D	ADVANCES TO IMPLEMENTING AGENCIES
8 - MUNICIPALITY OF SAN SALVADOR (MARKETS)			
* San Miguelito: sales stands	40,665	40,665	40,665
* San Miguelito: child care center	9,720	9,720	9,422
* Modelo: sales stands	2,022	2,022	2,022
* Tinetti: sales stands	35,915	35,915	35,915
* Tinetti: child care center repairs	10,000	10,000	6,848
* San Jacinto: repairs	4,600	4,600	4,600
* Market No. 5: design	320,000	320,000	11,968
* La Tiendona: rehabilitation	155,000	155,000	68,151
* San Miguelito: demolition of roof and child care center	120,000	120,000	107,600
* San Miguelito: design of roof and child care center	60,000	60,000	15,000
	757,922	757,922	302,192
9 - JUSTICE DEPT. (REGISTRY)			
* Temporary location at International Fair	120,000	120,000	120,000
10 -MINISTRY OF FINANCE			
* Temporary location at International Fair	120,000	120,000	120,000
11 -POSTAL SYSTEM/CEL			
* Temporary location at International Fair	60,000	60,000	60,000
12 -ATTORNEY GENERAL OFFICE/CEL			
* Temporary location at Children's Park	180,000	140,000	180,000
13 -NATIONAL ASSEMBLY			
* Building repairs	60,000	60,000	60,000
14 -MINISTRY OF PUBLIC WORKS			
* Bridges repairs	765,000	765,000	400,000
15 -CONTINGENCIES	234,000	234,000	0
COMPONENT TOTAL	8,437,922	7,879,807	5,836,471

ACCOUNTING FOR OTHER AID 1/
FUNDS OR COMMODITIES OBLIGATED OR
USED FOR ACTIVITIES ASSOCIATED WITH THE EARTHQUAKE
DURING FISCAL YEAR 1987

Activity	Funding Source 2/	Fiscal Year Funds 4/	Amount	Obligation/ Use Date 4/	Purpose of Activity
A. International Disaster Assistance for Emergency Relief Accounted for by OFDA	IDA	-	$2,550,000	-	Commodities, transportation and personnel provided for emergency relief
B. PL 480 Title II Commodities	USDA	-	$ 902,600	-	Commodities provided for the emergency food distribution program
C. A.I.D./GOES Jointly Programmed Local Currencies					
1. Operating Expense Trust Funds	GOES	-	$ 232,867	-	Emergency procurement for USAID/El Salvador (i) removal of office equipment, (ii) equipment/material purchases, (iii) rental of vehicles, (iv) personal services, and (v) maintenance supplies necessitated by earthquake disaster
2. Economic Support Funds (ESF)	GOES	-	$2,006,901	-	Funds provided to the Office of the Presidency and public utilities for costs associated with the earthquake
Sub-Total Local Currency			$2,239,768		
D. USAID/El Salvador Activities Funded with Appropriated U.S. Dollars					
1. Operating expenses	OE 3/	-	$3,435,700	-	Special rest and recuperation for USAID employees assisting in earthquake program; equipment and supplies associated with the earthquake program. Partial payment for purchase of new A.I.D. building for $5 million 3/

ACCOUNTING FOR OTHER AID 1/
FUNDS OR COMMODITIES OBLIGATED OR
USED FOR ACTIVITIES ASSOCIATED WITH THE EARTHQUAKE DURING FISCAL YEAR 1987

Activity	Funding Source 2/	Fiscal Year Funds	Amount	Obligation/ Use Date	Purpose of Activity
2. Program Development and Support (PD&S) Earthquake (Project No. 519-0332)	ESF	-	$ 999,999	-	Personal services contracts, equipment, vehicle rentals, administrative costs associated with the earthquake recovery program, including Price Waterhouse monitoring contract.
3. Public Services Restoration (Project No. 519-0279)	ESF	86 & 87	421,409	11/86 to 2/87	Procurement of items (e.g. generators, circuit breakers, etc.) for the electric utility company to repair or replace items damaged by the earthquake
4. Health System Vitalization (Project No. 519-0291)	DA	Multiple Years	112,768	11/14/86	Contractor used to dispense medication to earthquake victims
5. Program Development and Support (Project No. 519-0167)	ESF	85	30,058	10/21/86	Contract to monitor emergency commodity distribution during the earthquake aftermath
6. Program Development and Support (Project No. 519-0168)	DA	87	20,000	2/15/87	Contract with the University of New Mexico to assess damages caused by the earthquake
7. Program Development and Support (Project No. 519-0177)	DA	85	16,467	1/22/87	Review of earthquake damages and vehicle rental support
8. Program Development and Support (Project No. 519-0177)	DA	87	117,000	11/21/86	Contractor was partly used to draft and review scopes of work for consultants pursuant to needs resulting from the earthquake
9. Program Development and Support (Project No. 519-0177)	DA	87	192,190	1/13/87	PSC contractor for program monitoring, administration and design for the Earthquake Recovery Program and the Earthquake Reconstruction Project
10. Program Development and Support (Project No. 519-0177)	DA	87	209,562	1/13/87	PSC contract to monitor material distribution during earthquake aftermath

ACCOUNTING FOR OTHER AID 1/
FUNDS OR COMMODITIES OBLIGATED OR
USED FOR ACTIVITIES ASSOCIATED WITH THE EARTHQUAKE DURING FISCAL YEAR 1987

Activity	Funding Source 2/	Fiscal Year Funds	Amount	Obligation/ Use Date	Purpose of Activity
11. Program Development and Support(Project No. 519-0177)	DA	87	82,600	3/30/87	Contract with U.S. Geological Survey to evaluate seismic hazards
12. Program Development and Support (Project No. 519-0177)	DA	87	8,177	3/13/87	Contract to prepare report on the earthquake disaster
13. Program Development and Support (Project No. 519-0177)	DA	86	130,000	11/1/86	Contract with Arthur Young to monitor the earthquake relief program
Sub-total U.S. Dollar Accounts			$ 5,775,930		
Grand Total			$11,468,298		

1/ The amounts shown in this Exhibit funded activities not discussed elsewhere in this report and were obtained from USAID El Salvador reports and records. Because of severe time constraints, limited audit coverage was provided to the activities included in this Exhibit. As a result other A.I.D. funds not included in this Exhibit could have been used for the earthquake recovery.

2/ Acronyms are defined as follows: IDA (International Disaster Assistance), USDA (U.S. Department of Agriculture), GOES (Government of El Salvador), OE (Operating Expense), ESF (Economic Support Fund) and DA (Development Assistance). Appropriation codes were not identified for items A, B, C, D1 and D2.

3/ $121,000 funded by A.I.D. and $2,679,000 funded by Department of State (may not be State operating expenses).

4/ The Fiscal Year of the funds and the obligation/use date were not identified for items A, B, C, F1 and D2 because a legal opinion was not recommended for these items.

ANALYSIS OF AUDIT COVERAGE OF U.S. GOVERNMENT ASSISTANCE 1/
PROVIDED FOR EL SALVADOR IN RESPONSE TO THE
EARTHQUAKE DURING FISCAL YEAR 1987

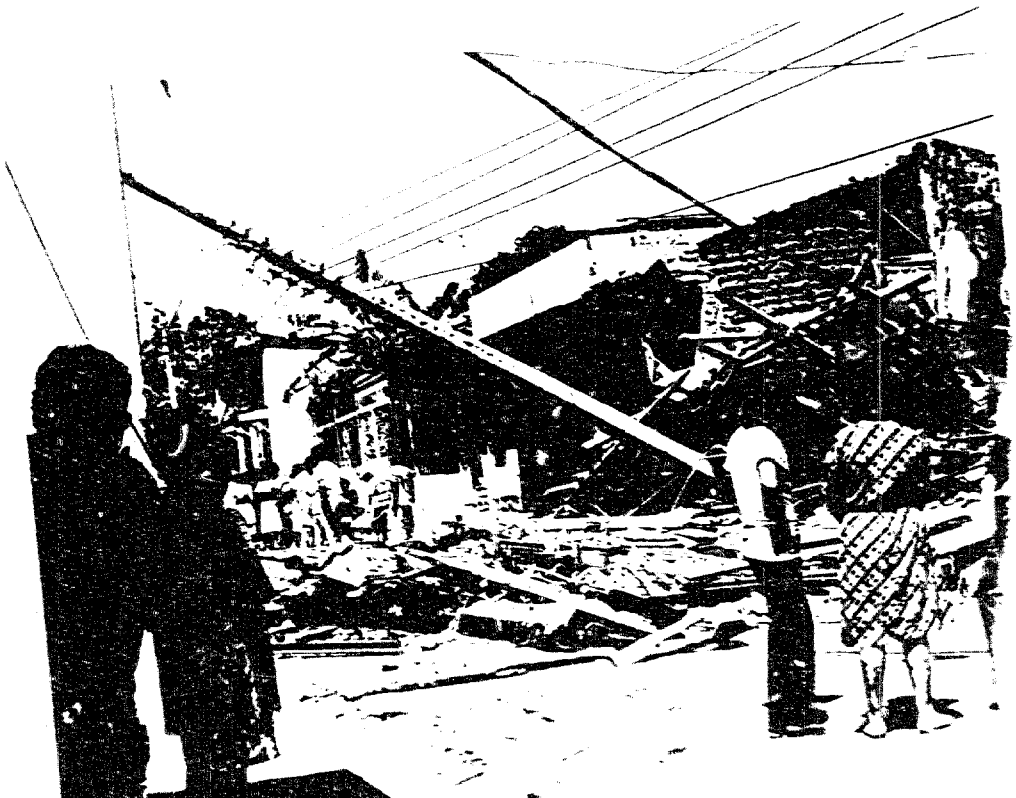
Sources of Funding	Resources Obligated/ Committed	Funds Expended/ Commodities Provided	Type of Assistance	Discussed In Report	Audit Coverage
Emergency Relief					
USA (IDA)	$ 2,550,000	$ 2,550,000	Commodities, Transportation and Personal Services	Exhibit 3; Appendix 2	
USA (IDA)	25,000	$ 2,185	Ambassador's Grant for Relief Supplies	Finding 5; Appendices 7, 8	
USA (IDA)	25,000	$ NA	OFDA Grant for Relief Supplies (519-0330)	Finding 5; Appendix 7	
USDA	902,600	$ 902,600	PL 480 Title II Commodities for GOES Emergency Feeding Program	Exhibit 3; Appendix 3	
Subtotal	$ 3,502,600				
Recovery:					
IDA	$ 50,000,000	$23,487,156	Earthquake Recovery Program (519-0331)	Findings 1, 2, 3; Exhibits 1, 2 Appendices 4, 6, 7, 8, 9, 10	
USA (IDA)	300,000	$ 253,395	Emergency Shelter Support (519-0330)	Appendices 5, 7, 8, 9,	
GOES	2,239,768	$ NA	A.I.D./GOES Jointly Programmed Local Currencies	Exhibit 3	None
U.S. DOE State	5,775,930	$ NA	Other USAID/El Salvador Activities Funded with Appropriated U.S. Dollars	Finding 4; Exhibit 3	
IBRD	75,000,000	$ -	Earthquake Reconstruction Project (519-0333)	Background	None
Subtotal	$133,315,698				
Grand Total	$136,818,298				

1/ Sources are defined as follows: IDA (International Disaster Assistance), USDA (U.S. Department of Agriculture), GOES (Government of El Salvador), OE (Operating Expense), ESF (Economic Support Fund), DA (Development Assistance) OFDA (Office of Foreign Disaster Assistance [illegible] (Department of State); and NA (Information not available).

2/ Noted in the scope section of the audit report, findings, exhibits and appendices

PHOTOGRAPHS OF DAMAGE CAUSED BY
THE EARTHQUAKE OF
OCTOBER 10, 1986

Earthquake damages to the "Ruben Dario" Building. More than 200 people were killed when the building collapsed.



Earthquake damages to houses and electrical services, in the San Jacinto area.

ACCOMPLISHMENTS OF OFDA EMERGENCY RELIEF PROGRAM 1/

The A.I.D. Office of U.S. Foreign Disaster Assistance (OFDA) with the assistance of USAID/El Salvador managed the U.S. government's emergency relief program. According to the USAID/El Salvador Earthquake Disaster Report, OFDA contributed a total of about $2,900,000 for emergency relief mainly during the first two weeks following the earthquake. OFDA provided $2,550,000 in transportation services, personnel and commodities, and $350,000 to USAID/El Salvador for temporary shelter and relief supplies. The major commodities provided were:

- 1,433 rolls of plastic sheeting
- 1,741 tents
- 6,900 blankets
- 340 body bags
- 50 litters
- 36 water bladders (3,000 gallon capacity)

The GOES and the U.S. government effectively organized their relief operations to respond to the earthquake of October 10, 1986. The GOES established an ad hoc private sector committee called the Business Commission for Disaster Assistance (COEDA) to receive and account for national and international contributions of material and money. On October 24, 1986, COEDA's function to monitor donations was transferred to the National Emergency Committee (COEN).

OFDA sent a five-member team to San Salvador to coordinate the A.I.D. relief effort. This team was supplemented with up to 20 USAID/El Salvador personnel including the Mission's Disaster Relief Officer. USAID/El Salvador assigned one of its contractors (Arthur Young and Company) to computerize and keep track of goods received and to audit inventories. USAID/El Salvador also assigned its Private Sector Office to assist COEDA in its relief efforts.

COEDA required that all commodities received from other countries be accounted for before being distributed. The fairgrounds were designated as the assembly point for all incoming international relief supplies. Arthur Young and Company was assigned the responsibility to account for the receipt and distribution of all relief supplies. In November 1986 Arthur Young issued three reports that accounted for the receipt and distribution of commodities and money contributed by international donors.

1/ The information included in this Appendix was obtained from records and interviews with officials of USAID/El Salvador and was not independently verified by I.G. auditors, unless otherwise indicated in this Appendix.

Although we did not audit the A.I.D. emergency relief operation, our review of reports and interviews with USAID/El Salvador officials suggests that the A.I.D. effort was timely, substantial and well managed. The U.S. responded quickly with emergency relief. The U.S. Ambassador declared a disaster on the day of the earthquake. Most of the U.S. emergency relief was flown to the city on U.S. military flights. Within hours of the earthquake two helicopters arrived from Honduras with medical supplies. By noon of the next day, four C-130's had arrived bringing personnel and relief supplies. Many U.S. Embassy and USAID/El Salvador personnel and A.I.D.-financed contractors were assigned to assist in the relief effort. USAID/El Salvador also established internal controls to account for the receipt and distribution of relief supplies. A.I.D. commodities not used for the relief operations (255 tents and 24 water bladders) were accounted for and donated to the GOES for future disasters. We inventoried the A.I.D. commodities donated to the GOES and found that the tents were fully accounted for but that six of 24 water bladders were missing and could not be accounted for.

ACCOMPLISHMENTS OF PL 480 TITLE II EMERGENCY FOOD DISTRIBUTION PROGRAM 1/

According to USAID/El Salvador's Earthquake Disaster Report, the most critical need after the quake was food. Many persons had lost their food supplies or their resources to purchase more, especially if they lost their source of income. Local markets and stores lost large quantities of food or were shut down and were not able to satisfy the food demand.

The distribution of food to meet the immediate emergency demands in the first weeks was carried out by the GOES, Red Cross, the Archdiocese's Ecclesiastical Emergency Committee, and other groups. Although some food donations were sent by plane from other countries, by far the major portion of food to feed the quake victims came from PL 480 Title II inventories in El Salvador and Guatemala. According to USAID/El Salvador, 4,207.3 metric tons of PL 480 food commodities valued at $902,600 were used in the emergency food distribution program.

The United States Government agreed to replenish the commodities used in the program. We verified that this had taken place for 3,204 metric tons borrowed from PL 480 Title II stocks in El Salvador.

An estimated 130,793 families received emergency food rations during the food distribution program. In the first 11 days of the emergency, GOES authorities distributed 15-day rations to an estimated 60,000 families. By November 1, 1986, Ecclesiastical Emergency Committee had distributed one month provisions to 38,793 families. In the first month after the quake, the Red Cross had distributed 7-day rations to 32,000 families.

1/ The information included in this Appendix was obtained from records and interviews with officials of USAID/El Salvador and was not independently verified by IG auditors, unless otherwise indicated in the report.

ACCOMPLISHMENTS OF EL SALVADOR EARTHQUAKE RECOVERY PROGRAM 1/ (Project No. 519-0331)

On November 21, 1986 A.I.D. granted to GOES $50 million for the El Salvador Earthquake Recovery Program (Project No. 519-0331). The purpose of the project was to assist the GOES in meeting basic human needs and reviving economic activity in the areas severely affected by the earthquake. The project was to be completed by November 20, 1987, but was extended to January 20, 1988. As of September 30, 1987, the project budget and expenditures consisted of the following:

Component	Budget	Expenditures
1) Employment Generation/Rubble Removal	$ 2,200,000	$ -
2) Micro/Small Business Credit	10,000,000	5,992,434
3) Temporary Shelter	4,460,000	3,709,879
4) Slum Rehabilitation	3,340,000	-
5) Home Repair/Reconstruction Credit	21,562,078	13,606,399
6) Restoration of Public Services	8,437,922	178,444
	$50,000,000	$23,487,156

The official GOES representative for the project was the Ministry of Planning. The Ministry was to be responsible for controlling disbursements and accounting for program funds, which they assigned to its Technical Secretariat for External Financing (SETEFE). SETEFE was to disburse funds directly to the implementing agencies from a separate local currency account, with the approval of the National Emergency Finance Committee (COMFIEN).

The Committee for Metropolitan Reconstruction (CREM) (which was created by Legislative Decree No. 563 dated December 23, 1986) was responsible for overall direction and implementation of the project. Because the CREM had attempted several times to engage in questionable procurement practices, USAID/El Salvador and the GOES agreed on February 5, 1987 to establish a Special Procurement Commission (CEA) to manage the acquisition of all goods and services financed with project funds.

On January 5, 1987 USAID/El Salvador contracted a Senior Special Assistant to coordinate the activities of USAID/El Salvador staff in the implementation of the project. The Senior Special Assistant was under the supervision of the Associate Mission Director for Operations.

1/ The information contained in this Appendix has not been verified by the RIG auditors, unless otherwise indicated in the Appendix.

A description of the six project components, as modified during project implementation, follows:

1. Employment Generation/Rubble Removal

The objective of this component was to finance up to 1.2 million person-days of labor to remove rubble to areas where it could be picked up and trucked to appropriate dump sites. Picks, shovels, wheelbarrows and related tools necessary for the work were to be purchased. Trucks and front-end loaders were to be rented. The CREM was to be the central coordinating mechanism for this component.

This activity was to be implemented by the CREM with the assistance of the Municipality of San Salvador and the Ministry of Public Works. This component was completed in June 1987. According to USAID/El Salvador, a total of 897,206 person-days of work was generated compared to projections of 1.2 million person-days, while 114,608 cubic meters of rubble was removed as of December 31, 1987. The original budget for the component was $4 million but actual estimated costs were only $2.2 million. Costs were lower than planned because (1) less labor was required than estimated, (2) labor was supervised by the Municipality of San Salvador instead of through a contract with a private company, and (3) trucks and equipment were obtained at lower cost from the Ministry of Public Works than from commercial sources.

2. Micro/Small Business Repair Credit

The objective of this component was to finance 5,000 loans to micro and small businesses for the reconstruction and repair of buildings, the replacement or repair of machinery and equipment, and the replacement of inventories and working capital. The loans were to be administered by existing financial institutions under a contract with the Ministry of Planning. Micro businesses with assets of up to $20,000 or small businesses with assets of up to $100,000 would be eligible to receive loans. Loan terms would be at 5 percent interest for 3 to 12 years, up to a maximum loan of $10,000 for micro businesses and $15,000 for small businesses. Reflows were to be deposited in the Central Bank to be used for similar purposes as agreed to between the GOES and A.I.D.

Approximately 3,070 business loan applications totaling $15 million were received under this credit line component. As of September 30, 1987 SETEFE had advanced $9.3 million, of which nearly $8.8 million, or 95 percent of the total advanced, had been disbursed for 2,340 loans.

Between September 30, 1987 and the termination date of the earthquake recovey program on January 20, 1988, the total advanced under the program was reduced by $253,680 to $9 million. Of this amount $8.9 million had been disbursed for 2,299 loans. This difference appears to represent a refund to SETEFE for ineligible business loans and a reprogramming of funds for home repair loans. The actual number of business loans was less than the 5,000 planned because the average loan amount was greater than originally anticipated.

For the most part, it appeared that the business loans went to qualified program recipients and were used for appropriate purposes. However, as discussed in finding No. 1, an undetermined amount of funds also went to individuals who did not qualify for program benefits and/or were used for ineligible purposes.

3. Temporary Shelter

The objective of this component was to provide packages of building materials (wood and galvanized metal sheeting) for the erection of temporary shelter to an estimated 32,495 families whose homes were damaged or destroyed by the earthquake. The municipalities were to identify the needs in each neighborhood. CREM was to purchase the materials and the municipalities were to make the distributions.

According to USAID/El Salvador, 34,498 families had received building materials for the construction or repair of a temporary shelter as of September 30, 1987. The A.I.D. distribution system included approximately 9% galvanized metal sheeting contributed by other donors. All wood, however, was contributed by A.I.D. and the total number benefitted came to 34,498 families, of which some 3,000 had also received limited amounts (partial packages to complement other assistance received) of building materials under the Emergency Shelter Support project (519-0330).

Price Waterhouse (under their monitoring contract with USAID/El Salvador) sampled 474 end-users from a universe of 32,505 in order to determine the disposition of the building materials. The sample results showed that 97 percent of beneficiary families had received the material. Sixty percent of the families had built temporary shelters with the materials and 31 percent of the families had the materials in storage. The remaining six percent that received material sold or gave it to others. Since Price Waterhouse's sample was not randomly selected, we could not project the sample's results to the beneficiary universe.

We drew a random sample of the Price Waterhouse sample to verify the accuracy of their work. A sample of 30 out of the original universe of 474 was selected. The results showed that 17 of the 30 families were found (which is not surprising considering that this was a temporary housing program) and of the 17 families found, 14, or 82 percent, had used their building materials.

In comparing the results of both samples, we found minimal differences. Therefore, we concluded that Price Waterhouse's sample could be reasonably relied upon.

According to USAID/El Salvador, an additional 1,626 families received building materials between September 30, 1987 and the end of the project, bringing the grand total of beneficiaries under this component to 36,124 families.

4. Slum Rehabilitation

The objective of this component was to repair or reconstruct small civil works subprojects such as retaining walls, curbings, drainage structures, side walks and other small-scale infrastructure, damaged by the earthquake. Such subprojects were to be carried out in approximately 12 of the 80 slum areas in the Municipality of San Salvador as mutually agreed by A.I.D. and the GOES. Individual subprojects were to be contracted out to qualified private sector firms. The Vice Minister of Housing was to be responsible for the implementation of these activities.

As of September 30, 1987, 15 infrastructure subprojects and two relocation subprojects had been started. The infrastructure subprojects were about 55 percent complete and the relocation subprojects 70 percent. The infrastructure subprojects consisted of small civil works such as retaining walls. The relocation subprojects involved the resettlement and the provision of housing for 1,276 families.

By the completion of the Earthquake Recovery Program (January 20, 1988), a total of 25 infrastructure and two relocation subprojects had been started. According to USAID/El Salvador all of these subprojects were completed except as noted below. One of the infrastructure subprojects was discontinued after 12 percent completion because an easement had not been obtained to lay a sewage line across nonproject land. Also, a sewage pump had not been installed in a lift station in one of the relocation subprojects. In March 1988 we verified that the subprojects had been completed as reported by USAID/El Salvador.

5. Home Repair Credit

The objective of this component was to finance an estimated 8,000 loans to repair or reconstruct homes damaged or destroyed by the earthquake. Existing financial institutions were to administer the loans under a contract with the Ministry of Planning. Loans were to be made to persons of low or medium incomes up to a maximum amount of $4,000. The loans were to be made at an interest rate of 5 percent up to a term of 20 years. Reflows were to be deposited in the Central Bank to be used for similar purpose as agreed to by the GOES and A.I.D.

Approximately 9,623 home loan applications were received under this credit line component. As of September 30, 1987 SETEFE had advanced $18.8 million, of which $18.7 million, or 99 percent of the total advanced at that time, had been disbursed for 6,373 loans. From September 30, 1987 until the termination of this component in January 1988, an additional $2.1 million had been advanced bringing the total advanced for home loans to $20.9 million. Of this amount, $20.6 million had been disbursed for 7,195 loans.

For the most part, it appeared that the home loans went to qualified program recipients and used for appropriate purposes. However, as discussed in finding No. 1, an undetermined amount of funds also went to individuals who did not qualify for program benefits and/or were used for ineligible purposes.

6. Public Services Restoration

The objective of this component was to provide high priority repairs, equipment supplies and spare parts for public buildings, utilities and installations. The coordinating agency for these activities was to be the Commission for the Restoration of Public Services (CRESP).

According to an USAID/El Salvador report dated September 18, 1987, 41 public service restoration activities, managed by fourteen implementing agencies, were at various stages of completion ranging from 20 percent to 100 percent.

From September 18, 1987 to December 31, 1987, USAID/El Salvador reported that an additional 5 activities were completed by December 31, 1987. A.I.D. auditors contracted Price Waterhouse to selectively verify the completion of reported activities. Based on Price Waterhouse's work in March 1988, we concluded that the activities under the Public Sector Restoration component were satisfactorily completed.

In addition USAID/El Salvador reported to us in April 1988 that the number of subprojects financed under this component had increased from 46 to 63 and ultimately could reach 75. These additional subprojects represent public services restoration activities financed and completed by the GOES before January 20, 1988 which USAID/El Salvador has agreed to reimburse from unused project funds.

ACCOMPLISHMENTS OF EMERGENCY SHELTER SUPPORT 1/ (PROJECT NO. 519-0330)

The earthquake which struck San Salvador and the surrounding area on October 10, 1986 left tens of thousands of families homeless. The immediate response by the Government of El Salvador (GOES) during the first chaotic weeks after the disaster was to establish a program to begin procuring and distributing building materials (metal sheets, lumber and nails) to affected families. During this period, the GOES received several donations, including assistance from the Agency for International Development (A.I.D.).

Project Description

USAID/El Salvador and the Municipality of San Salvador signed a $300,000 limited-scope emergency shelter support project agreement. These funds were granted through A.I.D.'s Office of Foreign Disaster Assistance on October 23, 1986.

The project consisted of the purchase and delivery of corrugated roofing, lumber and nails to families who needed temporary shelter or who needed to make repairs to make their existing shelter habitable. Tools and wheelbarrows would also be supplied to communities as needed. The funds provided under the grant would cover the cost of purchasing roofing, lumber and nails, including the cost of transport to the building sites of approximately 5,240 temporary shelters. The Municipality of San Salvador was responsible for managing the project and for assuring strict control over all materials and tools purchased and delivered with project funds. The municipality was also responsible for maintaining separate and complete financial accounts for all project funds. This project was to end on January 20, 1987 but was extended to April 30, 1987.

Project Accomplishments

Based on the best information available, we estimate that 6,000 to 8,000 families benefited from this program. Since A.I.D.'s building material contribution was a little more than 60 percent of total donations to the project, we estimated that U.S. resources through the Emergency Shelter Support Project benefited between 3,780 to 5,040 families. Although the project's goal was to assist 5,240 families, it was curtaield early in order to permit a phased initiation of material distribution under the Earthquake Recovery Program (Project 519-0331).

1/ The information included in this Appendix was obtained from records and interviews with officials of USAID/El Salvador, Municipality of San Salvador and Contract Corporation of America and was not independently verified by IG auditors, unless otherwise indicated in this Appendix.

According to the Municipality of San Salvador, 7,538 families received building materials. The Contract Corporation of America (CCA), a firm hired by USAID/El Salvador to monitor project activities, reported that 6,191 beneficiary families received materials. According to USAID/El Salvador officials, CCA's figure did not include about 1,860 families who were served at the earliest stages of the program. This happened because the materials went directly to the communities and not through a distribution center where CCA personnel were located. Therefore, the total would come to about 8,051 beneficiaries.

In attempting to verify the number of beneficiaries reported by CCA, we discovered that CCA did not have source documents to support its figures. Additionally, the information provided by the Municipality of San Salvador could only be partially substantiated. Therefore, AID auditors, with the assistance of USAID/El Salvador and Price Waterhouse personnel, pieced together a beneficiary list of approximately 4,200 families based on information obtained from the Municipality of San Salvador and the building material distribution centers. In making our final analysis of potential beneficiary families served, we added about 1,860 families who were served at the earliest stages for a total of about 6,000. The added families were not part of our list of about 4,200 families because there were no names and addresses by which to identify them.

Based on our beneficiary list of 4,200 families, we drew a statistically valid sample of 80 families to be visited to verify the distribution and use of building materials. We employed Price Waterhouse to perform this work under our supervision. The sample had a 90 percent confidence level, a 5 percent rate of error and a 4 percent rate of precision.

The results of our sample were as follows:

(1) 64 percent (51) of the families were found. 42 families said they had used the materials, 8 families stated that they had the materials in storage, and one family said they had not received any materials.

(2) 36 percent (29) of the families were not found because they had moved, were not at home or their home could not be found.

Based on this sample, it is our opinion that a substantial percentage of the targeted beneficiaries did obtain building materials under this project.

Under the project agreement, the Municipality of San Salvador was responsible for managing the project and for ensuring the establishment of strict controls over all materials and tools purchased and delivered with project funds. We found that the Municipality of San Salvador and USAID/El Salvador had maintained controls in order to safeguard these materials. For example, delivery reports were utilized in order to move building materials from storage sites to distribution sites. In addition, USAID/El Salvador hired CCA in order to observe and monitor the movement and distribution of these goods. CCA provided USAID/El Salvador with periodic monitoring reports which outlined how much building material was delivered to the various distribution sites and how many beneficiaries were served.

The accountability of the materials distributed for the project may not have been adequate because material distribution figures compiled by CCA and the Municipality of San Salvador did not agree.

	CCA (As of January 30, 1987)	Municipality (As of February 25, 1987)
Items	Quantity	Quantity
Lumber (2"x4"x12')	22,595	30,892
Lumber (2"x2"x14')	14,867	11,257
Metal sheets	21,351	17,070

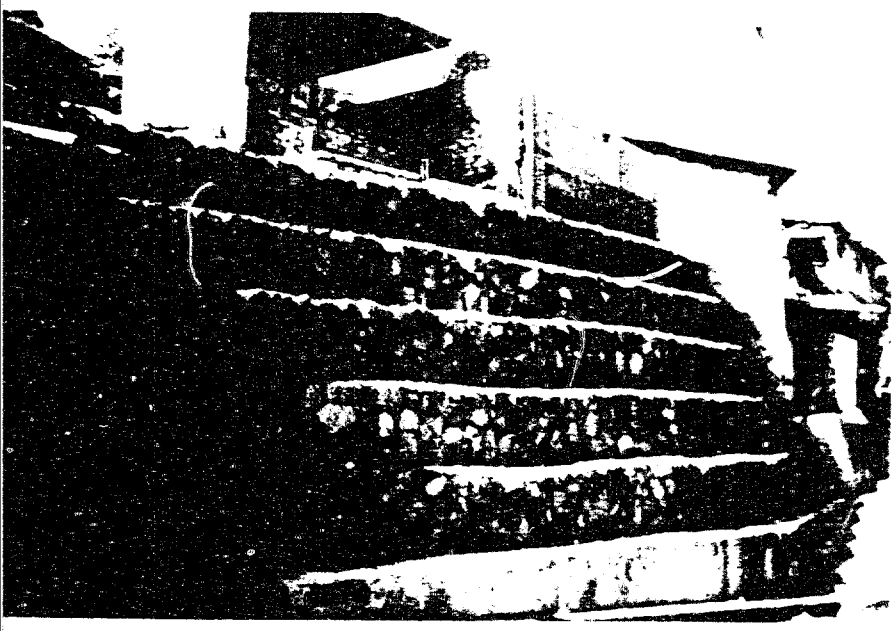
It should be pointed out that deliveries under this program had ended by February 6, 1987 in order to initiate the Temporary Shelter component of the Earthquake Recovery Program (Project 519-0331).

When the program ended, the Municipality reported the following quantities of building materials remaining in its inventory:

Items	Quantity
Lumber (2"x4"x12')	22,851
Lumber (2"x2"x14')	5,699
Metal sheets	28,792

The ending inventory represented about 50 percent of the total materials donated, most of which had been delivered by suppliers during the month of January. The Municipality of San Salvador used these materials under the Temporary Shelter Component of A.I.D.'s Earthquake Recovery Program (Project No. 519-0331).

PHOTOGRAPHS OF FACILITIES REPAIRED OR RECONSTRUCTED WITH FUNDS PROVIDED UNDER THE EL SALVADOR EARTHQUAKE RECOVERY PROGRAM (PROJECT No. 519-0331)



Retention wall built in the "FENADESAL Community," financed under the Slum Rehabilitation component of the Earthquake Recovery Program (Project 519-0331)

Classrooms and playground built at the "Japan School," financed under the Public Services Restoration component of the Earthquake Recovey Program (Project 519-0331)

Best Available Copy

ACCOUNTING FOR INTERNATIONAL DISASTER ASSISTANCE FUNDS MADE AVAILABLE TO USAID/EL SALVADOR DURING FISCAL YEAR 1987

Except for two small grants totaling $36,957, USAID/El Salvador had properly accounted for $50,336,957 in International Disaster Assistance funds made available for earthquake relief, rehabilitation and reconstruction during fiscal year 1987. Funds were used for the following projects or activities:

Project/Activity	Obligations	Expenditures	Advances
Ambassador's Relief Grant	11,970	2,185	-
OFDA Operating Grant (Project 519-0330)	24,987	-	-
Emergency Shelter Support (OFDA funds, Project 519-0330)	300,000	253,395	300,000
Earthquake Recovery Program (Project 519-0331)	$50,000,000	$23,487,156	$44,458,725
	$50,336,957	$23,742,736	$44,758,725

We audited each of these activities to determine whether funds advanced and expended by USAID/El Salvador were properly accounted for as of September 30, 1987. The results of our review for these activities are presented below.

1. OFDA and Ambassador's Relief Grants

Our review of $36,957 obligated as of September 30, 1987 for the OFDA and the Ambassador's Relief grants disclosed that the separate accounting records maintained by USAID/El Salvador for these grants needed to be updated (see Finding No. 5).

2. Emergency Shelter Support (Project No. 519-0330)

Our review of the $300,000 Emergency Shelter Support Project as of September 30, 1987 disclosed that USAID/El Salvador had properly accounted for obligations and advances of $300,000 and expenditures of $253,395. We traced all transactions (entries) supporting USAID/El Salvador's "Project Financial Status Report" to obligating documents and vouchers for advances and liquidations. All of the transactions (entries) were supported by the required documentation and were properly recorded.

3. Earthquake Recovery Program Project 519-0351

Our review of Earthquake Recovery Program as of September 30, 1987 disclosed that (1) USAID/El Salvador had properly accounted for obligations of $50,000,000 and expenditures of $23,487,156 and (2) USAID/El Salvador and SETEFE had properly accounted for A.I.D. advances to SETEFE of $44,458,725. The audit procedures used to reach this conclusion and our findings are described in the following paragraphs.

USAID/El Salvador financial statements for the program are shown in Exhibit 1. These statements were based on USAID/El Salvador financial reports and payment vouchers. These statements showed the movement of all funds under the program. We traced all transactions (entries) supporting the financial statements to obligating documents and vouchers for advances, liquidations, reimbursements and direct payments. All of the transactions (entries) were supported by the required documentation and were properly classified and recorded. All A.I.D. advances to SETEFE had been properly authorized prior to the disbursement of funds.

SETEFE's financial statements for the program are shown in Exhibit 2. These statements were based on a SETEFE financial report. We verified that the total advances shown on USAID/El Salvador financial statements were in agreement with those shown on SETEFE's financial statements. We also verified that all of the SETEFE advances to implementing agencies were properly classified and recorded in SETEFE's financial statements and had been received by the authorized implementing agency. We also found that SETEFE had advanced some funds to financial institutions at the start of the program prior to obtaining signed contracts with the institutions.

We fully accounted for the $44,458,725 in A.I.D. funds advanced to SETEFE. These funds should have consisted of SETEFE advances to implementing agencies of $37,516,068 plus cash on hand of $6,942,657. We verified the cash per SETEFE's books to its bank statements and reconciliations and found that SETEFE had loaned $159,956 to a non-project activity. This loan was repaid on November 25, 1987. We also found that SETEFE had commingled the cash from the earthquake program with cash from other programs in the same bank account contrary to the requirements of the grant agreement. On November 3, 1987 SETEFE established a separate account at the Central Bank and transferred the required funds into that account. According to USAID/El Salvador, the establishment of separate accounts at the Central Bank requires a legislative decree. This was not done for the project until March 1987. USAID/El Salvador believes that given these normal bureaucratic delays SETEFE exercised its option to use the existing revolving fund. This emergency procedure was authorized by the legislative decree.

ELIGIBILITY OF EXPENDITURES FOR INTERNATIONAL DISASTER ASSISTANCE FUNDS MADE AVAILABLE TO USAID/EL SALVADOR DURING FISCAL YEAR 1987

Except for an undetermined amount of expenditures liquidated under the credit components of the Earthquake Recovery Program and $2,185 of expenditures under the Ambassador's Relief Grant, International Disaster Assistance funds expended by USAID El Salvador during fiscal year 1987 were eligible under the terms of the respective agreements.

Total expenditures audited were $23,742,736. As can be seen below, Price Waterhouse reviewed expenditures of $20,011,372 under its monitoring contract with USAID El Salvador, leaving $3,731,364 in expenditures to be reviewed by us.

Activity	USAID ES Expenditures	Expenditures Reviewed by Price Waterhouse	Expenditures Reviewed by AID Auditors
Earthquake Recovery Program (Project No. 519-0331)			
1) Employment Generation/ Rubble Removal	-	-	-
2) Micro/Small Business Credit	$ 5,992,434	$ 5,992,434	-
3) Temporary Shelter	3,709,879	412,539	$ 3,297,340
4) Slum Rehabilitation	-	-	-
5) Home Repair/Reconstruction Credit	13,606,399	13,606,399	-
6) Restoration of Public Services	178,444	-	178,444
Sub-Total	$23,487,156	$20,011,372	$ 3,475,784
Emergency Shelter Support (OFDA funds, Project 519-0330)	253,395	-	253,395
Ambassador's Relief Grant	2,185	-	2,185
	$23,742,736	$20,011,372	$ 3,731,364

The objective of this phase of our audit was to determine whether funds expended were supported by adequate documentation and were used in accordance with established eligibility criteria. As part of this review, we selectively verified whether (1) loans were made to eligible recipients and used as intended; (2) commodities purchased with project funds were properly accounted for and used as intended; and (3) facilities constructed or repaired with project funds were constructed or repaired as intended.

1. Eligibility of Expenditures Reviewed by Price Waterhouse

Under a monitoring contract with USAID/El Salvador, Price Waterhouse reviewed $20,011,372 of expenditures for the Earthquake Recovery Program of which $19,598,833 was for the credit components (Micro/ Small Business and Home Repair/Reconstruction) and $412,539 for the Temporary Shelter component. Our audit relied on the work performed by Price Waterhouse after making appropriate tests to verify the accuracy of their work.

Price Waterhouse found that all expenditures under the Temporary Shelter component ($412,539) were eligible. The expenditures were supported by the required documentation (see Appendix 3) and commodities purchased with project funds were properly accounted for and generally used as intended (see Appendix 4).

However, Price Waterhouse identified some ineligible expenditures for loans made under the credit component. The amount of ineligible loans could not be determined from the work performed by Price Waterhouse because the results of their sample could not be projected to the universe because it was not randomly selected. We also found some other loans that may not be eligible. The issue of questionable loans is presented in Finding No. 1 of this report.

In our opinion, the work performed by Price Waterhouse under the monitoring contract with USAID/El Salvador was generally accurate. We selectively traced their findings presented in eight reports to their working papers and found that their findings were generally supported. We also visited a sample of financial institutions and beneficiaries included in the scope of the Price Waterhouse reviews and found no significant differences to indicate that their working papers were not accurate.

2. Eligibility of Expenditures Reviewed by the AID Auditors

We reviewed $3,731,364 in expenditures under the following activities:

Activity	Amount
Earthquake Recovery Program (Project 519-0331)	
- Temporary Shelter	$3,297,340
- Restoration of Public Services	178,444
Emergency Shelter Support (Project 519-033)	253,395
Ambassador's Relief Grant	2,185
	$3,731,364

We employed the auditing firm of Price Waterhouse to assist us with this review and supervised their work.

Except for the Ambassador's Relief Grant of $2,185 (which we did not audit because of incomplete USAID/El Salvador accounting records), we found that all expenditures were eligible. Expenditures for $3,729,179 under the Earthquake Recovery Program and Emergency Shelter Support project were supported by adequate documentation (see Appendix 9).

We found that the commodities purchased with project funds for the Temporary Shelter component of the Earthquake Recovery Program ($3,297,340) were properly accounted for and generally used as intended (see Appendix 4). However, we could not fully verify that the commodities purchased under the Emergency Shelter Support project ($253,395) were properly accounted for and used as intended. Inventory control records could not be reconciled and the Municipality of San Salvador did not have a complete list of families who reportedly had received building materials (see Appendix 5).

We found that the activities under the Restoration of Public Services component ($178,444) of the Earthquake Recovery Program had been satisfactorily completed (see Appendix 4).

We did not audit the funds expended ($2,185) for the Ambassador's Relief Grant because USAID/El Salvador subsidiary accounting records were incomplete and they could not locate all of the supporting documentation. A detailed description of this problem is presented in Finding No. 5 of this report.

ACCEPTABILITY OF PROCUREMENT TRANSACTIONS FOR EL SALVADOR EARTHQUAKE RECOVERY PROGRAM (PROJECT NO. 519-0331), AND TEMPORARY SHELTER SUPPORT (PROJECT NO. 519-0330)

1. Earthquake Recovery Program (519-0331) - Temporary Shelter Component

Under the Temporary Shelter component, $4,460,000 was obligated and $3,709,877 was expended as of September 30, 1987. Our objective was to verify whether the $3,709,877 expended was in accordance with A.I.D. procurement requirements.

a. International Procurement Transactions

Price Waterhouse was contracted, under the supervision of A.I.D. auditors, to audit $3,297,340 in international procurement transactions. The Price Waterhouse auditors determined whether the procurement transactions were made in accordance with the procurement criteria contained in A.I.D. Handbook 11. Based on Price Waterhouse's work and our review of that work, we concluded that the international procurement transactions were properly made in accordance with A.I.D. procurement criteria.

The following was the step-by-step analysis of the procurement criteria used by Price Waterhouse and their findings:

(1) Formal A.I.D. approval is required when contracts exceed $100,000. This criteria was complied with.

(2) A.I.D. must approve Request for Quotations and Invitation for Bids (IFB) for contracts which exceed $100,000. Compliance with this procedure was noted.

(3) Contracts must be awarded through formal competitive bidding procedures unless a waiver is granted. The procedure was not complied with because a waiver had been obtained from the A.I.D. Administrator (STATE cable No. 361484, dated November 20, 1986).

(4) If the estimated value of the contract is more than $100,000, IFB's should be published in the Commerce Business Daily of the U.S. Department of Commerce. Again, this procedure was waived by the A.I.D. Administrator (STATE cable No. 361484, dated November 20, 1986).

(5) Claims by suppliers for payment must be supported by appropriate and complete documentation. Documentation for payment was appropriate and complete.

(6) Mandatory clauses set forth in Section 2.13 of A.I.D. Handbook 11 must be included in contracts. These clauses were included in all contracts.

(7) Fixed-price contracts are normally used in the procurement of materials. All contracts were fixed-price contracts.

(8) Evaluation of offers must be conducted by a panel set up by the contracting agency. The Special Committee for Acquisition (CEA) was established for this purpose.

(9) Normally, the total amount due is paid to the supplier when the paying agent receives shipping documents. Ninety percent was paid when shipping documents were received and the remaining ten percent was paid when the goods were delivered by the supplier.

b. Local Procurement Transactions

Under its monitoring contract with USAID/El Salvador, Price Waterhouse audited $412,539 in local procurement expenditures. According to Price Waterhouse's September 30, 1987 monitoring report, these procurement expenditures were made in accordance with procurement criteria established for the project. Based on Price Waterhouse's work and our review of that work, which included tracing the information in their report to their workpapers (source documentation), we concluded that the local procurements were properly made in accordance with the agreed upon procurement criteria.

The following is a description of the work done by Price Waterhouse to verify the proper procurement of these goods:

(1) Price Waterhouse reviewed virtually 100 percent of the documentation supporting building materials procured by CREM 1/ amounting to $412,539.

Documentation reviewed was the following:

a) Vendor invoices
b) Purchase orders approved
c) Warehouse material receipts

1/ Metropolitan Reconstruction Emergency Committee set up by the GOES to procure project goods and services.

The above documentation was reviewed to determine evidence of compliance with the following requirements:

a) Financial requirement
b) Accuracy of footing and extension
c) Approval of the purchase and payment
d) Evidence of receipt of materials procured

(2) Price Waterhouse also reviewed procurement transactions for compliance with Section III-A of the procurement regulations approved by Implementation Letter No.3 dated December 30, 1986. These requirements included approval limits and bidding by vendors.

(3) Price Waterhouse also reviewed the transactions to determine whether the procurements received approval by the Special Committee for Acquisitions.

2. Earthquake Recovery Program (519-0331) - Restoration of Public Services Component

Under the Restoration of Public Services component, $8,437,922 was obligated and $178,443 was expended as of September 30, 1987. Our objective was to verify whether the $178,443 expended was in accordance with A.I.D. procurement procedures.

Price Waterhouse was contracted, under the supervision of A.I.D. auditors, to analyze $178,443 in international procurements. The Price Waterhouse auditors specifically determined whether the procurements made were in accordance with the procurement criteria set out in A.I.D. Handbook 11. Based on Price Waterhouse's work and our review of that work, we concluded that the international procurements were properly made in accordance with A.I.D. procurement criteria. The analysis done by Price Waterhouse to determine that the proper procurement criteria were used for this component was the same analysis as that done on the Temporary Shelter component (Project 519-0331), as explained earlier in this Appendix.

3. Emergency Shelter Support (519-0330)

Under the Emergency Shelter Support Project, $300,000 was obligated and $253,395 was expended as of September 30, 1987. Our objective was to verify whether the $253,395 was expended in accordance with the project agreement.

Procurements under this project were made "off-the-shelf." No formal procurement procedures were required by the project agreement, since there was no time to obtain quotations, and purchases were made on an emergency basis. We found that the Municipality maintained accurate invoices of all purchased goods and services (amounting to $253,395), which were audited by the accounting firm of Price Waterhouse under our supervision. Based on Price Waterhouse's work and our review of that work, we concluded that the procurements were properly made in accordance with the project agreement.

The following is a financial summary of the $253,395 worth of goods and services procured under this agreement.

TYPE	COST
Metal Sheets	$131,595
Lumber (2" x 4" x 12')	85,336
Lumber (2" x 2" x 14')	20,318
Nails 4"	6,400
Wheelbarrows	3,542
Hoes	634
Crowbars	171
Shovels	144
IBM Services	4,435
Travel per diem	200
Import expenses	620
	$253,395

SUMMARY OF INELIGIBLE CREDIT DISBURSEMENTS UNDER THE EL SALVADOR EARTHQUAKE RECOVERY PROGRAM (PROJECT NO. 519-0331)

As discussed in Finding No. 1, an undetermined amount of home and business repair loan funds were loaned to individuals who did not qualify for program assistance, were used for ineligible purposes and/or were approved without adequate support or justifying documentation. The audit estimated that these cases accounted for at least $4 million, or 15 percent, of the total home and business credit disbursements. This estimate is based on reviews performed by a local Price Waterhouse accounting firm affiliate, 3 of the 18 participating financial institutions, USAID/El Salvador, the Association of Salvadoran Banks, and this audit 1/.

Price Waterhouse - Substantial work in this area was performed by an accounting firm affiliated with Price Waterhouse (PW). USAID/El Salvador contracted with PW in January 1987 to, among other things, monitor the credit line program. PW auditors worked closely with Mission personnel in establishing the scope and focus of this monitoring effort. PW's monitoring efforts concentrated on the 18 participating financial institutions' capability to effectively administer the home and business credits, as well as on the appropriateness of program fund uses.

During program implementation PW issued five interim monitoring reports which the Mission used as the basis for redefining eligibility criteria and making adjustments in the credit program 2/. For two of these reports, dated April 30, 1987 and August 31, 1987, PW selected a total of 3,061 loan files (2,112 home and 949 business loans) representing $9.9 million in disbursements, or about 36 percent of the total disbursed as of the study dates. For 1,263 of these files, representing $4.3 million, PW auditors made site inspections to verify the extent of damages and uses of funds.

1/ Our estimate was reduced by deleting all known ineligible loans listed more than once in these various reviews. We identified 194 such loans, representing $663,137.

2/ We traced selective parts of these monitoring reports to supporting workpaper documentation and then verified on a selective basis the accuracy of information that PW had obtained through its review of financial institutions' credit line files and physical inspections. With only minor exceptions, we found that the reports were satisfactorily supported by generally complete and accurate documentation.

Based primarily on its site inspections of damages, PW classified 177 home and business loans as ineligible, representing about $594,515 or 13 percent of the total sample. The institutions did not accept PW's findings that all of the loans were ineligible, and requested that PW reconsider their findings in 141 cases, based on additional information to be provided by the institutions. PW officials stated that they had wanted to inspect the subject properties prior to finalizing a decision on their eligibility.

However, the Mission's position was that the final decisions would be based only on a review of the additional documentation submitted by the institutions. At the end of the audit, 62 loans representing $196,696 had been tentatively reversed from ineligible to eligible by PW. As a result of these potential reversals, the number of loans classified ineligible by PW as of February 1988 was 115, representing $397,819. Our audit did not review the documentation used to support the 62 potential reversals. However, one of these loans happened to be reviewed during our limited verification of Price Waterhouse's workpapers. In our opinion, reversing that particular loan of $4,000 to eligible would be inappropriate given the property's large size and high value. It apparently involved a high-income family which was not the program's intended target group. Based on this example, it appears that site inspections should be an integral part of the process for determining the final eligibility status of questionable loans. See Appendix 10-1 for examples of expensive homes repaired under the credit component.

At our request, Price Waterhouse summarized certain loan data that it had gathered during its monitoring reviews which we considered important in assessing program compliance. PW was able to provide us with information on family income, damage verification, estimates of repair costs and end-uses of loan funds. However, another important category that we requested information on -- amount of business assets -- was not available. PW officials stated that this information was not generally documented in the files and therefore they had not bothered to collect it. The absence of this information in the loan files raises a question as to whether or not all business loan recipients actually met the program's business size eligibility criteria.

An analysis of PW's detailed data for the other categories revealed the following:

- 478, or 22 percent, of the 2,112 home files reviewed by PW did not contain information on monthly family income. Of the remaining 1,634 files, 117, or 7 percent, contained documentation which supported monthly incomes in excess of $800 per month 3/. Of the 117 high income loans, 35 represented incomes over $1,200 per month. The 117 cases represented a total loan amount of $413,630. The accuracy of income data was not verified. Based on an inspection of one home and information obtained from the owner, we learned that the income reported on that credit application was not accurate. It appeared that reported incomes may have only reflected the applicant's monthly income as opposed to total family income, as intended by the program. As a result, the number of high income cases are probably understated, in our opinion.

- In its February 27, 1987 monitoring report, PW identified examples of home loans which they considered ineligible on the basis of high income levels. PW officials stated that the Mission did not appear concerned with income levels since they were never precisely defined. As a result, PW did not subsequently identify in its reports loans to individuals with high incomes.

- 932, or 30 percent, of the 3,061 home and business files reviewed by Price Waterhouse did not contain evidence of physical inspections. These 932 cases represented a total loan amount of $3.2 million. Site inspections were important to verify that a given property existed and was in fact damaged by the earthquake, and that the requested loan amount did not exceed repair estimates.

- In 40 cases, the amount of funds loaned for home and business repairs exceeded or appeared to have exceeded actual damages. These loans represented $186,315. The amount in excess of actual damages could not be fully established.

- The loan proceeds of 41 home and business loans were used for ineligible purposes. These loans represented $146,779. The amount used for ineligible purposes could not be fully established. Ineligible uses included paying off existing debts and expanding the size of damaged buildings.

3/ Home loans were intended for low and middle-income families. Specific income ranges were never defined. Price Waterhouse used $800 per month as the top of the middle-income range. This amount appears reasonable given that the maximum family income eligibility criteria for the follow-on Earthquake Reconstruction project (No. 519-0333), with basically the same target group, is currently $700 per month.

- The extent to which loan repair funds were used for ineligible purposes was difficult to determine, but may have been greater than generally estimated. For example, one financial institution which required its employees who had obtained home loans to report on their uses, found that, of the 123 responding, 26 or 21 percent, stated they had used some of the home repair funds for other purposes. Also, PW found only limited evidence that the institutions had followed up and confirmed the use of loan funds.

Institutional Reviews - Three of the 18 participating financial institutions identified an additional 43 ineligible home loans through in-house reviews. These reviews were initiated at the request of the President of El Salvador during a March 23, 1987 meeting with the heads of the involved financial institutions. Among other things, the institutions were requested to review existing home and business credit disbursements and to identify those loans that were ineligible because the properties involved did not suffer damages. Of the 15 institutions responding, 3 identified 43 ineligible home credits representing $134,788. It is uncertain how the institutions conducted their reviews to determine ineligible loans. No business loans were reported in this group.

USAID Reviews - USAID/El Salvador reviews identified at least 22 additional ineligible loans. The Mission initiated studies of both the home and business credit lines soon after the credit program was implemented to determine how the institutions were performing and whether or not program adjustments were needed. Only part of the USAID's housing study data was located. A review of existing data showed that 11 of 109 business credits, representing $56,000, or about 10 percent, appear to have been ineligible. Of 24 home loans reviewed, 11, representing $31,300, also appeared ineligible. None of these business and home loans (22 in total) had been included in Price Waterhouse's sample.

Salvadoran Bank Association - The Salvadoran Bank Association (ABANSA) identified nine duplicate loans not included in other reviews. The Association was responsible under the program for daily entry into its computer of home and business loan data submitted to it by participating financial institutions. The primary purpose of this activity was to identify and hopefully prevent individuals from obtaining multiple loans. IG auditors consider the second loans obtained by these nine individuals to be ineligible, as one must assume that the first loan amount was based on actual damages, and because program criteria limited the maximum loan amount to $4,000 for home loans and $15,000 for business loans. Three of the nine borrowers received combined amounts in excees of the allowed maximums. The nine additional loans totaled $43,877.

RIG Audit - The current audit raised questions about the appropriateness of other loans. These loans were identified during the process of reviewing and verifying the information gathered by Price Waterhouse.

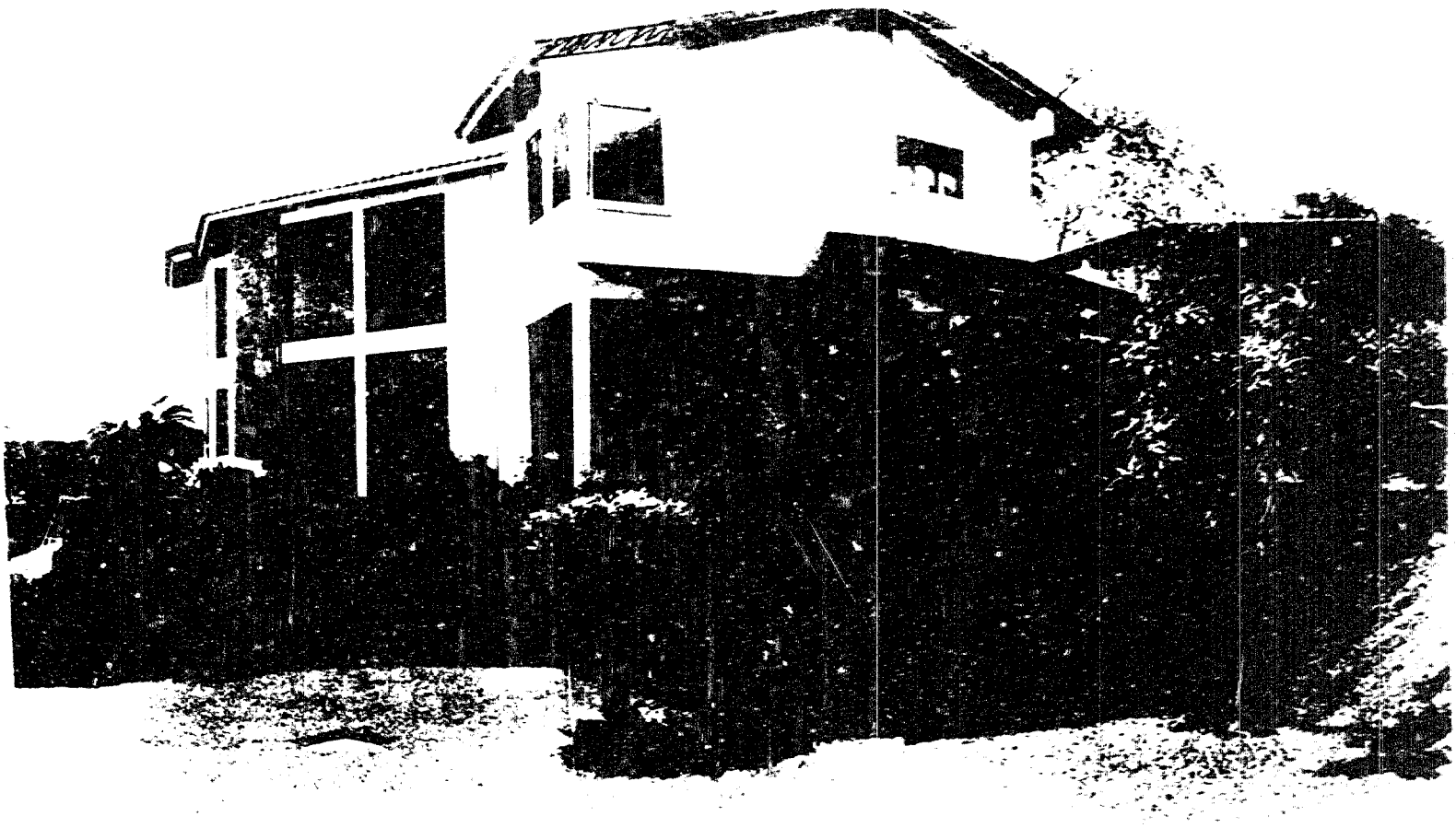
- The current audit disclosed that Price Waterhouse auditors could not find some loan files at the financial institutions and/or could not always locate the property in question. PW had not reported the extent of these anomalies. An examination of Price Waterhouse's documentation showed that its auditors could not locate 12 of the 3,061 files selected for review at the institutions. In addition, 41 of the 1,205 properties selected to be physically inspected could not be located and were substituted for by other properties.

- It was also noted that some program loan recipients had received damage compensation from insurance companies. For example, at two savings and loan associations we identified twelve loans in which the recipients obtained more funds than the cost of repairing actual damages through a combination of insurance reimbursements and program loans. This was inconsistent with providing assistance to those who did not otherwise have the resources to repair earthquake damages and limiting loans to actual damages that did not exceed the program limit. Neither the Earthquake Recovery Project (No. 519-0331) nor the follow-on Earthquake Reconstruction project (No. 519-0333) had established mechanisms to identify program borrowers that had earthquake insurance coverage. We were told that the former USAID Controller had verbally recommended that insurance proceeds which duplicated the purposes of the loan be paid over to A.I.D. We found no evidence that this recommendation was documented or implemented. We were also told that the loan criteria under the follow-on project did not specifically require that insurance proceeds be considered in determining the loan amount.

- Finally it was noted that PW had identified six banks in its August 31, 1987 report that had made business loans for working capital to professional enterprises. The number or value of loans in this category was not determined; however, program guidelines prohibited loans for working capital to this type of business.

PHOTOGRAPHS OF EXTENSIVE HOMES
REPAIRED UNDER THE EARTHQUAKE
RECOVERY PROGRAM'S CREDIT COMPONENT

PHOTOGRAPHS OF EXPENSIVE HOMES
REPAIRED UNDER THE EARTHQUAKE
RECOVERY PROGRAM'S CREDIT COMPONENT



memorandum

DATE: April 4, 1991

REPLY TO ATTN OF: Henry Bassford, Director, USAID/El Salvador

SUBJECT: Mission Response to Audit Report of Earthquake Relief

TO: Solange Gothard, RIG/A/T

Attached is the Mission's response to the Earthquake Relief audit report. This response is being hand carried to Washington today by Mr. David Bockler, in order to get it to you as soon as possible.

As you know, both RIG/A/T and the Mission faced very difficult deadlines for the completion of the RIG's report and the Mission's response. The Mission received the final draft of the report at close of business on Friday, March 29, and was given little more than a week to prepare the response. Unfortunately, the next week being Semana Santa, the entire Government of El Salvador went on vacation, and we were not able to contact our counterparts to obtain information and documentation needed for our response until only April 4. We have tried our very best in the limited time available to respond to the comprehensive and complex report.

I personally feel the audit report is an excellent account that should prove helpful to the Agency. Even before the report was issued, the Mission had already incorporated most of its recommendations into the design of the follow-on project, Earthquake Reconstruction. We will strive to incorporate the remaining recommendations as well. We would like to note, however, that the auditors issued the draft report before we had a chance to point out several inaccurate statements and subsequent erroneous conclusions. Attached, we have indicated these in the same order as they occurred in the draft report. We hope that you will be able to make the appropriate corrections before issuing your final report to the Congress.

This Mission commends the spirit of collaboration on the part of RIG/A/T in assisting the Mission achieve its goals, and accurately portraying a detailed accounting as mandated by Congress.

Best Available Copy

OPTIONAL FORM NO. 10
REV. 1-80
GSA FPMR (41 CFR) 101-11.6
5010-114

COMMENTS OF REPLY TO AUDIT REPORT
EARTHQUAKE RECOVERY PROJECT, 519-0331
OFDA EARTHQUAKE EMERGENCY RELIEF FUNDS, 519-0330

Please include the following in the Executive Summary: "The Mission notes that some of the points of difference highlighted in the exit conference between the Regional Inspector General's Team and the El Salvador Mission have been taken into account and that minor alterations were made in the second draft with respect to Mission recommendations regarding inaccuracies, tone, opinions and materiality.

The draft audit report as written still contains a few inaccuracies, faulty cause-effect relationships and conclusions reached which are inaccurate and misleading to the uninformed reader. The mission's comments contained herein are directed at correcting those technical errors and conclusions. The Mission commends the spirit of collaboration on the part of RIG/A/T in assisting the Mission achieve its goals, and accurately portraying a detailed accounting as mandated by Congress.

The benefits of the experience in the preceeding phases of the $50 million earthquake reconstruction process, rescue, relief and recovery and the constructive recommendations of this audit have enabled the Mission to begin the $75 million reconstruction phase with a better understanding of the institutional capacity of the agencies involved and has permitted the refinement of the procedures used in the highly successful previous efforts which are now concluded."

Specific comments are made on the draft report as follows:

I. EXECUTIVE SUMMARY

The numerical data presented on page No. iii for project outputs/accomplishments are inaccurate.

The following figures should be used:

a) Person-days-of work generated 897,206 vice 792,669 per report.

b) Rubble removed 114,608 cubic meters vice 112,352 per report.

c) 26 small, medium size and large infrastructure subprojects vice 26 small infrastructure subprojects.

The third clarification is made because most of the urbanization projects under the Slum Rehabilitation included the introduction of sewerage, storm drainage,

systems and electrical grids, all of which are considered more appropriately in the medium-size and heavy infrastructure categories.

d) Under Restoration of Public Services, 63 medium and large scale (not 41 as indicated in the report) activities were carried out. Moreover, each of the 63 involved an array of subactivities, e.g. the Ministry of Education alone, (which appears in the audit report as one activity), included the construction of 724 classrooms in 58 locations of the City, the repair of 240 classrooms in another 46 locations of the City and the preliminary design of 5 major educational institutions. The use of 41 subprojects for the entire activity's output diminishes the success of the project and is also misleading.

e) On the housing sector the following notes of correction are offered:

Page iii Paragraph 2 should read: "...inventories and working capital; 34,498 families received A.I.D. financed building materials (see page 16). It is technically inaccurate to use methodology described in appendix 4, page 5, paragraph 3 to arrive at No. of beneficiary families. The fact that 8% of one type of material came from another donor does not mean that A.I.D. did not service 100% of the families with some kind of materials. As a matter of fact AID did provide lumber, nails, transportation and related administrative and financial control costs for distribution to all families.

II. INTRODUCTION

On page No. 1 of the introduction, we suggest the use of damage statistics and casualties as agreed in the exit conference and as provided in telcon Seckler/RIG on March 25, 1988, instead of those used in the draft audit report.

Page 5, 2nd Paragraph the last sentence should read: included in the $5,775,930 cited above, is $421,409 in the category Commodity Procured.....

On Page 5, last Paragraph first sentence RIG should add the following phrase at the end of the sentence "as project components are completed." (See RIG/A/T Memo dated 6 March, 1987 attached as Annex I)

III. RESULTS OF AUDIT

Figures used in paragraph 1 of page No. 11 should coincide with accomplishment figures provided in this critique. Also appearing is the erroneous comment regarding "(The program's largest components)" in the final sentence of paragraph No. 1 of page 11. The Restoration of Public Services Component financed at $11,692,656 is the second largest component of the project.

IV. RECOMMENDATION NO. 1

"We recommend that USAID/El Salvador, in consultation with the Government of El Salvador, establish and implement a plan to:

a. Identify all ineligible home and business loans, and

b. Obtain restitution or substitution of eligible loans for such ineligible disbursements."

The Mission concurs with the RIG that the credit lines for home and business loans need to be more fully examined; however, we do not concur with the recommendation that all ineligible loans be identified. We believe the recommendation is pre-mature and not cost beneficial.

As stated in the report, Price Waterhouse has been contracted to perform a non federal audit of this project which will be used to supplement this audit. It is most important to recognize that all previous Price Waterhouse work was directed as financial oversight or end-use reports. Statistics cited in this audit pertaining to prior Price Waterhouse reports are still preliminary. Of a total of 141 questionable loans out of 3,061 sampled, 55 still require resolution.

Moreover, RIG has not considered the sample completed by Price Waterhouse as valid for audit purposes. Yet in the audit, RIG suggests that the percentage of ineligible loans is 13%, based on "the cumulative findings of formal and informal reviews performed by the accounting firm of Price Waterhouse, 3 of the 18 participating financial institutions, USAID/El Salvador, the Association of Salvadoran Banks and this audit."

The Mission concurs with the audit that an undetermined amount of loans went for ineligible purposes. We do not concur with the percentage. We strongly feel the 13% cited in the Price Waterhouse report to be high, and based on incomplete data. We agree that we must determine the degree of ineligible loans, and have begun to perform a non federal audit to determine same. (Whatever recommendation is warranted should consider cost of its implementation in relation to the benefits to be derived.)

In summary, we do not agree with the recommendation as written, and respectfully request a deletion of same until a valid sample is taken. The audit supports this approach. Experience has shown that not all implementing entities performed with the same degree of acceptability. To suggest that a percentage be projected to the entire population is incorrect.

Responsible implementing institutions would not accept arbitrary charges of restitution. The non federal audit requires the time necessary for its succesful completion, together with the full range of independence for an unbiased report. The Mission in concert with the RIG will push for restitution in those cases where restitution is warranted. Maximum identification should be within a reasonable range of cost.

As the RIG Audit Team is aware, the mission identified the deficiencies which led to this recommendation nearly a year before the audit was initiated and has worked actively with the GOES to determine the extent of the problem, provide interim remedial solutions and has substituted eligible loans for those loans judged ineligible. As a result of early program adjustments, the mission was able to make corrections in the credit activities reducing the isolated cases lacking adherence to project precepts.

A strategy, with its attendant procedures and developed in close consultation with the GOES, has been in process since January of 1987 shortly after the initiation of the credit component and as soon as the deficiencies first became suspect. This process, several months under implementation by the time this audit was initiated, should continue in close colaboration with the non-federal audit team and in continued consultation with the GOES.

The Mission agrees to a final solution along the lines of the second RIG option with the specific, detailed methodology and strategy to be developed by USAID/El Salvador working with the non-federal audit team and the appropriate GOES agencies.

The Mission objects to the lack of balance in the first sentence of page 15. There admittedly was a "trade-off" in the approach adopted by the Mission. One hundred percent purity could have been gained by fixing rigid and detailed identification, selection and approval criteria in which all cases could have been investigated one-by-one and certified with great accuracy with respect to: existence of earthquake damage, magnitude of damage, prior earthquake beneficiary income levels, geographic location of the victims, end uses and time lapses between receipt of funds and application of funds to the problem, etc. To do so, however, would have been so time consuming that only a fraction of the target group would have been served during the short life of an emergency project (viz. this project was an emergency response to a severe natural disaster). As it is, about 10,000 families and businesses in great need received assistance. The Mission operated with a sense of urgency to serve earthquake victims as quickly as possible. The auditors do not seem to relate to this urgency, a year after the earthquake, in the same way that the Mission did when confronted with the disaster.

The Mission notes that never in the history of this country have so many people, in such great need, benefited so quickly through so many institutions and with so much financial assistance. This is an historical fact. It may have had its shortcomings, but in the mission's eyes the approach used was better than any alternative offered to date. The resulting problems are manageable and will be remedied.

Page 15, 2nd. Paragraph: The RIG conclusion is based on a sample that according to both PW and the RIG auditors is not projectable to the universe because it is not statistically valid. Furthermore, some of the PW findings are not definitive and have been strongly objected to by the financial institutions. Several cases still are still under review preliminary to an eligibility determination.

Page 17, 1st. Paragraph, 2nd. sentence: The sentence should read: "reversed from ineligible to eligible by PW." Otherwise it would appear that the Mi sion has overriden PW which is totally contrary to fact.

Page 22, 1st. Paragraph addresses the issue of insurance claims. The audit comment is that "Neither the Earthquake Recovery Project, 519-0331 nor the follow-on Earthquake Reconstruction Project, 519-0333 took earthquake insurance into account."

The statement is inaccurate. During the design of the Recovery Project (which took place under very trying circumstances only days after the earthquake, and during a period when the GOES was largely demobilized in terms of ready access to information, files, records or even interagency resource personnel who were engaged in rescue and massive relief efforts) several discussions took place between USAID, INPEP (Pension Institute for Public Employees), SETEFE, the Ministry of Planning and the Central Reserve Bank in which the subject of insurance claims was amply debated. It was the consensus of the participating agencies not to take into account insurance claims because there were too many unknown factors and doubts about insurance claims to consider them as a significant source of reflows at the project design stage. To illustrate: 1) it was not known if there would, in fact, be any claims paid in the first year after the earthquake; 2) if paid, the extent to which claims would be large enough to be meaningful was not known; 3) when payments, if any, would be made was an imponderable; 4) the extent to which the loan funds offered under the Recovery Project would be adequate to cover damages incurred was also not known; 5) the manner in which insurance companies would make payments (installments, in-kind materials, etc.) was also not certain.

In recent meetings held among the Vice Minister of Housing and Urban Development, SETEFE, the DGR (General Reconstruction Directorate), the National Housing Finance Company (FNV), and USAID, it was substantiated that most of the beneficiary group receiving loans had no earthquake insurance at all and that those who did receive claims noted that they a) came in small amounts (for only a fraction of the initial cost of the original structure), b) experienced long delays in receiving the claims, and finally c) many recipients did not receive cash at all but rather offsetting adjustments to their housing payments.

The statement that the Mission has not taken into account insurance proceeds for the follow-on Reconstruction Project is inaccurate. Discussions have taken place with the various institutions involved in the credit lines of the Reconstruction activity. The Mission concedes that a manageable and equitable procedure has yet to be developed, but the issue is being dealt with and agreement will be reached on insurance proceeds. A policy concerning such proceeds will be incorporated into the interinstitutional agreements for the respective credit lines under the follow-on Earthquake Reconstruction Project (519-0333). In addition, the issue will be addressed in the administrative procedures of Project 519-0333, and finally be a salient clause in the contracts for individual subloans governing insurance proceeds. Even now, however, the Mission and the GOES doubt that insurance reflows will be a significant factor based on existing knowledge of the target group, and judging from the experience gained thus far with insurance claim recoveries.

V. RECOMMENDATION No. 2

"We recommend that USAID/El Salvador obtain from the 18 participating financial institutions, through the Government of El Salvador Secretariat for External Financing, reports on the status of their earthquake program loan balances, delinquencies and reflows on a quarterly basis."

The Mission fully agrees with the recommendation to obtain financial information on the status of credit lines with respect to: loan balances, delinquencies and reflows on a quarterly basis.

To this end, SETEFE has already taken the following measures:

1. Notified all financial institutions to begin filing such reports on a monthly basis, (See Annex II for sample copy of letter). and

2. Provided the financial institutions with specific, guidance and procedures regarding the content of the monthly reports.

The Mission takes exception with the auditors' statements made in paragraphs No. 3 and No. 4 on page 30 that the Mission was not aware of the status of reflows. The Mission had, on several occasions, requested and received information from SETEFE regarding the status of loan reflows on an "As-Needed Basis", e.g. such information was requested and provided by SETEFE prior to all important meetings with the presidents of the financial institutions, prior to the meetings with the President of The Republic and representatives of the financial institutions; prior to project reviews with the President of The Republic and the U.S. Ambassador; and for the purpose of gaining periodic operational data. We specifically cite PIL No. 31, which is attached as Annex III, and offer SETEFE letter No. B-428-87 (Annex IV), also attached as evidence to support that the Mission was aware and concerned.

Information beyond that which was specifically requested by USAID and supplied by SETEFE was not necessary for management purposes. The mission's primary concern focused upon the financial institutions' ability to absorb and manage funds properly.

The Mission requests deletion of the auditor's opinions expressed on page No. 31.

VI. RECOMMENDATION No. 3

"We recommend that USAID/El Salvador:

a. Obtain evidence from the Ministry of Planning demonstrating that participating institutions are depositing the Government of El Salvador's portion of the reflows into the corresponding special account, and

b. Formulate, in consultation with the Ministry of Planning, a plan as to how these funds will be used."

The Mission readily accepts the recommendation as written.

With respect to part a, and in accordance with various conversations that took place during 1987 with the GOES, the following has already taken place: a) SETEFE requested the opening of a special account in the BCR on February 12, 1988 per Annex V, b) the BCR acknowledged establishment of the account on February 19, 1988 (see Annex VI), c) on April 6, 1988 SETEFE instructed the financial institutions to begin deposit of reflows (see Annex II).

Evidence that deposits are being made will be provided to the RIG promptly upon the receipt of deposits to this account.

With respect to part b of the recommmendation, the Ministry of Planning and USAID have developed a mechanism for recovery of reflows and end uses of such reflows, i.e. for use in the low cost housing sector and for small businesses credit, see Annex VII. A reply of concurrence is being drafted and will be provided shortly to RIG thereby closing this audit recommendation.

The Mission disagrees with statements made on pages 32 and 36 which assert that USAID/El Salvador had not established formal plans for the use of reflows. Again, as pointed out to the auditors at the exit conference, Project Implementation Letter No. 31 dated July 23, 1987 (see Annex III) constitutes formal agreement for the use of said reflows. It is further noted that this agreement was made at a date well in advance of the earliest availability of such reflows, taking into consideration that the financial institutions had negotiated with the Ministry of Planning the right to hold all reflows. The holding period of up to 180 days following their collection was decided as a means of offsetting the enormous costs associated with the administration and supervision of such a large number of small loans.

Finally, USAID/El Salvador wishes to clarify that reflows were to be used soley for earthquake victims. To wit: The program Grant Agreement stipulates that the reflows pertaining to Micro and Small Enterprise Credit "would be deposited in the Central Bank to be utilized for Small Business Credit according to terms to be agreed upon between the GOES and A.I.D." (Page 2 Annex 1 of Project Agreement). Therefore the Mission finds the auditors' comments regarding the management and uses of reflows and page No. 37 and on other repeated references throughout the report to be inaccurate regarding the quote provision of additional credit assistance to El Salvador's earthquake victims and or to assist in similar activities unquote.

Notwithstanding this clarification, the Mission maintains that it reached timely agreement with the GOES, as specified in PIL No. 31, for the uses of the reflows. The fact that reflows were not required is neither due to the failure to consider them, nor to the lack of demand for them; but rather due to a lack of absorptive capacity on the part of the financial institutions to use them properly.

Recommendation No. 4

"We recommend that the General Counsel, Bureau for Latin America and the Caribbean, A.I.D., determine whether development assistance and economic support funds obligated or used for activities associated with earthquake relief were employed in a manner consistent with authorized project or legislative requirements and specify any corrective actions required."

The Mission concurs with this recommendation with regard to the $421,409 used from the Public Services Restoration project (519-0279) and will request an opinion on the entire $1,340,231 in funds obligated or used which has been questioned by RIG. However, we wish to point out that $806,054 of this amount is PD&S funds, of which all but one contract was obligated prior to the receipt by the Mission on March 15, 1987 of a budget allowance for earthquake PD&S. The Mission believes that the uses made of PD&S funds were consistent with legislative requirements.

The use of the Health System Vitalization contractors to dispense medication to earthquake victims shortly after the earthquake was both within the scope of their contract and the project purposes and a perhaps life-saving use of a valuable resource. The alternative was that they do nothing.

As the auditors note, the requirements for Congressional Notifications are unclear and realize the process is tedious - six weeks at best. The Mission believes the appropriate actions were taken.

Recommendation No. 5

"USAID/El Salvador should:

a. update its separate accounting records for the Office of U.S. Foreign Disaster Assistance and the Ambassador's grants, and

b. advise A.I.D./Washington of the updated balances for obligations and expenditures."

As mentioned in an earlier part of this report, after the earthquake AID had no office, no supplies, and only a skeleton staff. The Controller's office operated out of the guesthouse, then made two other moves before moving into Loma Linda two months after the earthquake. Even though fund cites had been received, no cash was available as the banks were closed and the Embassy/AID petty cash was inaccessible due to damage to the Embassy. We began operations with cash borrowed from employees who had recently sold POVs. In addition, no handbooks were available for consultation until months after the quake.

In spite of these difficulties, the audit does note that the Controller's office adequately accounted for the receipt and expenditure of petty cash funds.

OFDA Grant (Project 519-0330)

p. 45 - The audit says the auditors only saw documentation for $10,566. This is the amount of the purchase orders that were issued. In addition, copies of documentation for miscelleneous obligations were given to the auditors. It was explained to them that, at the time the budget allowance was received, the mission did not have any ledgers or forms and that the obligating documents were sheets of paper prepared by the Controller's office and signed by the project officers. Attached as Annex VIII are copies of all obligations in the amount of $21,343.44, which is the corrected obligation total. Disbursements in the amount of $15,259.44 have been recorded and, upon receipt of an AOC from Washington, accounting for this grant will be complete.

p. 45 - The sub-cashier used colones 36,800 ($7,360) (temporarily borrowed from an employee as noted above) and later obtained colones 50,000 ($10,000) from the embassy cashier for a total of $17,360, not $57,199 as stated in the report. The audit is in error when it states that the record did not distinguish between funds spent for the grants and for OE. The spreadsheet maintained by the sub-cashier was only a record of cash in and out. However, the supporting documentation (copies of which were provided to the auditors) attached to this spreadsheet clearly identified the fund cites used.

Ambassador's Relief Grant

The Mission did maintain subsidiary records of petty cash transactions and purchase orders issued by the Mission. However, much of this grant was used for procurement done through the Panama mission and arranged by OFDA personnel temporarily working in San Salvador. As San Salvador was on minimize, and the official accounting station is AID/W, Panama AOC'd the charges to AID/W and did not provide San Salvador with this information. The eleven day period is complete and correct. No further petty cash disbursements were made from this fund after October 31, 1986.

As noted above in the discussion of the OFDA grant, the auditors were provided with copies of documentation, but in their report only they gave credence to the typical obligating document, i.e. a purchase order. The Mission has forwarded all obligation information to AID/W and AOC'd all disbursements. Copies of the AOC and pertinent documentation are attached (Annex IX).

The Mission has taken action on Recommendation No. 5. The manual records have been posted on the computer and all postings are current. An AOC has been issued to AID/W and they have been advised of the obligation amount. Mission requests this recommendation be deleted or closed upon issuance of the report.

VII. INTERNAL CONTROLS

The Mission requests that RIG make adjustments to Part II Section B. Compliance and Internal Controls, pursuant to comments provided herewith by USAID/El Salvador. The Mission suggests deletion of the first and third items.

First (Also Appendix 7- Item 2.)

The Mission did not advance funds to the Municipality of San Salvador prior to the signing of an obligating grant agreement. The Mission signed the Limited Scope Grant Agreement with the Municipality on October 21, 1986 specifically. The Director and the Mayor signed the agreement and immediately a check for $300,000 was delivered to the Mayor. Later, the Minister of Planning insisted that he, as a representative of the GOES, should also sign the agreement.

As a courtesy, a new signature page was prepared, filling in place for the Minister's signature. The Director, the Mayor and the Minister of Planning then signed the newly prepared signature page. The page was not dated when signed (See undated copy, Annex X). Later, probably when the agreement was forwarded to AID/W, the erroneous date of October 23, 1986 was inserted on the signature page instead of October 21, 1986.

The Mission had a legitimate obligation upon the signatures of both the Mission Director and the Mayor. As evidence that the agreement was signed on October 21, 1986, we are submitting copies of the following documents (see Annex X):

1. An unsigned copy of the Limited Scope Grant Agreement prepared for two signatures with a PACD of January 20, 1987.

2. A signed undated copy containing the three signatures. This is a copy of the original retained by SETEFE at the Ministry of Planning. The PACD is still January 20, 1987.

3.. A signed copy of the grant agreement with the typed in date of October 23, 1986.

4. A copy of the voucher which refers to the obligating agreement dated October 21, 1986.

5. A copy of a memo to the Associate Director defining implementation responsibilities under this grant and referring to the agreement signed 10/21/86.

Further, the former Mission Controller remembers taking the check with him to the ceremony and when the agreement was first signed, immediately turning over the check. The Mission requests that this internal control deficiency be deleted and that in Appendix 7, the last paragraph of page 2 be deleted.

Second

Mission due to time constraints is not cognizant that SETEFE operated improperly and without authorization during emergency period.

VIII. OTHER PERTINENT MATTERS

Reference is made to Page 31, 1st. Paragraph which states that the program "would have had greater impact in assisting the intended target groups..... if the most affected areas with the highest concentration of these groups had been designated, and or identified by map delineation at the program's outset." Suggestion is also made that the U.S. Geological Survey studies of these areas could have been used. With respect to the latter, the U.S. Geological Survey information was not available at the time of the program's design.

Even the information available to the Mission now is of limited value for accurate selection purposes. It should be pointed out that such a geographic demarcation for the target group would have also eliminated a large number of eligible and worthy beneficiaries,
people who had enormous damage but resided outside the highest areas of earthquake damage.

Given the circumstances and the objectives of the program, the Mission opted to broaden the boundaries of the program to insure the inclusion of all valid requests for assistance. We continue to stand by this decision.

Not withstanding the above, the Mission is using geographic boundaries for the implementation of the Earthquake Reconstruction project, 519-0333; however, the delineation is more largely due to the desire to focus and direct the redevelopment of the Capital City rather than for qualifying the target group.

The last paragraph on page 53, states that mission employees were given preferential treatment for receiving loans. The Mission wishes to go on record officially stating that no partiality was shown to mission employees by USAID or the U.S. Embassy. In fact, and as reported to the audit team during the exit conference, the Mission when approached by the financial institutions repeatedly stated that mission employees should be given the same consideration as all other applicants.

The auditor's comments on this matter imply that 200 other applicants did not receive loans even though they had submitted and obtained loan approvals prior to the submission of Mission employee applications. The Mission was taken by surprise with this finding and questions that 37 Mission employees could have displaced 200 other applicants. We question the auditor's conclusion. Does this mean that A.I.D. employees receive loan amounts five times higher than the norm? If this was the case, we wonder why the finding has not been disclosed?

Best Available Copy

On the bottom of page 56 the auditors state that OFDA did not properly account for 24 water bladders. On page 56, however, it is acknowledged that 18 bladders were accounted for leaving only six bladders unaccounted for. We ask that this inconsistency be rectified. The former Mission Disaster Relief Officer has stated that the remaining six bladders were made available to the OFDA Regional Representative in Costa Rica. Evidence of transfer and receipt is being sought.

Page 57: The $620 item questioned by the RIG as an import expense was determined to be a bank charge for currency conversion, and as such, as a valid reimbursable project cost. RIG may wish to delete this item.

APPENDIX 4, Page 5 of 9, 2nd Paragraph: The number 32,773 should read: "...34,498. This number includes 121 families provided temporary shelter by IVU." The text is inaccurate. It fails to include families that benefited after July 6, 1987, the official closing date of the distribution program up to September 30, 1987, the audit cut off date. See page 14 for total number of beneficiary families. Likewise, the audited number assumes that 8% of benefitted families received exclusively materials from other donors. This is not true as explained in the following paragraph.

APPENDIX 4, Page 5, 3rd. Paragraph: This paragraph should read: "The A.I.D. distribution system included approximately 8% galvanized metal sheeting contributed by other donors. All wood, however, was contributed by A.I.D. and the total number benefitted came to 34,498 families, of which some 3,000 had also received limited amounts (partial packages to complement other assistance received) of building materials under the Temporary Shelter Support project. The component's goal was to distribute building materials to 32,345 families."

APPENDIX 4, Page 5 of 9, 4th Paragraph should read: "The sample results showed that 97% of beneficiary families had received the materials. Sixty percent of the families had built temporary shelters with the materials and 31% had the materials in storage. The remaining 6% that received material sold or gave it to others." See "Price Waterhouse Report No. 18 for the correct percentages; as was stated in the draft, the paragraph is inaccurate.

APPENDIX 4, Page 6 of 9, 4th Paragraph, line 1 should read: "The leftover building material..."

APPENDIX 4, Page 7 of 9, 1st. Paragraph. The following phrase should be added to the end of the paragraph: "This material was distributed after September 30, 1987 to 1,600 families."

Best Available Copy

APPENDIX 5, Page 2 of 5, 2nd. Paragraph, the last line, should read: "...5,040 families. Eighty four percent of the funds were spent on materials and 16% on transportation costs for this project and the Temporary Shelter Component of the Earthquake Recovery Program (Project No. 519-0331). Although the project's goal had been to assist 5,240 families, it was curtailed early in order to permit a phased initiation of material distribution under the Earthquake Recovery Program."

APPENDIX 5, Page 3 of 5, 1st. Paragraph should read: "In attempting to verify the number of beneficiaries reported by CCA, the only source documents to support its figures consisted of the recorded number of families observed by the monitors receiving the materials at each distribution point. Under the emergency conditions, it was not always possible to record the names of all the families benefitted. Additionally, the information..."

APPENDIX 5, Page 4 of 5, 6th. Paragraph should read: "Based on this sample, it can reasonably be concluded that almost all of the materials distributed under this project reached the targeted beneficiaries." (This is a much more accurate statement. In reality, if the sample is used as a basis, of 50 families interviewed, 42 used the materials and 8 stored them. That amounts to 100% receipt of materials. The audit states that one family (which would raise the number of families benefited to 51, a slight inconsistency) claimed it did not receive the materials. Even if this one family is considered, the percentage would be 98% receipt. It is unsound, given the nature of this universe, to make assumptions one way or the other about families that could not be found or interviewed. They cannot be included as part of the sample.)

APPENDIX 5, Page 5 of 5 2nd. Paragraph, final sentence should read: "It should be pointed out that deliveries under this program had ended by February 6, 1987, in order to initiate the Earthquake Recovery Program which followed." (The audit text ignores the transition from 519-0330 to the 519-0331, which was the beginning of a new program.)

APPENDIX 5, Page 5 of 5, final paragraph, should read: "The ending inventory represented about 50 percent of the total materials donated, most of which had been delivered by suppliers during the month of January. The Municipality..." (This version of text explains why 50% of the materials were still in inventory. The material had just been delivered when the new program was readied to begin. Thus distribution took place along with materials procured under 519-0331.)

Best Available Copy

FINAL NUMBER OF BENEFICIARIES IN THE TEMPORARY SHELTER PROGRAM (519-0331)

		Families
A.	Up to September 30, 1987	
	General Distribution 2nd Phase	32,950
	Distribution by IVU	121
	Leftovers distributed to the relocation sites, 10 de Octubre	920
	and La Selva	356
	Distributed to the Communities Altos de San Francisco	25
	Corazón de María	83
	Other Pending Families	43
	Total	34,498
B.	After September 30, 1987	
	Distributed by IVU to families	268
	Transferred from IVU to Tikal	1,232
	Transferred from IVU to 10 de Octubre	126
	Total	1,626
C.	Grand Total Number of Families Benefited under 519-0331	36,124

APPENDIX 7, Page 4 of 4, 2nd. Paragraph, commingling of funds: This situation was due to the following reason: Establishment of separate accounts at the Central Reserve Bank of El Salvador (BCR) requires a legislative decree incorporating specific project resources into the extraordinary budget of the GOES. In case of the Earthquake Recovery Project, the decree was passed in March 1987, and published in the GOES official gazette in June 1987. Given these normal bureaucratic delays, SETEFE exercised its option to use the existing revolving fund account to receive and channel project funds to the beneficiaries. This emergency procedure was authorized by the legislative decree (See Annex XI).

LIST OF RECOMMENDATIONS

Page

Recommendation No. 1

We recommend that USAID/El Salvador, in consultation with the Government of El Salvador, establish and implement a plan to 9

a. identify as many ineligible home and business loans by institution as may be cost-effective, and

b. obtain restitution or substitution of eligible loans for such ineligible disbursements.

Recommendation No. 2

We recommend that USAID/El Salvador obtain from the 18 participating financial institutions, through the Government of El Salvador Secretariat for External Financing, reports on the status of their earthquake program loan balances, delinquencies and reflows on a quarterly basis. 14

Recommendation No. 3

We recommend that USAID/El Salvador: 17

a. obtain evidence from the Ministry of Planning demonstrating that participating institutions are depositing the Government of El Salvador's portion of the reflows into the corresponding special account, and

b. formulate, in consultation with the Ministry of Planning, a plan as to how these funds will be used, as intended by the program agreement.

LIST OF RECOMMENDATIONS

Page

Recommendation No. 4

We recommend that USAID/El Salvador obtain a legal opinion from the General Counsel, Bureau for Latin America and the Caribbean, A.I.D., to determine whether development assistance and economic support funds obligated or used for activities associated with earthquake relief were employed in a manner consistent with authorized project or legislative requirements and take any corrective actions required by the legal opinion. 21

Recommendation No. 5

USAID/El Salvador should: 25

a. update its separate accounting records for the Office of U.S. Foreign Disaster Assistance and the Ambassador's grants, and

b. advise A.I.D./Washington of the updated balances for obligations and expenditures.

REPORT DISTRIBUTION

	No. of Copies
House Committee on Appropriations	5
Senate Committee on Appropriations	5
Director, USAID/El Salvador	5
AA/LAC	2
LAC/CAP/EL	1
LAC/DR	1
LAC/DP	1
LAC/GC	1
LAC/CONT	1
LAC/RLAs	1
GAO Panama Branch	1
AA/FI	2
OFDA	2
GC	1
LEG	1
M/FM/ASD	5
PPC/CDIE	1
FVA/PPE	2
FVA/FFP	2
XA/PR	1
AA/XA	1
IG	1
AIG/A	1
IG/PPO	1
IG/PSA	1
IG/LC	1
IG/ADM/C&R	12
IG/I	1
RIG/I/T	1
Other RIGs	1