

DC-APR-978

ISA 68740

**AUDIT OF  
THE SMALL FARMER DIVERSIFICATION  
SYSTEMS PROJECT COMPONENT WITH THE  
NATIONAL BANK FOR AGRICULTURAL  
DEVELOPMENT**

**Audit Report No. 1-520-89-52-N  
September 18, 1989**

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

AGENCY FOR INTERNATIONAL DEVELOPMENT  
OFFICE OF THE REGIONAL INSPECTOR GENERAL  
AMERICAN EMBASSY  
TEGUCIGALPA - HONDURAS

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

September 18, 1989

MEMORANDUM

TO: USAID/Guatemala Director, Anthony J. Cauterucci

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

SUBJECT: Audit Report No. 1-520-89-52-N, "Audit of the Small Farmer Diversification Systems Project Component with the National Bank for Agricultural Development"

This report presents the results of a non-Federal financial audit requested by your Mission of the Small Farmer Diversification Systems Project, USAID/Guatemala Project No. 520-0255, component implemented by the National Bank for Agricultural Development (Banco Nacional de Desarrollo Agricola - BANDESA). The audit covered the period from the start of BANDESA's project operations on July 7, 1983 through June 30, 1987. It did not cover the remainder of the project period which ended on March 31, 1989. The accounting firm Touche Ross in Guatemala prepared the report which is dated August 21, 1989.

The project's major goal is to strengthen the Guatemalan agricultural sector's livestock and to stimulate small farm diversification from basic grains to higher value diversified crops of greater labor intensity. BANDESA's role in the project is to manage a trust fund created under the project's loan agreement to provide loans and grants to small and medium-sized farmers. The trust fund received about US\$2.0 million in project funds during the audit period.

The purpose of this audit was to determine whether: (1) the financial statements for the project component implemented by BANDESA fairly present project receipts and disbursements for the period with disclosure of questionable expenditures, if any,

(2) BANDESA's internal control system is adequate to manage the project component's funds, and (3) BANDESA has complied with agreement terms and applicable laws and regulations.

Touche Ross qualified its opinion on the financial statements for the project component because the funds received by BANDESA were not reconciled with those disbursed by USAID/Guatemala and the auditors were unable to apply alternative procedures to assure themselves that the project's funds were fully accounted for. The auditors found that BANDESA had not attempted to reconcile the funds it received with the records of either USAID/Guatemala or the coordinating unit established for the project and that it had not recorded expenditures made by USAID/Guatemala directly on its behalf. Additionally, they found that the Government of Guatemala's (GOG) Ministry of Public Finances (MFP) commingled the funds received from A.I.D. with the GOG's own funds and released funds to the project component based upon the GOG budget which was not in agreement with the A.I.D. reimbursements intended for the project component. Touche Ross' study and evaluation of the system of internal control over the project component revealed weaknesses which, in its opinion, result in more than a relatively low risk that errors or irregularities in amounts that would be material in relation to the project component's financial statements may occur and not be detected within a timely period. Major control weaknesses found were deficiencies in the processing of transactions through the electronic data processing system and inadequate controls over cash receipts. Also noted were deficiencies in the aging of overdue loans outstanding, the lack of supervision over the final use of some loans, lack of authorization for some grant-type payments, and failure to record a number of accounting transactions including the establishment of reserves for uncollectible loans. For the transactions it tested, Touche Ross found that BANDESA generally complied with the terms of the agreement and applicable laws and regulations except for agreement requirements to maintain separate accounting for A.I.D. versus counterpart funds. However, since this project component involves a revolving trust fund, with initial capital and reflows used to make loans and grants, Touche Ross felt it is impractical to maintain separate accountability for A.I.D. funds once they were placed into the trust fund. Nothing came to the attention of Touche Ross that caused them to believe that untested items were not in compliance with agreement terms and applicable laws and

regulations. Touche Ross identified Q.16,387 (US\$6,069) in questionable costs which involved a small number of loans where the funds were used for nonproject purposes and some grant-type payments made without evidence of proper authorization.

The Touche Ross report contains 12 recommendations regarding improvements needed in BANDESA's accountability for A.I.D. funds, internal controls, and compliance with the agreement terms and applicable laws and regulations. Although the project ended on March 31, 1989, we note that USAID/Guatemala continues to work with BANDESA on a similar follow-on project, the Highlands Agricultural Development Project, USAID/Guatemala Project No. 520-0274 phase II. We believe that the conditions noted during this audit will likely be applicable in this new project and therefore, USAID/Guatemala should require implementation of all the Touche Ross recommendations to the extent they would be appropriate in settling matters related to the audited project or useful in promoting better accountability over the new project. In this regard, we consider those findings related to the lack of accountability for A.I.D. funds, inadequate internal controls over the electronic data processing system and cash receipts, and the questionable costs to be particularly significant. Also, we believe that a final close-out audit is needed for the project component since the audit found a lack of full accountability over A.I.D. funds and material internal control weaknesses. We are making the following recommendations which will be included in the Office of the Inspector General's audit recommendation follow-up system.

Recommendation No. 1

We recommend that USAID/Guatemala negotiate a settlement with the National Bank for Agricultural Development (BANDESA) concerning the disposition of the Q.16,387 (US\$6,069) of costs considered questionable by the Touche Ross report dated August 21, 1989.

Recommendation No. 2

We recommend that USAID/Guatemala require the Government of Guatemala's (GOG) Ministry of Public Finances (MFP) to establish and maintain separate accounts and accountability for A.I.D. project funds which should not be commingled with the GOG's own

funds. Failing this, USAID/Guatemala should consider providing the funds directly to the implementing entity without passing through the MFP.

Recommendation No. 3

We recommend that USAID/Guatemala require the National Bank for Agricultural Development (BANDESA) to implement adequate internal controls over data processing and cash receipts. Material weaknesses in these areas are described by the Touche Ross report dated August 21, 1989.

Recommendation No. 4

We recommend that USAID/Guatemala arrange for a final close-out audit of the Small Farmer Diversification Systems Project, USAID/Guatemala Project No. 520-0255, component implemented by the National Bank for Agricultural Development. This should include a regular financial audit covering the period July 1, 1987 to March 31, 1989 with additional steps included to determine the amounts of A.I.D. funds provided for this component during the project's life.

The Touche Ross report was discussed with representatives from BANDESA and USAID/Guatemala on July 6, 1989 and their comments were considered in preparing this final report.

Please advise this office within 30 days of actions planned or taken to resolve and close the recommendations.

*Lara & González, CPA*  
Member Firm  
*Touche Ross International*

AUDIT OF THE SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

TABLE OF CONTENTS

	<u>Page</u>
Transmittal Letter and Summary	
Background	i
Audit objectives and scope	iii
Results of audit	iv
Management comments	v
Financial Statements	
Auditor's opinion	1
Financial Statements	3
Notes to the financial statements	6
Findings	10
Internal Controls	
Auditor's opinion	13
Findings	15
Compliance with Applicable Laws, Regulations and Agreement Terms	
Auditor's opinion	25
Findings	27
List of Report Recommendations	28
Management Comments	Annex 1

*Lara & González, CPA*  
Member Firm  
*Touche Ross International*

August 21, 1989

Mr. Coinage N. Gothard, Jr.  
Regional Inspector General for Audit  
U. S. Agency for International Development  
Tegucigalpa, Honduras, C. A.

Dear Mr. Gothard:

This report presents the results of our audit of the Small Farmer Diversification Systems Project, USAID/Guatemala Project No. 520-0255, component implemented by the National Bank for Agricultural Development (Banco Nacional de Desarrollo Agrícola - BANDESA), from July 7, 1983 to June 30, 1987.

BACKGROUND

On August 28 and September 24, 1981, the Government of Guatemala (GOG), through the Ministry of Public Finances (Ministerio de Finanzas Públicas - MPF), the Ministry of Agriculture, Livestock, and Food (Ministerio de Agricultura, Ganadería y Alimentación - MAGA), and the National Board of Economic Planning (Consejo Nacional de Planificación Económica - CNPE), signed grant agreement No. 520-0255 for US\$3,696,000 and loan agreement No. 520-T-034 for US\$5,500,000 with the U. S. Agency for International Development in Guatemala (USAID/Guatemala) for the Small Farmer Diversification Systems Project. The A.I.D. committed funds were for the purpose of financing the acquisition of the goods and services necessary to carry out the project. In addition to these funds the Government of Guatemala (GOG) committed a minimum of US\$6,700,000 in counterpart funds to finance administrative expenses and other direct and indirect costs related to the project. The completion date of the project, originally scheduled for March 31, 1987, was extended to March 31, 1989.

The project's major goal is to strengthen the agricultural sector's livestock and to stimulate small farm diversification from basic grains to higher value diversified crops of greater labor intensity. The project activities are: a) applied research and technology adaptation, b) extension and promotion, c) loans and social cost payments (contributions), d) in-service training,

e) project coordination, and f) nutritional impact evaluation.

As part of the project's loan agreement, a trust fund agreement was signed by the MPF, MAGA, and the National Bank for Agricultural Development (BANDESA). The main objective of the trust fund agreement was to provide funds to finance short and long-term loans for fruit and vegetable production, cattle raising, small scale irrigation works, and social cost payments (contributions) to project beneficiaries. Under the trust fund agreement, A.I.D. was to provide US\$3,000,000 of funds from the loan agreement No. 520-T-034 and the GOG was to provide US\$2,200,000 as counterpart contribution.

BANDESA is an autonomous decentralized banking entity of the GOG whose general objective is to promote and administer the provision of credit facilities from the GOG to the agricultural sector of the country, mainly to the small and medium-sized farmer. Its funds are obtained by means of Government trust funds and from its capital, reserves, and liabilities. BANDESA's role in the project is to manage the trust fund created by the above agreement to provide loan facilities to small and medium-sized farmers.

In addition to BANDESA there were five other institutions of the Government's agricultural sector involved in implementing the overall project as follows:

- . the Coordinating Unit for the Agricultural Diversification Program (Unidad Coordinadora del Programa de Agricultura - UCPRODA) was formed specifically to coordinate the project activities. This coordination included receiving reimbursement requests from the implementing institutions, obtaining the reimbursements from USAID/Guatemala and distributing them back to the implementing institutions; and preparing consolidated financial information on the project based on fund accountability statements or other financial statements received from each implementing institution;
- . the General Directorate for Agricultural Services (Dirección General de Servicios Agrícolas - DIGESA) was responsible for project activities involving the transfer of agricultural technology for crop production. In addition, DIGESA was responsible for reviewing and approving the technical aspects of the studies for the component's loan beneficiaries, supervising the final use of loans, and approving social cost payment disbursements made by BANDESA;
- . the General Directorate for Livestock Services (Dirección General de Servicios Pecuarios - DIGESEPE) was responsible for the livestock extension activities, focusing primarily on improving management practices related to disease, parasite control, and nutrition/feed supply;

- . the Institute of Agricultural Science and Technology (Instituto de Ciencia y Tecnología Agrícola - ICTA) was primarily responsible for the implementation of the applied research and technology adaptation component; and
- . the Technical Assistance Team (Equipo de Asistencia Técnica - EAT) was a group of professionals with extensive agricultural experience organized to coordinate some technical assistance to the project.

#### AUDIT OBJECTIVES AND SCOPE

The general objective was to perform a financial and compliance audit of the Small Farmer Diversification Systems Project component managed by the National Bank for Agricultural Development (BANDESA), for the period from July 7, 1983 to June 30, 1987. The financial statements of the trust fund, created under the project, provide the complete accounting of this component's financial information. Our review was made in accordance with generally accepted auditing standards and the United States Comptroller General's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision). Accordingly, we included such tests of the accounting records and such other audit procedures as we considered necessary in the circumstances. Our examination was made to determine whether:

1. The financial statements of the project component managed by BANDESA present fairly the component's financial position for the period from July 7, 1983 to June 30, 1987, with disclosure of questionable expenditures, if any.
2. BANDESA's internal accounting control system is adequate to manage the project component's funds as required by USAID/Guatemala. In this regard, our study included controls over the following project areas: accounting systems, disbursement and collection of loans and interest, and vehicles.
3. BANDESA has complied with applicable laws, regulations, agreement terms, and implementation letters which may have a material effect on the financial statements.

The scope of our work consisted of:

1. Reviewing the project component's financial statements for the period from July 7, 1983 to June 30, 1987.
2. Conducting a study and evaluation of the internal accounting controls, including controls over accounting systems, disbursement and collection of loans and interest, and vehicles.

3. Determining whether BANDESA has complied with agreement terms, conditions of the loan agreement, amendments, project implementation letters, and applicable laws and regulations.

## RESULTS OF AUDIT

### Financial Statements

The results of our examination of the financial statements of the project component managed by BANDESA disclosed that, except for the lack of reconciliation between funds received by BANDESA with those disbursed from USAID/Guatemala, and questionable costs of Q.16,387, the financial statements present fairly the financial position for the period from July 7, 1983 to June 30, 1987.

Some transactions, as detailed in finding No. 8 of the report on internal controls, had not been recorded by BANDESA in the component's accounting records. They were recorded on June 30, 1987 as an adjustment based on our recommendation.

### Internal Controls

Our study and evaluation of the internal controls disclosed conditions that we believe result in more than a relatively low risk that errors or irregularities, in amounts that would be material in relation to the project component's financial statements, may occur and not be detected within a timely period. These conditions were the following:

1. Electronic data processing (EDP) controls were inadequate.
2. Controls over computer tape files and report copies were deficient.
3. The EDP department had not developed and implemented a disaster recovery plan.
4. A reserve for uncollectable loans was not recorded.
5. Reports on aging of overdue loans outstanding had deficiencies.
6. There was a lack of supervision over the final use of some loans.
7. There was a lack of control over prenumbered cash receipt forms.
8. Some transactions were not recorded.
9. There was a lack of authorization on some social cost payments.

As set forth in the scope of work, our study and evaluation of BANDESA's internal controls included the following major areas with the following results:

- A. Accounting Systems. Controls in this area were not adequate mainly in the recording of transactions in the EDP Department as explained in the findings No. 1 through No. 3 in the report on internal controls.
- B. Disbursements and Recovery of Loans and Interest. Our evaluation in this area disclosed the following: lack of a reserve for possible loan losses, deficient aging reports on loan balances, lack of control over prenumbered cash receipt forms, and no evidence of authorization on social cost payments. See findings No. 4 through No. 9 in the report on internal controls.
- C. Vehicle Controls. Our evaluation of the vehicle controls did not disclose any material weakness.

Compliance with Applicable Laws, Regulations, and Agreement Terms

As a result of our review, except for the absence of separate records by source of funds for the project, which was required by the agreement, we believe that BANDESA has complied in general terms with applicable laws, regulations, and with the project's agreement terms, amendments, and project implementation letters. Nothing came to our attention that caused us to believe that untested items were not in compliance with applicable laws, regulations, and agreement terms.

MANAGEMENT COMMENTS

A draft copy of this report was provided to BANDESA and on July 6, 1989 was discussed with them. BANDESA provided written comments which we have included as Annex I.

BANDESA took exception to our statement that questionable loans and social cost payments made were due to inadequate internal controls. It said the amounts were minimal in relation to the total amounts loaned and granted. It also stated that the problem with lack of reconciliations between itself, the Coordinating Unit for the Agricultural Diversification Program (UCPRODA) and A.I.D. and the problem with the Government of Guatemala not passing through A.I.D. reimbursements to BANDESA were both of a nature beyond BANDESA's control and that it therefore shared no blame in the matter. Lastly, BANDESA did not agree that vehicles provided for the project by A.I.D. should be accounted for under the trust fund. It stated that the trust

fund agreement does not mention these fixed assets and that in similar situations such assets have been recorded as part of the bank's financial statements rather than the specific trust fund.

We do not agree with BANDESA's contention that just because the number and amounts of the loans and social cost payments that we questioned were small in comparison to the total of such loans and grants that a conclusion should be drawn that internal controls in this areas were okay. BANDESA needs to have controls to assure that loans are used for the purposes authorized by the agreement and that social cost payments are authorized by the appropriate entity as specified in the agreement. Controls need to be in place to assure that each and every loan and social cost payment are in accordance with agreement terms. Additionally, BANDESA needs to strenghten its internal controls in the other areas mentioned in the audit report.

Regarding the problem of reconciling the money that BANDESA has recorded as being received from A.I.D. with the money that A.I.D. shows as having been disbursed, we admit that the resolution of the recommendation will require coordination with various entities outside BANDESA's control. However, BANDESA still has a key role in implementing the recommendation and cannot consider the problem to be someone else's.

Lastly, we consider the proper accounting for fixed assets provided by A.I.D. to the project would be to account for them as part of the trust fund because BANDESA represented to us that the trust fund showed the complete accounting for the project. However the important point is to have full accountability over A.I.D. funds. We would tend to believe that mixing the A.I.D. fixed assets with those of the remainder of the organization would lead to misuse and loss of accountability.

TOUCHE ROSS & CO.



Lic./Rolando Lara Leiva

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255  
REPORT ON FINANCIAL STATEMENTS  
AUDITOR'S OPINION

We have performed a financial and compliance audit of the balance sheet of the trust fund created under the Small Farmer Diversification Systems Project, USAID/Guatemala Project No. 520-0255, as of June 30, 1987 and the related statements of revenues and expenses and cash flow for the period from July 7, 1983 to June 30, 1987. The trust fund is managed by the National Bank for Agricultural Development (Banco Nacional de Desarrollo Agrícola - BANDESA). Except as explained in the following paragraph, our examination was made in accordance with generally accepted auditing standards and the United States Comptroller General's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision) and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary under the circumstances.

As described in the accompanying finding No. 1, the funds received by BANDESA were not reconciled with those disbursed by USAID/Guatemala and we were unable to apply alternative procedures to satisfy ourselves of the funds disbursed by USAID/Guatemala and received by BANDESA.

As described in Note D, we considered costs of Q.16,387 to be questionable. These consisted of social cost payments (contributions) which were made without the approval of DIGESA and loans which were used for other than agreed upon purposes.

As described in Note A.1, BANDESA reports its income on a modified cash basis, in which revenues are recognized when received, rather than when earned; but expenses and liabilities are recorded when they are incurred. Accordingly the accompanying financial statements are not intended to present the financial information in conformity with generally accepted accounting

*Lara & González, CPA*

*Member Firm*

*Touche Ross International*

principles.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to reconcile funds disbursed by USAID/Guatemala with those received by BANDESA, the financial statements referred to above present fairly the financial position of the trust fund created under the Small Farmer Diversification Systems Project, USAID/Guatemala Project No. 520-0255, as of June 30, 1987; and the results of its operations and its sources and uses of funds for the period from July 7, 1983 to June 30, 1987, on the basis of accounting described in Note A which has been applied consistently during the period.

*Touche Ross & Co.*

June 27, 1988  
Guatemala

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
 COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
 USAID/GUATEMALA PROJECT No. 520-0255

BALANCE SHEET

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT TRUST FUND

JUNE 30, 1987

<u>A S S E T S</u>		<u>LIABILITIES AND TRUST FUND'S EQUITY</u>	
Current Assets:		Current Liabilities:	
Cash (Q.285,561 in savings accounts, 11%)	Q.1,102,578	Approved Loans not Disbursed	Q. 620,252
Investments: (Note D)		Accrued Expenses	87,072
Loans receivable, less reserve for uncollectable loan losses of Q.210,000	2,332,585	Advances from Government of Guatemala	<u>325,182</u>
Interest Receivable on Loans	110,801		<u>1,032,506</u>
Other receivables	393,333	Social Cost Payments:	
Approved Loans not Disbursed	620,252	Funds Received	659,825
Vehicles	<u>50,655</u>	Funds Disbursed	<u>(606,423)</u>
			<u>53,402</u>
		Deferred Credits:	
		Unearned Income	<u>110,801</u>
		Trust Fund's Equity: (Note B)	
		Grants disbursed to the trust fund by:	
		U.S. Agency for International Development	2,022,766
		Government of Guatemala	<u>1,495,491</u>
			3,518,257
		Other Asset Contributions	50,655
		Excess of Expenses Over Revenues	<u>(155,417)</u>
			<u>3,413,495</u>
	Q.4,610,204		Q.4,610,204
	=====		=====
Memorandum Accounts:			
Loan Guaranties-Agrarian Pledge	Q.8,154,370		
Loan Guaranties-Pledge Held by Beneficiaries	646,902		
Loan Guaranties-Mortgages	<u>174,979</u>		
	Q.8,976,251		
	=====		

See notes to the trust fund's financial statements.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT

USAID/GUATEMALA PROJECT No. 520-0255

STATEMENT OF REVENUES AND EXPENSES

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT TRUST FUND

From July 7, 1983 to June 30, 1987

Revenue:		
Government of Guatemala Contributions		Q. 108,186
Other Trust Fund Contributions		73,895
Loan Interest		95,729
Savings Account Interest		45,610
Other		<u>310</u>
Total Revenue		<u>323,730</u>
Expenses:		
Operation Expenses:		
Paid in Cash	Q.182,130	
Accrued Expenses	<u>87,017</u>	269,147
Uncollectible Loans		<u>210,000</u>
Total Expenses		<u>479,147</u>
Excess of Expenses Over Revenue		Q. (155,417) =====

See notes to the trust fund's financial statements.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
 COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
 USAID/GUATEMALA PROJECT No. 520-0255

CASH FLOW STATEMENT

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT TRUST FUND

From July 7, 1983 to June 30, 1987

SOURCES OF FUNDS:

Contributions for loans to project's beneficiaries:	
A.I.D.	Q.1,629,601
Government of Guatemala	1,495,491
Contributions for social cost payments	
A.I.D.	380,318
Government of Guatemala	279,507
Government of Guatemala contribution for operating expenses	108,186
Advances from the Government of Guatemala	325,182
Other trust fund contributions	73,895
 Collections of:	
Loan principal	875,096
Interest	95,729
 Savings account interest	45,610
 Other revenue	310
Other liabilities	<u>55</u>
 Total Sources	<u>5,308,980</u>

USES OF FUNDS:

Loan disbursements	3,417,681
Social cost payment disbursements	606,423
Operating expenses	182,130
Other account receivable	<u>168</u>
 Total Uses of Funds	<u>4,206,402</u>

Cash to June 30, 1987	Q.1,102,578
	=====

See notes to the trust fund's financial statements.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT

USAID/GUATEMALA PROJECT No. 520-0255

NOTES TO THE FINANCIAL STATEMENTS

From July 7, 1983 to June 30, 1987

A. Summary of Significant Accounting Policies

1. Basis of Presentation. BANDESA is a bank supervised by Guatemala's Superintendent of Banks. Consequently, it has adopted the practices applicable to banks in Guatemala. Under these practices, it uses a modified cash basis of accounting in which revenues are recognized when received, rather than when earned; but expenses and liabilities are recorded when they are incurred. The presentation of the project trust fund's financial statements is done in accordance with the format used by the banks of Guatemala.
2. Operational Expenses. The expenses incurred by the BANDESA's trust fund department are allocated to the different trust funds, including the project's trust fund based on procedures that were approved by A.I.D. From July 7, 1983 to June 30, 1987, the project's trust fund was charged a total of Q.269,147 for operational expenses.
3. Trust Fund's Equity. The project trust fund's equity is made up of A.I.D. contributions from loan agreement No. 520-T-034 and GOG counterpart contributions as specified by the project agreement.
4. Social Cost Payments. Social cost payments are cash contributions to project beneficiaries. The funds received for social cost payments are recorded as liabilities. Disbursements to beneficiaries reduce the amount of these liabilities.

B. Grant and Loan Agreements

On August 28, and September 24, 1981, the Government of Guatemala (GOG), through the Ministry of Public Finances, (Ministerio de Finanzas Públicas - MPF); the Ministry of Agriculture, Livestock, and Food (Ministerio de Agricultura, Ganadería y Alimentación - MAGA); and the National Board of Economic Planning (Consejo Nacional de Planificación Económica - CNPE), signed grant agreement No. 520-0255 for US\$3,696,000 and loan agreement No. 520-T-034 for US\$5,500,000 with the U.S. Agency for International Development in Guatemala (USAID/Guatemala). The completion date of the project, originally scheduled for March 31, 1987, was extended to March 31, 1989.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT

COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT

USAID/GUATEMALA PROJECT No. 520-0255

STATEMENT OF REVENUES AND EXPENSES

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT TRUST FUND

From July 7, 1983 to June 30, 1987

The agreements were signed to implement the Small Farmer Diversification Systems Project through six Guatemalan Government institutions. The project's major goal was to strengthen the agricultural sector's livestock and to stimulate small farm diversification from basic grains to higher value diversified crops of greater labor intensity. The project activities were: a) applied research and technology adaptation, b) extension and promotion, c) loans and social cost payments (contributions), d) in-service training, e) project coordination, and f) nutritional impact evaluation.

BANDESA is responsible for the administration of the trust fund component of the Small Farmer Diversification Systems Project. It provides loans and social cost payments (contributions) to small farmers to promote agricultural diversification, basically in the areas of agriculture, cattle, and small scale irrigation infrastructure.

C. Implementing Institution

BANDESA is an autonomous and decentralized banking institution of the Government of Guatemala (GOG). It was created by the Congress of the Republic of Guatemala on December 22, 1970, starting operations in May 1971. Its objectives are to promote and administer the provision of credit facilities from GOG to the agricultural sector of the country, mainly to the small and medium-sized farmers. Its funds come from Government trust funds and from its capital, reserves, and liabilities. BANDESA operates 37 state agencies, 31 rural collecting centers, and 5 information offices around the country.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT

USAID/GUATEMALA PROJECT No. 520-0255

STATEMENT OF REVENUES AND EXPENSES

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT TRUST FUND

From July 7, 1983 to June 30, 1987

D. Questionable Costs

Due to inadequate internal controls, funds amounting to Q.16,387 were questionable, and are itemized as follows:

- . Five farmers who received loans used these funds for purposes other than those required by the agreement terms. Q. 9,384
  - . Six beneficiaries received social cost payments without evidence of authorization by DIGESA's coordinator. 7,003
- Q.16,387  
=====

E. Trust Fund Agreement

As part of loan agreement No. 520-T-034, a trust fund agreement was signed on December 3, 1982 by the Ministry of Public Finances (MPF), the Ministry of Agriculture, Livestock, and Food (MAGA), and the National Bank for Agricultural Development (BANDESA). The main objective of the trust fund agreement was to provide funds to finance short and long-term loans for fruit and vegetable production, cattle raising, small scale irrigation works, and social cost payments to project beneficiaries. Under the trust fund agreement, A.I.D. was to provide US\$3,000,000 of funds from loan agreement No. 520-T-034 and the GOG was to provide US\$2,200,000 as counterpart contribution. The reflows of loans and interest generated from the loans collections were to be used to continue providing loans to small and medium-sized farmers.

Among the conditions of the trust fund agreement were:

- . The agreement is for a 20-year term.
- . 8% interest rate for short and long-term loans to individual farmers, 5% and 6% to cooperatives and organized groups; 2% for small-irrigation works loans. On September 21, 1987, these rates were changed to 10% interest for all the loans.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT

USAID/GUATEMALA PROJECT No. 520-0255

STATEMENT OF REVENUES AND EXPENSES

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT TRUST FUND

From July 7, 1983 to June 30, 1987

- . Establish a revolving fund.
- . Invest the excess reflows generated from the loan collections and interest in non-government saving accounts.
- . GOG counterpart contribution for operating expenses will be provided based on 5% of current loans and 7% of loan reflows.
- . Maximum amount of loans is Q.25,000 for individual farmers and Q.250,000 for cooperatives. Cooperatives are not allowed to disburse loans for amounts over Q.5,000 per member.

F. Monetary Unit

The project trust fund's financial statements are stated in Quetzales (Q.), the monetary unit of Guatemala. Foreign currency transactions must be realized through the banking system in which three different exchange rates have been established: the official market rate (Q.1:US\$1) to pay the public debt and those private liabilities registered prior to June 6, 1986; the regulated market rate to pay for imports and liquidate exports, and the banking market rate for those transactions not included in the above mentioned markets. As of June 30, 1987, the regulated market rate was Q.2.50:US\$1 and the banking market rate was Q.2.60:US\$1. On June 23, 1988, the exchange rate applied in the regulated and banking markets was unified at Q.2.70:US\$1.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON FINANCIAL STATEMENTS

FINDINGS

1. Financial Information Was not Reconciled

Condition:

- A. BANDESA never attempted to reconcile the funds it received for the project's trust fund with the funds disbursed by USAID/Guatemala.
- B. Also, BANDESA had not attempted to reconcile its records with those of the Coordinating Unit for the Agricultural Diversification Program (UCPRODA), and UCPRODA was submitting financial information to USAID/Guatemala, which purported to reflect BANDESA information, that did not agree with BANDESA's information.
- C. USAID/Guatemala had directly purchased some fixed assets, but not all of these transactions had been recorded by BANDESA.

Criteria:

As part of the internal control system over project funds, the project trust fund's financial statements must be reconciled on a monthly basis with the reports prepared by UCPRODA and submitted to USAID/Guatemala and with USAID/Guatemala records of disbursements to the project.

Cause:

There was a lack of supervision over the project by the managements of BANDESA and UCPRODA and a lack of communication among BANDESA, UCPRODA and USAID/Guatemala.

Effect:

The financial information prepared and provided by BANDESA and UCPRODA was not reliable. Errors or irregularities could occur and not be detected on a timely basis.

Recommendation:

USAID/Guatemala should require the National Bank for Agricultural Development (BANDESA) to:

- A. Reconcile, on a monthly basis, its financial statements with information reported by the Coordinating Unit for the

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON FINANCIAL STATEMENTS

FINDINGS

- Agricultural Diversification Program (UCPRODA) to USAID/Guatemala and investigate differences, if any.
- B. Reconcile, on a monthly basis, the funds it receives for the project with the amounts disbursed by USAID/Guatemala.
- C. Record expenditures paid directly by USAID/Guatemala. These expenditures should be identified as having been paid directly by USAID/Guatemala.
2. Funds Were Commingled at the Government of Guatemala Level and not Provided to the Project as Reimbursed by A.I.D.

Condition:

USAID/Guatemala funds disbursed for the project component had been commingled with the Government of Guatemala's (GOG's) funds before the GOG provided the A.I.D. funds to BANDESA. Additionally, GOG's Ministry of Public Finances (MPF) disbursed the USAID/Guatemala funds to the project revolving fund bank account for BANDESA based on GOG's planned disbursements for this component of the project rather than simply passing on the amounts received from USAID/Guatemala.

Criteria:

- A. Section B.5, Annex II of the loan and grant agreements required that a separate bank account should be established for the project funds.
- B. USAID/Guatemala funds should be disbursed by MPF to the project implementing institutions in the amounts provided by USAID/Guatemala.

Cause:

The MPF followed the plan of disbursements of the GOG which was different from the amounts reimbursed by USAID/Guatemala.

Effect:

As BANDESA did not keep track of USAID/Guatemala's advances and reimbursements to it, it was not possible to reconcile the funds disbursed from A.I.D.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON FINANCIAL STATEMENTS

FINDINGS

Recommendation:

USAID/Guatemala should require the Government of Guatemala (Ministry of Public Finances) to keep USAID/Guatemala funds separate and to distribute the funds to the implementing institutions for each project component based on USAID/Guatemala's budgetary and reimbursement determination.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT

USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

AUDITOR'S OPINION

We have performed a financial and compliance audit of the financial statements of the Small Farmer Diversification Systems Project, USAID/Guatemala Project No. 520-0255, component managed by the National Bank for Agricultural Development (Banco Nacional de Desarrollo Agrícola - BANDESA) for the period from July 7, 1983 to June 30, 1987 and have issued our report thereon dated June 27, 1988. As part of our examination, we performed a study and evaluation of BANDESA's system of internal accounting and administrative controls to the extent that we considered necessary to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the financial statements. Our study and evaluation was made in accordance with generally accepted auditing standards and the United States Comptroller General's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision), and was more limited than would be necessary to express an opinion on the system of internal accounting control taken as a whole. It included a review of the significant internal controls in the areas of accounting systems, disbursement and collection of loans and interest, and vehicles.

The management of BANDESA is responsible for establishing and maintaining a system of internal control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of an internal control system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization, and properly recorded to permit the preparation of financial information in accordance with generally accepted accounting principles and/or on a comprehensive accounting basis. Because of

*Lara & González, CPA*

*Member Firm*

*Touche Ross International*

inherent limitations in any system of internal control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with the procedures may deteriorate.

Our study and evaluation, made with the limited purpose as described in the first paragraph, would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the system of internal control of BANDESA taken as a whole, or on any of the categories of controls identified in the first paragraph. However our study and evaluation disclosed the conditions described in the accompanying findings No. 1 to No. 9, that we believe result in more than a relatively low risk that errors or irregularities in amounts that would be material in relation to the financial statements for this component of the project may occur and not be detected within a timely period.

These conditions were considered in determining the nature, timing, and extent of the audit tests to be applied in our examination of the component's financial statements for the period from July 7, 1983 to June 30, 1987, and this report does not affect our opinion on those financial statements.

This report is intended solely for the use of BANDESA and the U.S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter of public record.

*Touche Ross & Co.*

June 27, 1988  
Guatemala

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

1. Electronic Data Processing Controls Were Inadequate

Condition:

Transactions processed in BANDESA's electronic data processing (EDP) department were not adequately controlled due to the following:

- A. All the programmers had access to the information data files and utility and application programs and they were authorized to make changes without supervision by the EDP manager. For example, the program that determines the loan balances, interest, maturity, and other information (Program CAR 308), allows changes without special authorization and no record is generated showing that a change has been made.
- B. Twelve terminals were available inside the computer center and no restrictions existed for access to the system. No password was used to restrict on-line access to operators.
- C. Some utility programs included an editor program that allowed any user to make changes in the files without leaving any evidence. For example the program that processed loan balances, interest, maturity date, and others, CAR 308, allows changes to any data field.
- D. Our review showed vouchers which indicated that they were corrections to erroneous transactions that had been entered into the computer system. However, in the processing of the corrections the original record is erased without leaving an audit trail. Therefore, there was no way to check the original transaction or the appropriateness of the correction.
- E. Internal audit reviews of EDP activities were limited to physical security and some tests on inputs and outputs. Reviews of the contents of data files had never been performed.

Criteria:

The EDP system should contain procedures to limit access by unauthorized persons to the computer data files and software; to validate the input and output information; and to ensure that transactions are reviewed and approved by authorized officials.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

Some of the typical types of controls are: processing, authorization, edits, conversion, verification of processing, security controls, master file controls, change procedures, and periodic internal audits.

Cause:

The EDP department considers that the current flexible procedures facilitate providing assistance to users on a timely basis. There is lack of concern about the risks being incurred.

Effect:

The deficiencies mentioned above could result in loss of information, access to information by unauthorized personnel, changes to data files and programs, and the recording of unauthorized transactions without timely detection.

Recommendation:

USAID/Guatemala should require the National Bank for Agricultural Development (BANDESA) to implement an adequate internal control system in the electronic data processing (EDP) area to assure control of the transactions processed. The new controls to be implemented should include, among others:

- a) Policies of authorization and supervision over access to data files and utility and applications programs.
- b) Establishment of restrictions over access to the system through the terminals. Passwords should be changed periodically.
- c) Removal of all utility programs from the system with access to these programs being strictly controlled by the EDP manager.
- d) Planning and implementation of an intensive program to train internal audit personnel to audit the EDP department.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

2. Controls over Computer Tape Files and Report Copies Were Deficient

Condition:

- A. The computer system's memory maintains a record of the processing and results of only one day's transactions. Those of previous days are not retained.
- B. Data files on computer tapes are not delivered to the tape library immediately after they are utilized. Some computer tapes remain in the processing center for more than 30 days.
- C. The EDP department prepares several copies of the same reports. Apparently, however, not all the copies are used.

Criteria:

The computer system's memory should be able to keep the transactions recorded for a reasonable period of time to provide a trail of those transactions when it is deemed necessary. In addition, the library should have custody of tapes on data files and the computer center should submit them to the library as soon as they have been updated.

Cause:

The internal controls in the EDP department are weak and the memory capacity of the system may be insufficient.

Effect:

It was not possible to trace transactions processed through the computer. Therefore, unauthorized changes could be introduced to production tapes and not be detected opportunely. Also, in case of a mishap, BANDESA would not be able to reconstruct the information.

Recommendations:

The National Bank for Agricultural Development (BANDESA) should take the following additional measures to strenghten controls over computer files and report copies:

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

- A. Evaluate the system in place in order to determine whether it is necessary to expand the memory capacity of the computer system to retain a record of processed transactions for a reasonable period of time or whether the problem lies strictly in the applications programs.
- B. Keep a library of all the tapes processed in the computer center and assure that tapes are returned to the library as soon as they are updated. Library tapes should be kept in a safe place and access restricted to authorized personnel.
- C. Evaluate the distribution and number of copies needed of the reports generated by the electronic data processing department.

3. The Electronic Data Processing Department Had not Developed and Implemented a Disaster Recovery Plan

Condition:

All the programs, data files, and reports generated from the EDP system were kept in BANDESA's headquarters building. No extra copies were kept outside of the building.

Criteria:

A contingency plan should be developed, documented, and periodically tested to assure the ability to continue data processing services in the event of a disaster.

Cause:

BANDESA's management had not considered the risk that the lack of a disaster plan could imply.

Effect:

Serious disruptions in BANDESA's operations could occur if data files were damaged or lost.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

Recommendation:

The National Bank for Agricultural Development (BANDESA) should develop a disaster recovery plan for its electronic data processing system consisting of a disaster recovery team; off-site storage of a back-up system and data files and forms; a previously contracted back-up processing site for initiation of procedures and processing priorities; and procedures for updating the contingency plan.

4. A Reserve for Uncollectible Loans Was not Recorded

Condition:

As of June 30, 1987, matured loans and loan installments due represented 8% and 3% respectively, of the portfolio. However, BANDESA had not recorded a reserve for uncollectible loans. A reserve of Q.210,000 was recorded as a result of our recommendation.

Criteria:

A reserve for uncollectible loans should be determined, based on analysis of past experience and the nature of project loans.

Cause:

Transactions are recorded on a cash basis. In addition, the trust fund's agreement did not require this reserve.

Effect:

Financial statements did not present fairly the expected losses from uncollectable loans.

Recommendation:

USAID/Guatemala should require the National Bank for Agricultural Development (BANDESA) to evaluate and determine a reasonable percentage to compute as a reserve for uncollectible loans and interest and reevaluate and adjust this reserve on a periodic basis.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

5. Reports on Aging of Overdue Loans Outstanding had Deficiencies

Condition:

The reports on loan installments outstanding and overdue, reports CAR 520A and CAR 520B respectively, had weaknesses as follows:

- A. The reports were not totalled and reconciled with general ledger records.
- B. The CAR 520B report for May 1988, omitted two loans.
- C. There were errors in classifications of loans by geographical origin.
- D. The reports generated by the program for aging loans used improper aging classifications. For example, some loans which were 30, 90 and 180 days overdue, were classified with those more than 365 days past due. Loan aging ranges included a classification of 90 to 180 days, which we considered could hamper timely detection of seriously overdue loans.

Criteria:

Loan aging reports should be accurate so that management can make appropriate decisions.

Cause:

The program for aging loans was designed using the above mentioned ranges and there was lack of supervision over the preparation of aging reports.

Effect:

The lack of reliable information could result in management not taking necessary corrective measures on a timely basis.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

Recommendation:

The National Bank for Agricultural Development (BANDESA) should revise its software program for aging loans to ensure proper aging classification of all loans, reconcile on a monthly basis the aging reports with subsidiary and general ledgers, and establish aging ranges with 30-day intervals up to 180 days.

6. There Was Lack of Supervision over the Final Use of Some Loans

Condition:

During our on-site visits to loan beneficiaries, we detected that five farmers who had received loans for a total of Q.9,384 used the funds for purposes other than those required by the agreement.

Criteria:

The General Directorate for Agricultural Services (DIGESA) and BANDESA should closely supervise loans to ensure that funds are used as intended for the project.

Cause:

There was a lack of supervision by DIGESA, the institution in charge of the activity, and by BANDESA to ensure that the use of project loans was in accordance with the agreement.

Effect:

Some funds were not used to meet project objectives.

Recommendation:

The National Bank for Agricultural Development (BANDESA) should coordinate with the General Directorate for Agricultural Services (DIGESA) to institute close supervision over the uses of loans made with project funds to ensure that they are used only for intended purposes.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

7. There Was Lack of Control over Prenumbered Cash Receipt Forms

Condition:

When reviewing cash receipts we detected the following deficiencies:

- A. The cash receipts received from BANDESA's different agencies were segregated by the accounting department and processed by the electronic data processing (EDP) department by source of funds, without ensuring that all the cash receipt numbers were accounted for.
- B. There were two separate sets of prenumbered cash receipt forms being used by the bank's agencies.
- C. The internal audit department performed a review of cash receipts at BANDESA's 37 agency offices, including a review to determine whether all cash receipts numbers were issued in sequential order. However it did not compare the cash receipts reported by the agencies to those recorded in the headquarters office. Also, the voided receipts were kept in the agencies' files.

Criteria:

A good internal control system should establish procedures to ensure that all the cash receipts are reviewed and recorded, and that prenumbered cash receipt forms are properly used and verified.

Cause:

Management was not aware of the implied risk concerning the lack of control over prenumbered cash receipt forms.

Effect:

BANDESA's incomplete controls over cash receipts leaves open the possibility that improper use of funds could occur without being detected.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON INTERNAL CONTROLS

FINDINGS

Recommendation:

The National Bank for Agricultural Development (BANDESA) should implement procedures to ensure that all cash receipts are received and recorded in sequential order. Also, the agencies should be instructed to use only one set of prenumbered cash receipt forms and to withdraw the receipts that will no longer be used from circulation.

8. Some Transactions Were not Recorded

Condition:

The following transactions had not been recorded. They were incorporated as an adjustment suggested during the audit: expenses incurred by BANDESA and not reimbursed by USAID/Guatemala for Q.67,982 of indirect costs pending A.I.D. approval of BANDESA's methodology for allocating its indirect costs amongst its various trust funds; fixed assets worth Q.50,655 paid for directly by A.I.D. which BANDESA was aware of but for which it had not determined the proper accounting; and a reserve for uncollectible loans for Q.210,000.

Criteria:

In accordance with the modified cash basis accounting procedures used by BANDESA, revenues should be recorded when they are received and expenses when they are incurred.

Cause:

These transactions were unusual in nature and there was a lack of upper management supervision over the accounting department to assure that they were addressed.

Effect:

Financial information was not reliable.

Recommendation:

The National Bank for Agricultural Development (BANDESA) should exercise closer supervision over its accounting department to ensure that unusual and non-recurring type transactions, such as

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255  
REPORT ON INTERNAL CONTROLS

FINDINGS

those noted in this finding, are recorded on a timely basis.

9. There Was a Lack of Authorization on Some Social Cost Payments

Condition:

There were social cost payments (contributions) for Q.7,003 made without evidence of authorization from the General Directorate for Agricultural Services' (DIGESA's) coordinator.

Criteria:

Approved bylaws establish that social cost payments should be approved by DIGESA's coordinator of soil conservation prior to disbursement.

Cause:

We were told that authorization of DIGESA's coordinator was made in previous years. However, it could not be located.

Effect:

Social cost payments could be granted for non-project purposes.

Recommendation:

The National Bank for Agricultural Development (BANDESA) should ensure that all social cost payments are authorized by the General Directorate for Agricultural Services' (DIGESA's) coordinator prior to disbursement. Authorizations should be obtained in writing.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255  
REPORT ON COMPLIANCE WITH APPLICABLE LAWS, REGULATIONS,  
AND AGREEMENT TERMS  
AUDITOR'S OPINION

We have performed a financial and compliance audit of the financial statements of the Small Farmer Diversification Systems Project, USAID/Guatemala Project No. 520-0255, component managed by the National Bank for Agricultural Development (Banco Nacional de Desarrollo Agrícola - BANDESA) for the period from July 7, 1983, to June 30, 1987 and we have issued our report thereon dated June 27, 1988. Our study and evaluation was made in accordance with generally accepted auditing standards and the U.S. Comptroller General's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision), which includes requirements for the review of compliance with applicable laws, regulations, and agreement terms. Accordingly, our examination included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. The laws, regulations, and agreement terms reviewed for compliance included:

1. Grant agreement No. 520-0255 and loan agreement No. 520-T-034, their amendments and project implementation letters.
2. A.I.D. procurement regulations.
3. The project trust fund agreement.
4. Banking law of Guatemala.
5. Applicable tax laws in Guatemala.

The results of our study indicate, except for the accompanying finding No. 1, that for the items tested, BANDESA complied, in

*Lara & González, CPA*

*Member Firm*

*Touche Ross International*

general, with applicable laws, regulations, and agreement terms. Nothing came to our attention that caused us to believe that untested items were not in compliance with the applicable laws, regulations, and agreement terms.

This report is intended solely for the use of the management of BANDESA and the U. S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter of public record.

*Touche Ross & Co.*

June 27, 1988  
Guatemala

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

REPORT ON COMPLIANCE WITH APPLICABLE LAWS, REGULATIONS,  
AND AGREEMENT TERMS  
FINDINGS

1. A.I.D. and Counterpart Funds Were Commingled

Condition:

BANDESA had separate accounting records for the project's trust fund; however, within the trust fund itself the funds provided by USAID/Guatemala were commingled with Government of Guatemala (GOG) counterpart funds.

Criteria:

Section B.5, Annex II of the loan and grant agreements established the requirements for information, records, inspections, and periodic audits. One requirement was that funds from different sources not be commingled.

Cause:

The trust fund agreement signed by the Ministry of Public Finances (MPF), the Ministry of Agriculture, Livestock, and Food (MAGA), and BANDESA did not require separate records for A.I.D. and GOG counterpart funds. In addition, for trust funds it is not practical to separate funds by financing source because the reflows, earned interest, expenditures, and other transactions could only be segregated by source of funds based on assumptions as to what percentage of each transaction should be accounted for under A.I.D. versus counterpart funds.

Effect:

It was not possible to identify the trust fund's disbursements and available funds by source of funds. In addition, the above mentioned clause of the agreements was not complied with.

Recommendation:

The National Bank for Agricultural Development (BANDESA), as regards the project's trust fund, should request a waiver from USAID/Guatemala of the requirement for maintenance of separate accounts and accountability for A.I.D. funds.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

LIST OF REPORT RECOMMENDATIONS

FINANCIAL STATEMENTS

1. USAID/Guatemala should require the National Bank for Agricultural Development (BANDESA) to:
  - A. Reconcile, on a monthly basis, its financial statements with information reported by the Coordinating Unit for the Agricultural Diversification Program (UCPRODA) to USAID/Guatemala and investigate differences, if any.
  - B. Reconcile, on a monthly basis, the funds it receives for the project with the amounts disbursed by USAID/Guatemala.
  - C. Record expenditures paid directly by USAID/Guatemala. These expenditures should be identified as having been paid directly by USAID/Guatemala.
2. USAID/Guatemala should require the Government of Guatemala (Ministry of Public Finances) to keep USAID/Guatemala funds separate and to distribute the funds to the implementing institutions for each project component based on USAID/Guatemala's budgetary and reimbursement determination.

INTERNAL CONTROLS

1. USAID/Guatemala should require the National Bank for Agricultural Development (BANDESA) to implement an adequate internal control system in the electronic data processing (EDP) area to assure control of the transactions processed. The new controls to be implemented should include, among others:
  - a) Policies of authorization and supervision over access to data files and utility and applications programs.
  - b) Establishment of restrictions over access to the system through the terminals. Passwords should be changed periodically.
  - c) Removal of all utility programs from the system with access to these programs being strictly controlled by the EDP manager.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

LIST OF REPORT RECOMMENDATIONS

- d) Planning and implementation of an intensive program to train internal audit personnel to audit the EDP department.
2. The National Bank for Agricultural Development (BANDESA) should take the following additional measures to strengthen controls over computer files and report copies:
  - A. Evaluate the system in place in order to determine whether it is necessary to expand the memory capacity of the computer system to retain a record of processed transactions for a reasonable period of time or whether the problem lies strictly in the applications programs.
  - B. Keep a library of all the tapes processed in the computer center and assure that tapes are returned to the library as soon as they are updated. Library tapes should be kept in a safe place and access restricted to authorized personnel.
  - C. Evaluate the distribution and number of copies needed of the reports generated by the electronic data processing department.
3. The National Bank for Agricultural Development (BANDESA) should develop a disaster recovery plan for its electronic data processing system consisting of a disaster recovery team; off-site storage of a back-up system and data files and forms; a previously contracted back-up processing site for initiation of procedures and processing priorities; and procedures for updating the contingency plan.
4. USAID/Guatemala should require the National Bank for Agricultural Development (BANDESA) to evaluate and determine a reasonable percentage to compute as a reserve for uncollectible loans and interest and reevaluate and adjust this reserve on a periodic basis.
5. The National Bank for Agricultural Development (BANDESA) should revise its software utility program for aging loans to ensure proper aging classification of all loans, reconcile on a monthly basis the aging reports with subsidiary and general ledgers, and establish aging ranges with 30-day intervals up to 180 days.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT

COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT

USAID/GUATEMALA PROJECT No. 520-0255

LIST OF REPORT RECOMMENDATIONS

6. The National Bank for Agricultural Development (BANDESA) should coordinate with the General Directorate for Agricultural Services (DIGESA) to institute close supervision over the uses of loans made with project funds to ensure that they are used only for intended purposes.
7. The National Bank for Agricultural Development (BANDESA) should implement procedures to ensure that all cash receipts are received and recorded in sequential order. Also, the agencies should be instructed to use only one set of prenumbered cash receipt forms and to withdraw the receipts that will no longer be used from circulation.
8. The National Bank for Agricultural Development (BANDESA) should exercise closer supervision over its accounting department to ensure unusual and non-recurring type transactions are recorded on a timely basis.
9. The National Bank for Agricultural Development (BANDESA) should ensure that all social cost payments are authorized by the General Directorate for Agricultural Services' (DIGESA's) coordinator prior to disbursement. Authorizations should be obtained in writing.

COMPLIANCE WITH APPLICABLE LAWS, REGULATIONS, AND AGREEMENT TERMS

1. The National Bank for Agricultural Development (BANDESA), as regards the project's trust fund, should request a waiver from USAID/Guatemala of the requirement for maintenance of separate accounts and accountability for A.I.D. funds.

SMALL FARMER DIVERSIFICATION SYSTEMS PROJECT  
COMPONENT WITH THE NATIONAL BANK FOR AGRICULTURAL DEVELOPMENT  
USAID/GUATEMALA PROJECT No. 520-0255

MANAGEMENT COMMENTS

(Free Translation)

Observations to the audit report of The Small Farmer Diversification Systems Project, component with the National Bank for Agricultural Development, USAID/Guatemala Project No. 520-0255, performed by the firm Lara & González, CPA.

1. Report on the Financial Statements

1.1 Balance Sheet as of June 30, 1987 (p.3).

We do not agree to adjusting the balance by Q.50,655 which corresponds to vehicles provided to the Bank, for the following reasons:

- a) the articles of incorporation of the trust fund do not mention this asset in any of its clauses; therefore, it is not part of the Equity, which is only formed by capital to make loans and social cost payments.
- b) The vehicles were provided as logistic support to the Bank; consequently, the Institution recorded these vehicles in its financial statements. This criterion has been endorsed by A.I.D. officials in similar situations in other trust funds.
- c) If A.I.D. considers it necessary to include the value of the vehicles in the trust fund's financial statements, the trust fund articles of incorporation would have to be modified, causing unnecessary transactions.

1.2 Obligations and Trust Fund's Equity (p.3)

- a) The same observations given for 1.1 above apply to: Other Contributions to assets.

2. Notes to the Financial Statements

2.1 D. Questionable Costs (p.8)

We do not agree with the general implication that the internal controls are inadequate, because the Q.16,387 correspond to 11 questionable cases which are not representative of the trust fund's equity. It is also

important to mention that the Institution has effective controls for an adequate management of the portfolio in its regulations.

2.2 E. Trust Fund Agreement (p.8)

The last paragraph in this note expresses a different idea from what was stipulated in the agreement. Therefore, we suggest a different wording as follows: "Invest the funds not placed, because of lack of request for loans, in savings accounts or in stocks or bonds, except Government bonds."

3. Report on the Financial Statement Observations

3.1 The Financial Information Was not Reconciled (p.10)

According to the explanations given during the exit conference at USAID/Guatemala, these conditions refer to the project in general and not to the trust fund managed by the Bank; consequently, they can not be attributed to this Institution.

3.2 The funds were commingled at the Government of Guatemala level and they were not provided to the project as a reimbursement from A.I.D. (p.11). These observations correspond to the Ministry of Public Finance and not to the Bank.

4. List of Report Recommendations

4.1 Financial Statements, Number 1: (p.28)

Recommendation 1.A cannot be implemented, because the Coordinating Unit of the agricultural program (UCPRODA) no longer exists.

For recommendation 1.C, we make the same observations as described in 1.2 above (p.28), this recommendation (2, page 28) corresponds to the Ministry of Public Finance.

General Observations

It could be observed that in some parts the report refers to the project in general and in other parts specifically to the trust fund managed by the Bank. From this situation, it is inferred that many recommendations and observations are addressed to the project and not to the trust fund; therefore is necessary to state that this Institution is only accountable for the management of the aforementioned trust fund.

132

# BANCO NACIONAL DE DESARROLLO AGRICOLA

9a. CALLE No. 9-47, ZONA 1  
GUATEMALA, GUATEMALA, C. A.

## SUB-GERENCIA GENERAL

DIRECCION CABLEGRAFICA  
BANDESA

No. ASG-227-89  
Ref.: .....

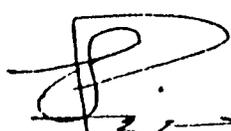
10 de julio de 1989

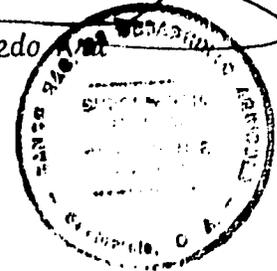
Señores  
Lara & González  
7a. Avenida 7-11 Zona 9  
Edificio Seguros Casa, 4o. Nivel  
Ciudad de Guatemala

Señores:

De acuerdo a lo conversado en la reunión del día 5 de julio de 1989, donde se discutió el informe de la Auditoría del Proyecto de Sistemas de Diversificación para el pequeño agricultor, me permito remitirle nuestras observaciones sobre el referido informe.

Atentamente,

  
Lic. Oscar Leonel Figueredo  
Subgerente General



c.c. Brian Rudert (oficina de Desarrollo Rural)  
Gerencia General  
Subgerencia de Crédito  
Subgerencia Bancaria  
Archivo

~~PRBA/ee.~~

117

OBSERVACIONES AL INFORME DE LA AUDITORIA DEL PROYECTO DE SISTEMAS DE DIVERSIFICACION PARA EL PEQUEÑO AGRICULTOR, COMPONENTE CON EL BANCO NACIONAL DE DESARROLLO AGRICOLA, USAID/GUATEMALA PROYECTO No. 520-0255, REALIZADA POR LA EMPRESA LARA & GONZALEZ.

1. INFORME SOBRE LOS ESTADOS FINANCIEROS

1.1. Balance General al 30 de junio de 1987 (Página 12)

No se está de acuerdo que el balance se ajuste en la cantidad de Q.50,655, correspondiente a los vehículos que fueron entregados al Banco, por las siguientes razones:

- a) La escritura constitutiva del Fideicomiso, en ninguna cláusula hace mención de este activo, por lo tanto no forma parte del Patrimonio, el cual unicamente está constituido por capital para conceder préstamos y pagos sociales.
- b) Los vehículos se entregaron como un apoyo logístico al Banco, por lo que la Institución los registra en sus propios estados financieros, criterio que ha sido avalado por funcionarios de AID., en situaciones similares de otros fideicomisos.
- c) De considerar AID que es necesario que se incluya el valor de los vehículos en los estados financieros del Fideicomiso, implicaría que se modifique la Escritura Constitutiva del Fideicomiso, lo cual provocaría trámites innecesarios.

1.2 Obligaciones y Patrimonio del Fideicomiso (Página 13)

- a) Las mismas observaciones descritas en el punto anterior, para el rubro. Otros aportes en bienes.

2. NOTAS A LOS ESTADOS FINANCIEROS

2.1 D. Costos Cuestionables (Página 18)

No estamos de acuerdo que se indique en forma general que los controles internos son inadecuados, en virtud de que los Q.16,387 corresponden a 11 casos cuestionables, lo cual no es representativo en relación con el capital fideicomitado; asimismo es importante mencionar que la Institución si cuenta con controles efectivos contenidos en manuales de normas y procedimientos, para una adecuada administración de la cartera.

/.....

2.2 E. Convenio del Fideicomiso (Página 19)

La redacción del último párrafo de esta página da una idea distinta a lo pactado contractualmente, por lo que se sugiere la siguiente redacción: "Invertir los fondos que no puedan ser colocados por falta de demandantes de crédito, en cuentas de ahorro o en valores de primer orden, excepto en valores del estado".

3. INFORME SOBRE LOS ESTADOS FINANCIEROS, OBSERVACIONES

3.1 La Información Financiera no fue conciliada: (Página 21)

De acuerdo a las explicaciones que se tuvieron cuando se discutió este informe en AID/Guatemala, estas condiciones se refieren al Proyecto en general y no al Fideicomiso administrado por el Banco, en consecuencia no son imputables a esta Institución.

3.2 Los fondos fueron mezclados a nivel del Gobierno de Guatemala y no se proporcionaron al Proyecto como reembolso de AID. (Página 22)

Estas observaciones no son imputables al Banco, sino corresponden al Ministerio de Finanzas Públicas.

4. LISTA DE RECOMENDACIONES DEL INFORME

4.1 Estados Financieros

Numeral 1: (Página 43)

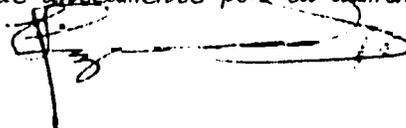
La recomendación A no es atendible, en virtud que la Unidad Coordinadora del Programa de Agricultura (UCPRODA) ya no existe.

Para la recomendación de la Literal C, se hacen las mismas observaciones descritas en el punto 1.1 numeral 2: (Página 43)

Esta recomendación corresponde al Ministerio de Finanzas Públicas.

5. OBSERVACIONES GENERALES

Se pudo comprobar que el referido informe, en algunas partes se refiere al proyecto en general y en otras es específico para el Fideicomiso administrado por el Banco, derivado de esta situación muchas observaciones y recomendaciones, corresponden al proyecto y no al Fideicomiso, por lo que es necesario hacer la salvedad que esta Institución responde únicamente por la administración del mencionado Fideicomiso.



APPENDIX 1

REPORT DISTRIBUTION

	<u>No. of Copies</u>
Director, USAID/Guatemala	5
AA/LAC	2
LAC/CAP/G	1
AA/M	2
GC	1
LAC/CONT	1
LAC/DP	1
LAC/DR	1
LAC/GC	1
AA/XA	2
LEG	1
M/FM/ASD	2
XA/PR	1
PPC/CDIE	3
IG	1
AIG/A	1
IG/PPO	2
IG/LC	1
IG/ADM/C&R	12
IG/I	1
RIG/I/T	1
Other RIG/As	1