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UNITED STATES
AGENCY FOR INTERNATIONAL DEVELOPMENT

THE
INSPECTOR
GENERAL



Regional Inspector General for Audit

TEGUCIGALPA

PD-NBC-018

ISA 68801

LIMITED PRE-AWARD
SURVEY OF THE CREDIT COMPONENT OF
THE EARTHQUAKE RECONSTRUCTION PROJECT
WITH BANCO NACIONAL DE FOMENTO INDUSTRIAL
USAID/EL SALVADOR PROJECT NO. 519-0333

Audit Report No. 1-519-89-15-N
January 9, 1989

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

AGENCY FOR INTERNATIONAL DEVELOPMENT

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

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

January 9, 1989

MEMORANDUM

TO : D/USAID/El Salvador, Henry H. Bassford
FROM : RIG/A/T, *Leino N. Gothard*
Coinage N. Gothard, Jr.
SUBJECT: Audit Report No. 1-519-89-15-N, "Limited Pre-award Survey of the Credit Component of the Earthquake Reconstruction Project with Banco Nacional de Fomento Industrial in El Salvador"

This report presents the results of a non-Federal limited pre-award survey requested by your Mission of the Credit Component of the Earthquake Reconstruction Project, USAID/El Salvador Project No. 519-0333, with Banco Nacional de Fomento Industrial (BANAFI) in El Salvador. The certified public accounting firm of Price Waterhouse in El Salvador prepared the report, which is dated December 12, 1988.

The purpose of this limited pre-award survey was to determine whether:
(1) BANAFI's accounting system contains sufficient capacity to accurately capture accounting data under the project and the internal accounting and administrative controls are adequate for USAID/El Salvador purposes, and
(2) BANAFI has the financial capability and administrative capacity for performing the proposed work.

In the opinion of Price Waterhouse, BANAFI's accounting system and internal controls are sufficient for recording, identifying and controlling data and operations related to the project. Also the auditors deemed that BANAFI appeared to have sufficient financial and management capability for undertaking the project.

The Price Waterhouse report contains 2 recommendations concerning BANAFI's management capability and its accounting system and internal controls. We believe the findings and recommendations have merit and should be implemented as follows:

Recommendation No. 1

We recommend that USAID/El Salvador require Banco Nacional de Fomento Industrial (BANAFI) to implement, as soon as possible, the 2 recommendations concerning its management capability and its accounting

system and internal controls contained in the Price Waterhouse report dated December 12, 1988.

This report is advisory only, since it is our policy not to include pre-award survey recommendations in the Office of the Inspector General's audit recommendation follow-up system unless the recommendations involve potential savings or cost avoidance.

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LIMITED PRE-AWARD SURVEY OF THE CREDIT COMPONENT
OF THE EARTHQUAKE RECONSTRUCTION PROJECT
WITH BANCO NACIONAL DE FOMENTO INDUSTRIAL
USAID/EL SALVADOR PROJECT NO. 519-0333

* * *

DECEMBER 12, 1988

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LIMITED PRE-AWARD SURVEY OF THE CREDIT COMPONENT
OF THE EARTHQUAKE RECONSTRUCTION PROJECT
WITH BANCO NACIONAL DE FOMENTO INDUSTRIAL
USAID/EL SALVADOR PROJECT NO. 519-0333

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Price Waterhouse



December 12, 1988

Mr. Coinage N. Gothard
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 limited pre-award survey of the credit component of the Earthquake Reconstruction Project assigned to Banco Nacional de Fomento Industrial (BANAFI), USAID/El Salvador Project No. 519-0333.

BACKGROUND

BANAFI was created by Law Decree 930 of December 22, 1981 to promote the development of industrial activities by providing financing and banking services to qualified industrial concerns. BANAFI is controlled by an assembly of governors, consisting of the ministers of Economy, Planning, Finance, External Trade and Agriculture, and the president of the Banco Central de Reserva (BCR). Management authority for the entity has been delegated to the directorate, which is comprised of a president, vice president and a deputy.

The Earthquake Reconstruction Project, USAID/El Salvador Project No. 519-0333, will provide \$75 million over a 36 month period through September 30, 1990 to assist El Salvador to restore the standard of living for Salvadorans affected by the October 10, 1986 earthquake. The project will immediately follow the \$50 million Earthquake Recovery Program, USAID/El Salvador Project No. 519-0331 and will strive to provide a long-term solution to the destruction caused by the earthquake. The initial project provided immediate and intermediate solutions over an approximate one year period.

The project purpose is to assist the Government of El Salvador and the private sector to repair and reconstruct homes, businesses, basic services, and infrastructure in metropolitan zones most seriously affected by the earthquake. The project includes two major components: credit and non-credit activities.

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The credit component's aim is to provide housing loans for repair and reconstruction of individual houses; reconstruction and rehabilitation of hostelryes for rental housing; and construction of new, low cost, condominium type apartments to replace hostelryes. The credit component's aim is to also provide business credit for private health services, private schools, and small business establishments.

The non-credit component will provide direct financing for construction of public schools, repair of municipal markets, highways reconstruction, repair of the ANDA water system, repair and reconstruction of health facilities, and development of relocation sites for families. Also, Private Voluntary Organizations (PVO) activities will be directly funded by USAID/El Salvador to provide housing assistance to low income families affected by the earthquake who have not been able to marshall the resources necessary to repair or replace their shelters.

The credit activities component includes housing credit and business credit. The housing credit will be administered by way of discount credit lines with the Central Bank of Reserve (Banco Central de Reserva - BCR), which will provide local currency to the National Housing Financier (Financiera Nacional de la Vivienda - FNV), which will in-turn provide funding to seven savings and loan associations in El Salvador, as needed, to provide loans for housing repair and reconstruction activities. The seven savings and loan associations involved are:

- (1) Crece, S. A.
- (2) APRISA, S. A. (Ahorro, Préstamos, Inversiones, S. A.)
- (3) Atlacatl, S. A.
- (4) AHORROMET (Ahorros Metropolitanos, S. A.)
- (5) CASA (Construcción y Ahorro, S. A.)
- (6) CREDISA (Crédito Inmobiliario, S. A.)
- (7) La Central de Ahorros, S. A.

The business credit will be administered as a rediscount credit line by the Central Bank of Reserve (BCR) to nine commercial banks, Banco Hipotecario - a private mortgage bank, Fondo de Financiamiento y Garantía para la Pequeña Empresa (FIGAPE) - a GOES financial institution, and Banco Nacional de Fomento Industrial (BANAFI) - a GOES bank. The nine commercial banks involved are:

- (1) Banco Agrícola Comercial
- (2) Banco Capitalizador
- (3) Banco de Comercio
- (4) Banco de Crédito Popular
- (5) Banco Cuscatlán
- (6) Banco de Desarrollo e Inversión
- (7) Banco Financiero

- (8) Banco Mercantil
- (9) Banco Salvadoreño

AUDIT OBJECTIVES AND SCOPE

The specific objectives of our limited pre-award survey were to determine whether:

1. BANAFI's accounting system contains sufficient capacity to accurately capture accounting data under the project and the internal accounting and administrative controls are adequate for USAID/El Salvador purposes, and
2. BANAFI has financial and administrative capability for performing the proposed work.

The survey was performed in accordance with generally accepted auditing standards and with the U.S. Comptroller General's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision) and accordingly included such tests as considered necessary in the circumstances.

The scope of our work consisted of:

1. Reviewing BANAFI's accounting system. This review included the evaluation of:
 - a. Internal accounting controls.
 - b. Policies for the management of funds and loans.
 - c. Procedures to request project funding, promote and receive credit applications, approve and disburse credits, and prepare periodic reports on credit lines.
2. Evaluating BANAFI's financial and administrative capability for performing the proposed work. This task included:
 - a. Evaluation of past performance in administering similar credit lines.
 - b. Ascertaining that current assets on hand are sufficient for BANAFI to function until USAID/El Salvador funding is received.

During our work, we were alert to situations or transactions that could be indicative of fraud, abuse and illegal expenditures and acts.

RESULTS OF AUDIT

Financial Capability

BANAFI appears to have sufficient financial capability for undertaking the business credit component of the Earthquake Reconstruction Project No. 519-0333, under the system of fund requests submitted to BCR, which administers the credit line by way of subsequent rediscounts to recover the loans granted.

Management Capability

BANAFI appears to have the management capability for undertaking the business credit component of the Earthquake Reconstruction Project No. 519-0333, except that no specific project budgets and cash flows have been considered in the entity's general plan.

Accounting system and internal accounting controls

BANAFI's accounting system appears to be adequate and its internal controls are deemed to be sufficient for recording, identifying and controlling data and operations related to the Earthquake Reconstruction Project No. 519-0333, except that its chart of accounts does not include specific accounts to control project operations.

MANAGEMENT COMMENTS:

On November 3, 1988, Price Waterhouse delivered the pre-award survey draft report to bank management. The transmittal letter requested management comments not later than November 11, 1988, pointing out that if no comments or response was delivered to Price Waterhouse, it would be understood that such draft report was accepted. At the date of this report the bank had not responded to Price Waterhouse.

Price Waterhouse

* * *

Price Waterhouse



BANCO NACIONAL DE FOMENTO INDUSTRIAL
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON FINANCIAL CAPABILITY

AUDITOR'S OPINION

We have performed a limited pre-award survey of Banco Nacional de Fomento Industrial's (BANAFI) financial capability to manage the credit component of the Earthquake Reconstruction Project, USAID/El Salvador Project No. 519-0333. The survey was performed pursuant to the statement of work for the limited pre-award survey and in accordance with the United States Comptroller General's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision). Our work included, to the extent we considered necessary, a review of audited financial statements as of December 31, 1987, unaudited financial statements as of June 30, 1988 and the operating budget for 1988.

Based on our review, as described in the first paragraph above, we believe that at present BANAFI has the financial capability for undertaking the business credit component of the Earthquake Reconstruction Project No. 519-0333 under the system of fund requests submitted to Banco Central de Reserva (BCR) to cover the approved loans. BCR administers the credit line by way of subsequent rediscounts to recover the loans granted.

This report is intended solely for the use of Banco Nacional de Fomento Industrial (BANAFI) and the United States Agency for International Development. This restriction is not intended to limit distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter of public record.

A handwritten signature in cursive script that reads "Price Waterhouse", located below the text of the report.

August 24, 1988
El Salvador, C. A.

Price Waterhouse



BANCO NACIONAL DE FOMENTO INDUSTRIAL
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT
USAID/EL SALVADOR PROJECT No. 519-0333

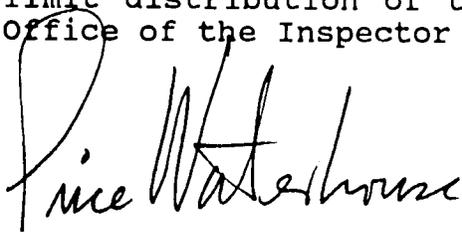
REPORT ON MANAGEMENT CAPABILITY

AUDITOR'S OPINION

We have performed a limited pre-award survey of Banco Nacional de Fomento Industrial's (BANAFI) capability for managing the credit component of the Earthquake Reconstruction Project, USAID/El Salvador Project No. 519-0333. The survey covered those areas we considered relevant to the criteria established by the statement of work for the limited pre-award survey. Our work was performed in accordance with the United States Comptroller General's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision).

Based on our study and understanding of the criteria included in the statement of work mentioned in the preceding paragraph, we believe that at present, Banco Nacional de Fomento Industrial (BANAFI) has the management capability for undertaking the bussiness credit component of the Earthquake Reconstruction Project No. 519-0333, except for finding No. 1 described in the following page.

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August 24, 1988
El Salvador, C. A.

BANCO NACIONAL DE FOMENTO INDUSTRIAL
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON MANAGEMENT CAPABILITY

FINDING

1. Project Related Budgets and Cash Flows Have not Been Prepared

Condition:

BANAFI had not prepared specific budgets and cash flows to execute project related operations and had not considered them in its general operation plans.

Criterion:

BANAFI should include project related budgets and cash flows into its general operation plans.

Cause:

Preparation of project budgets and cash flows or their inclusion in BANAFI's own plans had not been done because project related credit applications had not yet been received.

Effect:

Exclusion of project credit lines from plans and budgets could limit promotion of the project and result in lost opportunities for potential users.

Recommendation:

USAID/El Salvador should require BANAFI to prepare, approve and include project operations in its plans, budgets, and cash flows, in order to adequately promote project related benefits.

Price Waterhouse



BANCO NACIONAL DE FOMENTO INDUSTRIAL
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON THE ACCOUNTING SYSTEM AND INTERNAL ACCOUNTING CONTROLS

AUDITOR'S OPINION

We have performed a study and evaluation of the internal accounting and administrative control systems of Banco Nacional de Fomento Industrial (BANAFI) in connection with the limited pre-award survey of the credit component of the Earthquake Reconstruction Project, USAID/El Salvador Project No. 519-0333. The purpose of our study and evaluation was to determine the adequacy of the control systems to record transactions under the agreement. Our study and evaluation was performed in accordance with the United States Comptroller General's "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision) and pursuant to the criteria set forth in the statement of work for the limited pre-award survey. Our work was limited to an evaluation of the key controls over the procedures used to request project funding, promote and receive credit applications, approve and disburse credits, prepare periodic reports on credit lines and the record-keeping of such transactions.

The management of BANAFI is responsible for establishing and maintaining adequate internal control systems in areas of significance to the program covered by the above mentioned agreement. In fulfilling that responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of internal control systems are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against waste, loss, and misuse; that resources are properly used and in compliance with established policies and procedures and applicable laws and regulations; and that reliable data are obtained, maintained, and fairly disclosed in management reports.

Because of inherent limitations in any system of internal accounting and administrative controls, errors or irregularities may occur and not be detected. Also, projection of any evaluation of the systems 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.

Price Waterhouse



BANCO NACIONAL DE FOMENTO INDUSTRIAL
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON ACCOUNTING SYSTEM AND THE INTERNAL ACCOUNTING CONTROLS

AUDITOR'S OPINION

Based on our study and the criteria referred to in the first paragraph of this report, we believe that at present, the accounting system of Banco Nacional de Fomento Industrial appears to be adequate and its internal controls are deemed to be sufficient for recording identifying and controlling data and operations related to the business credit component of the Earthquake Reconstruction Project No. 519-0333, except for finding No. 1 described in the following page.

This report is intended solely for the use of Banco Nacional de Fomento Industrial (BANAFI) and the United States Agency for International Development. This restriction is not intended to limit distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter of public record.

Price Waterhouse

August 24, 1988
El Salvador, C. A.

BANCO NACIONAL DE FOMENTO INDUSTRIAL
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON THE ACCOUNTING SYSTEM AND INTERNAL ACCOUNTING CONTROLS

FINDINGS

1. The Chart of Accounts of BANAFI Did not Include Project Credit Line General Ledger Accounts and Subsidiary Accounts to Record and Control Project Operations

Condition:

BANAFI had not defined, approved and included in its chart of accounts specific general ledger accounts and subsidiary accounts to record, identify and control the subcomponents and beneficiaries of the business credit component of Project No. 519-0333.

Criterion:

According to Section B.5 (b) of Annex II to the agreement, the fund administrators should establish adequate accounting records to control separately specific project operations.

Cause:

The above mentioned specific general ledger accounts and subsidiary accounts had not been defined because project operations had not yet begun.

Effect:

Lack of specific accounts to identify project related operations could result in inadequate recording of project operations and unreliable financial data.

Recommendation:

USAID/El Salvador should require BANAFI to define and approve specific general ledger accounts and subsidiary accounts to identify, record and control project operations by subcomponent and credit beneficiaries.

BANCO NACIONAL DE FOMENTO INDUSTRIAL
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT
USAID/EL SALVADOR PROJECT No. 519-0333

LIST OF REPORT RECOMMENDATIONS

Management Capability

Recommendation 1:

USAID/El Salvador should require BANAFI to prepare, approve and include project operations in its plans, budgets, and cash flows, in order to adequately promote project related benefits.

Accounting System and Internal Accounting Controls

Recommendation 1:

USAID/El Salvador should require BANAFI to define and approve specific general ledger accounts and subsidiary accounts to identify, record and control project operations by subcomponent and credit beneficiaries.

APPENDIX 1

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