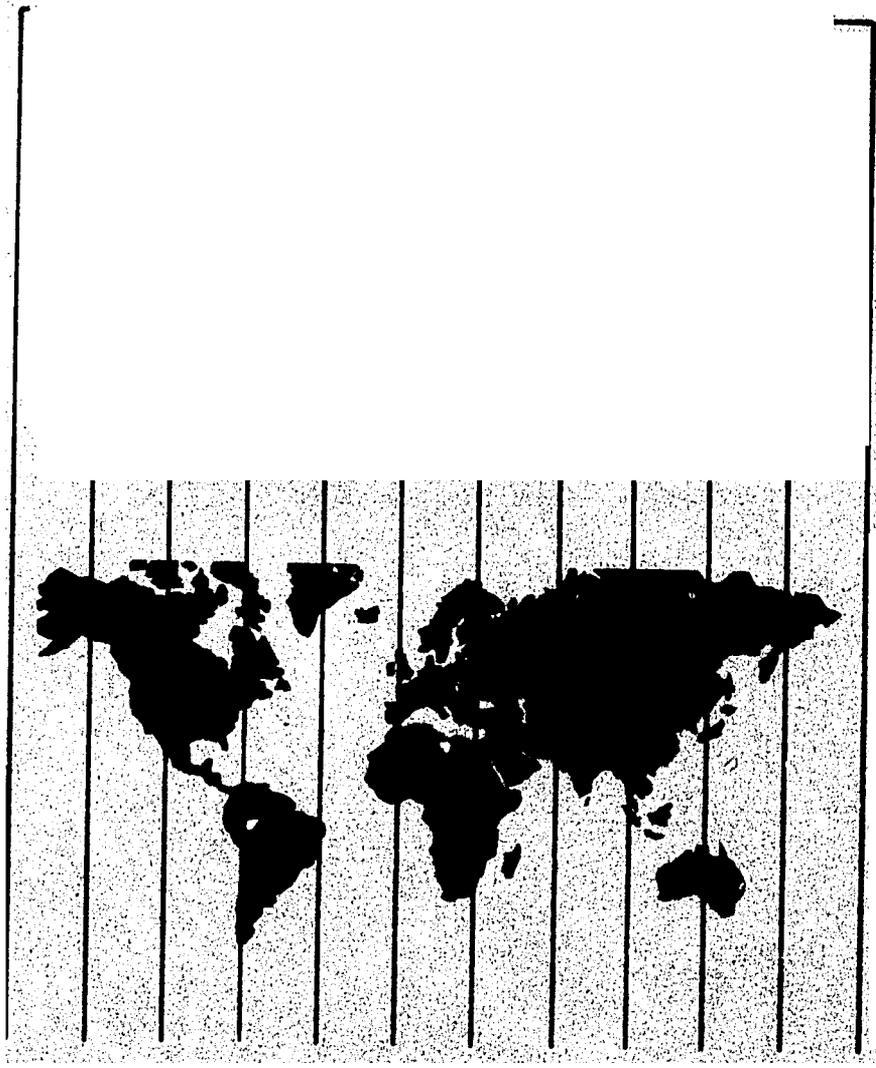


FD-ABC-09

UNITED STATES  
AGENCY FOR INTERNATIONAL DEVELOPMENT

THE  
INSPECTOR  
GENERAL



Regional Inspector General for Audit  
TEGUCIGALPA

PD-APG-019

ISN 62902

LIMITED PRE-AWARD  
SURVEY OF THE CREDIT COMPONENT OF  
THE EARTHQUAKE RECONSTRUCTION PROJECT  
WITH BANCO CAPITALIZADOR, S.A.  
USAID/EL SALVADOR PROJECT NO. 519-0333

Audit Report No. 1-519-89-16-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, *Conrad N. Gothard*  
Conrad N. Gothard, Jr.  
SUBJECT: Audit Report No. 1-519-89-16-N, "Limited Pre-award Survey of the Credit Component of the Earthquake Reconstruction Project with Banco Capitalizador, S.A. 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 Capitalizador, S.A. 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) Banco Capitalizador, S.A.'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) Banco Capitalizador, S.A. has the financial capability and administrative capacity for performing the proposed work.

In the opinion of Price Waterhouse, Banco Capitalizador, S.A.'s accounting system and internal controls are sufficient to record and control the project's operations, and its financial capability is sufficient for undertaking the project. However, it is Price Waterhouse's opinion that Banco Capitalizador, S.A. lacks the management capability for undertaking the project due to a number of deficiencies.

The Price Waterhouse report contains 6 recommendations concerning Banco Capitalizador, S.A.'s management capability and its accounting system and internal controls. We believe that the findings are significant and should be implemented as follows:

Recommendation No. 1

We recommend that USAID/El Salvador require Banco Capitalizador, S.A. to implement, as soon as possible, the 6 recommendations concerning its

b.

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.

LIMITED PRE-AWARD SURVEY OF THE CREDIT COMPONENT  
OF THE EARTHQUAKE RECONSTRUCTION PROJECT  
WITH BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
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 CAPITALIZADOR, SOCIEDAD ANONIMA  
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 Capitalizador, Sociedad Anonima (Banco Capitalizador, S. A.), USAID/El Salvador Project No. 519-0333.

### BACKGROUND

Banco Capitalizador, S. A. is a financial institution organized on May 9, 1956 to receive savings deposits and issue securities for compound interest on savings. Management rests with the Board of Directors which delegates direct management, general supervision and coordination of the bank's activities as well as legal representation to its president.

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 hostelrys for rental housing; and construction of new, low cost, condominium type apartments to replace hostelrys. 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 marshal 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. Banco Capitalizador, S. A.'s accounting system contains sufficient capacity to accurately capture accounting data under the program and its internal accounting and administrative controls are adequate for USAID/ES purposes, and
2. Banco Capitalizador, S. A. 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 Banco Capitalizador, S. A.'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 Banco Capitalizador, S. A.'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 Banco Capitalizador, S. A. to function until USAID/ES 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

Banco Capitalizador, S. A. 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 Banco Central de Reserva (BCR), which administers the credit line by way of rediscounts to recover the credits granted.

### Management Capability

Banco Capitalizador, S. A. appears to lack the management capability for undertaking the business credit component of the Earthquake Reconstruction Project No. 519-0333, because of the following:

- Project related budgets, cash flows and plans of action had not been prepared;
- There were no written, formally approved procedures applicable to loans;
- Instructions for loan management had not been adequately communicated and;
- There were insufficient human resources to properly execute project operations in the loan and accounting departments.

### Accounting System and Internal Accounting Controls

Banco Capitalizador, S. A. appears to have an adequate accounting system and sufficient internal controls to record and control the Project's general operations, except that:

- The chart of accounts did not include specific accounts to record and control project operations;
- There was no established review program of the operations and accounting records of the Project.

### 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 CAPITALIZADOR, SOCIEDAD ANONIMA  
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 Capitalizador, Sociedad Anonima's (Banco Capitalizador, S. A.) 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, Banco Capitalizador, S. A. 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 Capitalizador, Sociedad Anonima (Banco Capitalizador, S. A.) 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 12, 1988  
El Salvador, C. A.

*Price Waterhouse*



BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
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 Capitalizador, Sociedad Anonima's (Banco Capitalizador, S. A.) 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 Capitalizador, S. A. appears to lack the management capability for undertaking the business credit component of the Earthquake Reconstruction Project No. 519-0333, as shown by findings 1 to 4 described in the following pages.

This report is intended solely for the use of Banco Capitalizador, Sociedad Anonima (Banco Capitalizador, S. A.) 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 21, 1988  
El Salvador, C. A.

BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT  
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON MANAGEMENT CAPABILITY

FINDINGS

1. Project Related Budgets and Cash Flows Had Not Been Prepared.

Condition:

Banco Capitalizador, S. A. had not prepared specific budgets and cash flows to execute project related operations and had not considered them in its general operation plans.

Criterion:

Banco Capitalizador, S. A. should include project related budgets and cash flows in its general operation plans.

Cause:

Preparation of project budgets and cash flows or their inclusion in Banco Capitalizador'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 Banco Capitalizador, S. A. to prepare, approve and include project operations in its plans, budgets, and cash flows, in order to adequately promote project related benefits.

2. There Were no Written, Formally Approved Administrative Loan Procedures.

Condition:

Banco Capitalizador, S. A. lacks formal approved organization manuals (organization charts, position descriptions), general administrative procedures for the credit area, information and control systems for the BCR and ABANSA, or a filing system for its documentation. Banco Capitalizador also has not prepared

BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT  
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON MANAGEMENT CAPABILITY

FINDINGS

Plans of Action covering the Earthquake Reconstruction Project's related activities.

Criterion:

Banco Capitalizador, S. A. should have the administrative tools mentioned above, which should be approved and communicated to all corresponding internal levels.

Cause:

Present Banco Capitalizador, S. A. management is new and has not had time to remedy the deficiencies prevailing in the past.

Effect:

Lack of formal approved administrative procedures could have a negative effect on the activities and transactions of the project.

Recommendation:

Banco Capitalizador, S. A. management should prepare formal written administrative manuals and procedures for its own general and project activities.

3. The Project's Standards and Regulations Have Not Been Adequately Communicated

Condition:

The standards and regulations governing Project No. 519-0333 had not been distributed to the loan and other departments concerned with project execution.

Criterion:

All departments concerned with loan management and control should be fully aware of the regulations governing Project No., 519-0333 for adequate application of eligibility criteria.

BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT  
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON MANAGEMENT CAPABILITY

FINDINGS

Cause:

Due to the lack of demand for project loans, the entity had not considered it necessary to communicate the project's standards and regulations to its involved departments.

Effect:

Lack of full awareness of the above mentioned standards and regulations could result in noncompliance with agreement terms, lack of adherence to eligibility criteria, recording errors and submission of inaccurate data to the BCR.

Recommendation:

Banco Capitalizador, S. A. should communicate the project's standards and regulations to its loan and other departments concerned with project execution.

4. Insufficient Human Resources to Properly Execute the Project.

Condition:

The bank did not have sufficient human resources in the loan and accounting departments to properly execute project activities.

Criterion:

The bank should have sufficient human resources to execute both its normal operations and those of the project.

Cause:

The bank had not decided its degree of participation in the project and, therefore, the number of personnel required had not been considered. However, the loan department staffing was under study by the institution.

Effect:

Lack of sufficient human resources to undertake project activities and continue the bank's normal operations could lead to work overload of the personnel.

BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT  
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON MANAGEMENT CAPABILITY

FINDINGS

Recommendation:

Prior to execution of Project No. 519-0333, the bank should hire sufficient personnel to properly execute the project without affecting its normal operations.

*Price Waterhouse*



BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
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 Capitalizador, Sociedad Anonima (Banco Capitalizador, S. A.) 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 Banco Capitalizador, Sociedad Anonima (Banco Capitalizador, S. A.) 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 CAPITALIZADOR, SOCIEDAD ANONIMA  
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

Based on our study and the criteria referred to in the first paragraph of this report, we believe that Banco Capitalizador, S. A. has an adequate accounting system and sufficient internal controls to record and control the operations of the business credit component of project No. 519-0333, except for findings 1 to 2 described in the following pages.

This report is intended solely for the use of Banco Capitalizador, Sociedad Anonima (Banco Capitalizador, S. A.) 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 12, 1988  
El Salvador, C. A.

BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
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 Did Not Include Specific Project Credit Line General Ledger Accounts and Subsidiary Accounts to Record and Control Project Operations

Condition:

Banco Capitalizador, S. A. 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 have 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 Banco Capitalizador, S. A. to define and approve specific general ledger accounts and subsidiary accounts to identify, record and control project operations by subcomponent and credit beneficiaries.

BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
CREDIT COMPONENT OF THE EARTHQUAKE RECONSTRUCTION PROJECT  
USAID/EL SALVADOR PROJECT No. 519-0333

REPORT ON THE ACCOUNTING SYSTEM AND INTERNAL ACCOUNTING CONTROLS

FINDINGS

2. The Internal Audit Department Had no Specific Programs to Review and Evaluate the Project Related Operations.

Condition:

The Internal Audit Department of Banco Capitalizador, S. A. had not included in its work plans specific activities to review and evaluate the accounting records and administrative procedures related to the project.

Criterion:

The Internal Audit Department of Banco Capitalizador, S. A. should have specific work plans to review and evaluate project operations and accounting records.

Cause:

At present, the internal audit department is being restructured and the above mentioned work plans have not been established.

Effect:

Excluding specific work plans to monitor and evaluate project operations could lead to inadequate review of project operations.

Recommendation:

The Internal Audit Department of Banco Capitalizador, S. A. should prepare, approve and implement specific work plans to review and evaluate project operations and accounting records.

BANCO CAPITALIZADOR, SOCIEDAD ANONIMA  
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 Banco Capitalizador, S. A. to prepare, approve and include project operations in its plans, budgets, and cash flows, in order to adequately promote Project related benefits.

Recommendation 2:

Banco Capitalizador, S. A. management should prepare formal written administrative manuals and procedures for its own general and project activities.

Recommendation 3:

Banco Capitalizador, S. A. should communicate the project's standards and regulations to its loan and other departments concerned with project execution.

Recommendation 4:

Prior to execution of Project No. 519-0333, the bank should hire sufficient personnel to properly execute the project without affecting its normal operations.

The Accounting System and Internal Accounting Controls

Recommendation 1:

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

Recommendation 2:

The Internal Audit Department of Banco Capitalizador, S. A. should prepare, approve and implement specific work plans to review and evaluate project operations and accounting records.

APPENDIX 1

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