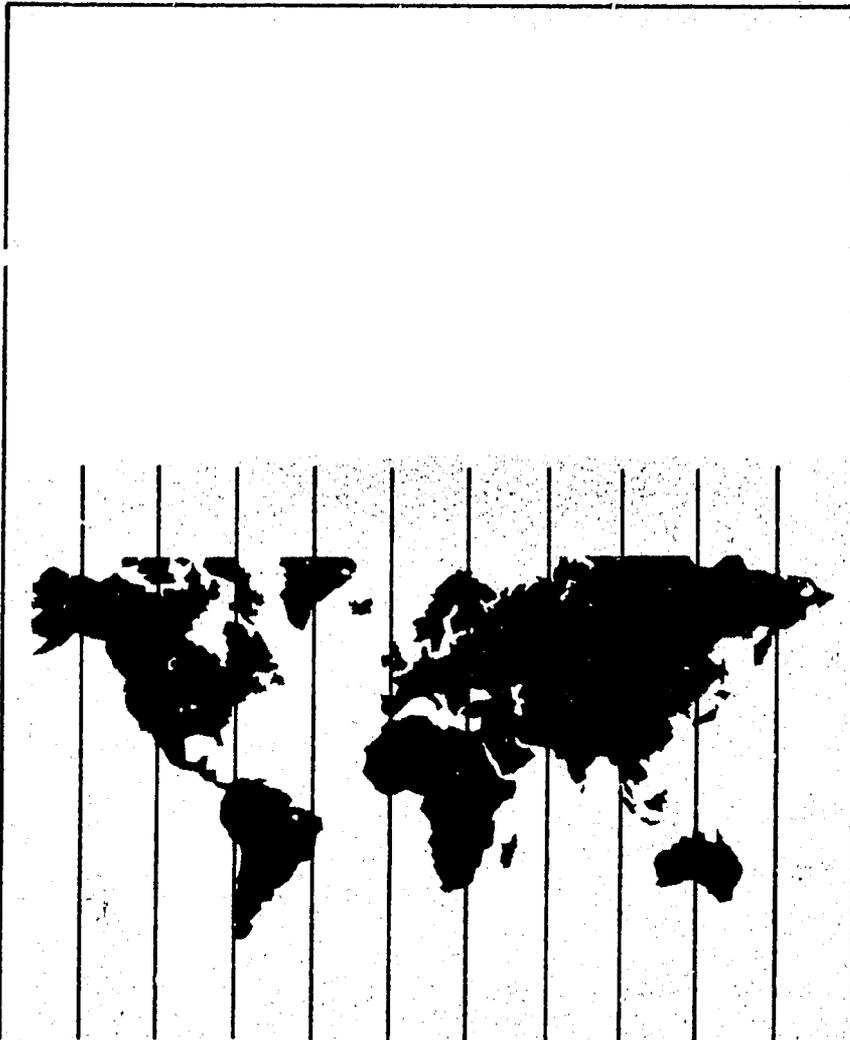


PD-ABD-054

UNITED STATES
AGENCY FOR INTERNATIONAL DEVELOPMENT

THE
INSPECTOR
GENERAL



Regional Inspector General for Audit

TEGUCIGALPA

**AUDIT OF ROCAP'S
PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES
OF CENTRAL AMERICA AND PANAMA
FEBRUARY 27, 1989 TO JUNE 30, 1990**

**AUDIT REPORT NO. 1-596-91-41-N
JULY 31, 1991**

AGENCY FOR INTERNATIONAL DEVELOPMENT

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AMERICAN EMBASSY
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July 31, 1991

MEMORANDUM

TO: D/ROCAP, Irene Castillo

FROM: RIG/A/T, Reginald Howard 

SUBJECT: Audit of ROCAP's Private Sector Initiatives Project, Managed by the Federation of Private Entities of Central America and Panama, February 27, 1989 to June 30, 1990

This report presents the results of a non-Federal financial audit of the Private Sector Initiatives Project, managed by the Federation of Private Entities of Central America and Panama (Federation), ROCAP Project No. 596-0149, for the period February 27, 1989 to June 30, 1990. The accounting firm of Deloitte Ross Tohmatsu prepared the report, which is dated June 30, 1991.

The purpose of the Private Sector Initiatives Project is to strengthen the capacity of the private sector of Central America and Panama. To attain this purpose the Federation furnishes technical assistance and training to its members and to other public and private organizations related to or associated with the development of the private sector. The audit coverage included A.I.D. funds totaling \$636,747 provided to the Federation for the Project.

The objectives of the audit were to determine whether: (1) the Federation's fund accountability statement for the period audited fairly presents Project receipts and disbursements, (2) the internal control structure of the Federation was adequate to manage Project operations, and (3) the Federation complied with agreement terms and applicable laws and regulations. The scope of the audit included an examination of the Federation's activities and transactions to the extent considered necessary to issue a report thereon for the period under audit.

The auditors found that, except for (1) not being able to review the Federation's bank reconciliations and the effects of an adjustment, if any, as might have resulted from this review; (2) the unreconciled difference of \$30,034 between the fund statement and the records of ROCAP; (3) the nonreporting of Project disbursements totaling \$11,606; (4) the misrecording of payments totaling

\$3,616; and (5) the incorrect monetary conversion method used by the Federation, the fund accountability statement fairly presents, in all material respects, the Project receipts and disbursements for activities managed by the Federation for the audit period.

The audit identified six material weaknesses in the Federation's internal control structure. Improvements in controls were needed in cash management, accounting and safeguarding of assets, documentation filing procedures, the reconciliation process, supervision over accounting records, and the monetary conversion method used for reporting purposes. With respect to compliance with agreement terms and applicable laws and regulations, the auditors found that the Federation complied in all material respects except it had not complied with Costa Rica's income tax and social security laws concerning its employees' withholdings and payments.

The report was discussed with the management of the Federation who expressed general agreement with the audit report.

We are including the following recommendations in the Office of the Inspector General's recommendation follow-up system:

Recommendation No. 1

We recommend that ROCAP, in conjunction with the Federation, develop an action plan with implementation timetable which will enable the Federation to improve its cash management system, accounting and safeguarding of assets, documentation filing procedures, supervision over accounting records, and method of reporting monetary conversions as identified in the Deloitte Ross Tohmatsu audit report dated June 30, 1991.

Recommendation No. 2

We recommend that ROCAP require the Federation to provide periodic reconciliations of its accounting records to the funds disbursed by ROCAP for the Project.

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

Deloitte Ross Tohmatsu



Apartado Postal 3667-1000
San José, Costa Rica
Teléfono: (506) 53-2466
Facsímil: (506) 53-1841

June 30, 1991

Mr. Reginald Howard
Regional Inspector General for Audit
U.S. Agency for International Development
Tegucigalpa, Honduras, C.A.

Dear Sir:

This report presents the results of our audit of the Private Sector Initiatives Project, ROCAP/Guatemala Project No. 596-0149, managed by the Federation of Private Entities of Central America and Panama (Federación de Entidades Privadas de Centro América y Panamá - FEDEPRICAP), for the period from February 27, 1989 to June 30, 1990.

BACKGROUND

The Federation of Private Entities of Central America and Panama (FEDEPRICAP), registered in the Republic of Panama, was founded on January 31, 1987, as an autonomous association of unions and associations of the private sector of Central America and Panama, its principal purpose was to promote, develop and increase the system of private enterprises, and promote the development of the potential resources for the economic and social development of the country members.

On February 27, 1989 FEDEPRICAP signed an agreement with the Agency for International Development of the United States of America, through the Regional Office of Projects for Central America and Panama Mission to Guatemala (ROCAP/Guatemala), to develop the Private Sector Initiatives Project, ROCAP/Guatemala Project No. 596-0149. The choice of FEDEPRICAP as the Project's manager was due to the similarity of its founding goals and those of the project, as may be seen below.

The total obligated amount by the ROCAP/Guatemala for the project is US\$680,000. Additionally, FEDEPRICAP has to contribute to the project as counterpart funds US\$196,600. The Agreement has been modified by three amendments, which added US\$80,000 to the original budget and modified the original internal budgetary

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structure. The project assistance completion date is August 27, 1992.

The budget breakdown by category is as follows:

Component	<u>ROCAP's Funds</u>	<u>FEDEPRICAP's Funds</u>
Personnel/FEDEPRICAP	US\$ 227,344	US\$ 82,455
Support services	89,600	4,200
Operating expenses	197,000	105,102
Training	166,056	
Auditing		4,843
Contingencies		
Total	US\$ 680,000	US\$ 196,600

Additionally, project paper amendments provide US\$600,000 for technical assistance provided by experts from CARANA Corporation in different fields according to the Project's goals and US\$300,000 for the contracting of a Private Sector Officer, who will be the coordinator of all the activities of ROCAP/Guatemala related to the project. These funds are not handled by FEDEPRICAP.

The fundamental goal of the Private Sector Initiatives Project is to strengthen the capacity of the private sector of Central America and Panama, so as to influence the direction of the socio-economic development and foster the knowledge and participation of the private sector in the development process. To attain this objective, FEDEPRICAP furnishes the technical assistance and training to its members and to other public and private organizations related or associated with this development.

The agreement considers six operating areas to develop the project, as follows: a) development of female leadership skills; b) fostering of the communication and training of authorities and entrepreneurs concerning drug trafficking so that this problem does not affect the regional licit trade; c) development of financial instruments for capital mobilization, promotion of stock markets in the region and creation of an information system for investors and other related activities; d) establishment of an economic block to develop international trade with other economic sectors of the world; e) improvement of the port and highway systems of the region as a part of the goals of the area to develop international commerce; and f) implementation of the information system of the different associations affiliated to FEDEPRICAP in the region.

AUDIT OBJECTIVES AND SCOPE

The general objective was to perform a financial audit of the Private Sector Initiatives Project, ROCAP/Guatemala Project No.

596-0149, managed by the Federation of Private Entities of Central America and Panama (FEDEPRICAP), for the period February 27, 1989 to June 30, 1990. We conducted our audit in accordance with generally accepted auditing standards and "Government Auditing Standards" (1988 Revision), issued by the Comptroller General of the United States and consequently included the tests of the accounting records and the other auditing procedures as we considered necessary under the circumstances. Our examination was made to determine whether:

- A. The fund accountability statement from February 27, 1989 to June 30, 1990, presents fairly, in all material respects, the financial activities of the Project during this period and that the costs incurred and financed by ROCAP/Guatemala are legitimate, fairly presented and reasonable in accordance with the terms of the agreement and the applicable laws and regulations.
- B. The internal control structure of FEDEPRICAP is adequate to manage the project operations.
- C. FEDEPRICAP complied with agreement terms and applicable laws and regulations which might affect the project goals and costs incurred.

We have been alert to situations or transactions that could be indicative of fraud, abuse and illegal expenditures and acts.

The scope of our work consisted of:

- A. Performance of an audit of the fund accountability statement:
 - a) To determine if the costs incurred in purchases and other disbursements were acceptable in accordance with the agreement.
 - b) To determine if the counterpart funds and other donations were obtained opportunely and in accordance with the agreement with ROCAP/Guatemala.
 - c) To obtain confirmations from ROCAP/Guatemala about the funding provided to FEDEPRICAP and from the legal advisors concerning claims and other contingencies.
 - d) To determine if the reports prepared by FEDEPRICAP for ROCAP/Guatemala were presented opportunely and adequately.
 - e) To determine if the FEDEPRICAP's records were reconciled to the information given by ROCAP/Guatemala related to the funds provided.
 - f) To determine if FEDEPRICAP paid reasonable prices for goods and services purchased with ROCAP/Guatemala funds,

and if FEDEPRICAP used fair and competitive practices to insure the most effective use of the project's funds.

- B. Performance of a study and evaluation of the internal control structure, including controls of funds, procurement systems, accounting and safeguarding of furniture and office equipment, budgets and information and communication systems.
- C. A determination of whether FEDEPRICAP complied with the terms and conditions of the agreement and its amendments and with the respective laws and regulations.

RESULTS OF AUDIT

Fund accountability statement

The results of the audit of the fund accountability statement of the Private Sector Initiatives Project, managed by the Federation of Private Entities of Central America and Panama (FEDEPRICAP), Agreement No 596-0149, ROCAP/Guatemala, showed that, except for the nonexistence of bank reconciliations, the unreconciled difference of US\$5,990 between the records of the Project and those of ROCAP/Guatemala, the items not included in the final reported figures amounting to US\$11,606, the wrong classification of payments made with FEDEPRICAP's funds amounting to US\$3,616, as Rocap's funds, and the incorrect accounting conversion of payments made in Costa Rican colones for reporting purposes, as explained in the corresponding report, the fund accountability statement presents fairly, in all material aspects, the income received and the disbursements made by the Private Sector Initiatives Project, ROCAP/Guatemala Project No. 596-0149, for the period February 27, 1989 to June 30, 1990, in accordance with the accounting basis applied and with the terms of the agreement and the applicable laws and regulations. In addition, there is a contingency for the unfulfillment of certain obligations established by the Income Tax Law and the Social Security Constitutive Law. Finally, except for the above mentioned matters, the costs reported as incurred are allowable, allocable and reasonable per the term of the agreement and AID regulations.

Internal Control Structure

Our study and evaluation of the internal control structure revealed some matters related with its operation which we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants and "Government Auditing Standards" (1988 Revision), issued by the Comptroller General of the United States. Reportable conditions involve matters coming to our attention related to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the

organization's ability to record, process, summarize and report financial data consistent with the assertions of management in the fund accountability statement. These conditions were the following:

1. There are control deficiencies in cash management.
2. The accounting and safeguarding control of office furniture and equipment is deficient.
3. Proper control procedures have not been established for the filing documents.
4. The fund accountability statement and the accounting records of ROCAP/Guatemala are not reconciled.
5. The procedures to supervise the accounting records should be improved.
6. The accounting conversion method of colones to dollars for reporting purposes should be improved.

We believe that the above mentioned conditions are material weaknesses.

As a part of the scope of our work, our study and evaluation of the internal control structure of FEDEPRICAP included the following areas:

- A. Funds Control. The funds control system is deficient, because the project's bank reconciliations are not prepared, the colones bank accounts are under the personal name of the executive director of the Federation who can sign them individually, there are no procedures to revise the checks paid by the bank and no reconciliations have been made between the balances of the check books and those of the accounting records.
- B. Goods and services procurement systems. Our evaluation of the goods and services procurement systems did not disclosed reportable conditions.
- C. Accounting and safeguarding controls of furniture and equipment. Controls on this area were inadequate. The fund accountability statement and those of ROCAP/Guatemala are not reconciled, some accounting supervision procedures are lacking, the accounting conversion method of colones to dollars for reporting purposes is inadequate, there are no procedures for filing documents, the furniture and equipment auxiliary record have not been summarized and it has not been reconciled with the accounting books, the assets acquired with ROCAP's funds and those bought with FEDEPRICAP's can not be differentiated, the auxiliary

record is not updated, and the values in colones and dollars are mixed.

- D. Budgetary controls. Reportable conditions were not found in this category.
- E. Information and communication controls. The system is being installed and neither reportable conditions nor material weaknesses were found in this category.

Compliance with Agreement Terms and Applicable Laws and Regulations.

As part of obtaining reasonable assurance about whether the fund accountability statement is free of material misstatement and in order to form an opinion on compliance with agreement terms and applicable laws and regulations, we performed tests to ensure that FEDEPRICAP complied with the agreement terms and applicable laws and regulations which may affect the Project's goals and costs incurred. Our tests of compliance disclosed the following instance of noncompliance:

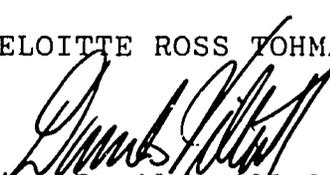
- A. The entity does not withhold the amounts which the high rank functionaries of the Federation should pay to the State according to the Income Tax Law and the Social Security Constitutive Law.

The results of our tests of compliance indicate that, with respect to items tested, except for the matter indicated above, the implementing unit has complied in all material respects, with agreement terms and applicable laws and regulations which may affect the project's goals and costs incurred. With respect to items not tested, nothing came to our attention that caused us to believe that the implementing entity had not complied, in all material respects, with the terms of the agreement and applicable laws and regulations which may affect the project's goals and costs incurred.

MANAGEMENT COMMENTS

This report has been discussed both with FEDEPRICAP and the Agency for International Development. They suggested minor changes which have been incorporated in this final report and as exhibit 1 are detailed the FEDEPRICAP's comments about the noncompliance explained in the prior page.

DELOITTE ROSS TOHMATSU



Lic. Danilo Villalta Loaiza
Partner



PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES OF
CENTRAL AMERICA AND PANAMA (FEDEPRICAP)
ROCAP/GUATEMALA, PROJECT No.596-0149

FUND ACCOUNTABILITY STATEMENT

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying fund accountability statement of the Private Sector Initiatives Project, ROCAP/Guatemala Project No. 596-0149, managed by the Federation of Private Entities of Central America and Panama, for the period February 27, 1989 to June 30, 1990. The fund accountability statement is the responsibility of the Federation of Private Entities of Central America and Panama's management. Our responsibility is to express an opinion on this fund accountability statement based on our audit.

Except as discussed in the following paragraph, we conducted our audit in accordance with generally accepted auditing standards and "Government Auditing Standards" (1988 Revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the fund accountability statement is free of material misstatements. Our audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the fund accountability statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall fund accountability statement presentation. We believe that our audit provide a reasonable basis for our opinion.

As described in the internal control finding No. 1, we could not verify the balance of the cash account as of June 30 1990, due to the fact that since February 1989 the bank reconciliations have not been prepared and there is no control of the balance recorded in books and checkbooks.

As mentioned in internal control findings No. 4 and 5, there is a difference not reconciled between the fund accountability statement and the records of ROCAP/Guatemala, for an amount of US\$5,990, and this statement does not include disbursements made for an amount of US\$11,606.

As described in internal control finding No. 5, we detected disbursements made with FEDEPRICAP funds, which have been recorded and classified as ROCAP's funds amounting to US\$3,616.

As expressed in Note A-3 to the fund accountability statement, the accounting method used by the Federation to convert the disbursements paid in Costa Rican colones to dollars of the United States for reporting purposes, causes differences between the amounts reported as payments made, and the disbursements received of ROCAP, who originated them. These differences are one of the causes why the sum of the income and the expenses of the program do not coincide with the cash available.

As described in Note A-1, the fund accountability statement was prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than generally accepted accounting 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 review the bank reconciliations of the project as explained in paragraph three, and except for the unreconciled difference between the records of the Project and those of ROCAP/Guatemala, the items not included in the final reported figures, the wrong inclusion of payments made with FEDEPRICAP's funds as ROCAP's funds, and the incorrect accounting conversion of payments made in Costa Rican colones for reporting purposes, as described in paragraphs four to six, the accompanying fund accountability statement presents fairly, in all material respects, the income received and the disbursements made by the Private Sector Initiatives Project, ROCAP/Guatemala Project No.596-0149, for the period from February 27, 1989 to June 30, 1990, on the basis of accounting described in Note A-1.

As explained in Note D to the fund accountability statement, there is a contingency caused by the noncompliance with the Income Tax Law and Constitutive Social Security Law because the Federation is neither withholding from its high rank functionaries the social security contributions nor paying their corresponding portion.

This report is intended solely for the use of the United States Agency for International Development, the Government of Guatemala and the Federation of Private Entities of Central America and Panama. 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.



San Jose, Costa Rica
December 12, 1990

PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES OF
CENTRAL AMERICA AND PANAMA (FEDEPRICAP)
ROCAP/GUATEMALA, PROJECT No.596-0149

FUND ACCOUNTABILITY STATEMENT
for the period February 27, 1989 to June 30, 1990
(in U.S. dollars)

Budget Categories	Obligated Amount	Actual
Income:	<u>US\$ 680,000</u>	<u>US\$ 636,747</u>
Disbursements:		
FEDEPRICAP personnel	227,344	202,772
Supporting expenses	89,600	13,762
Operating expenses	197,000	197,847
Training	<u>166,056</u>	<u>180,977</u>
	<u>US\$ 680,000</u>	595,358
Unaccumulated disbursements		<u>11,606</u>
Total disbursements		<u>606,964</u>
Available project funds		29,783
Funds as per books as of June 30, 1990		<u>59,817</u>
Unreconciled difference		<u>US\$ 30,034</u>

See notes to fund accountability statement.

PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES OF
CENTRAL AMERICA AND PANAMA (FEDEPRICAP)
ROCAP/GUATEMALA, PROJECT No.596-0149

NOTES TO THE FUND ACCOUNTABILITY STATEMENT
February 27, 1989 to June 30, 1990

A. Summary of the most relevant accounting policies

1. Accounting basis. The fund accountability statement has been prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than generally accepted accounting principles. Therefore the disbursements are recognized when they are paid and not when the corresponding liability is incurred.
2. Currency. The accounting records are maintained in Costa Rican colones (¢), the legal currency in use in the Republic of Costa Rica. The rates of exchange in effect as of June 30, 1990 for the official purchase of dollars was ¢20.00 per US\$1.00 and for the interbank rate of exchange ¢89.55 per US\$1.00.

The official rate of exchange is established by Congressional Law, and is applicable to a very small number of transactions. The interbank rate is established by the Central Bank, which modifies it periodically. It operates for exports, imports and all other financial transactions.
3. Conversion policy. The fund accountability statement is prepared originally in Costa Rican colones, and then converted to U.S. dollars using the purchase interbank rate prevailing at the closing date of the month.

B. ROCAP/Guatemala Project No. 596-0149

On February 27, 1989 FEDEPRICAP signed an agreement with the Agency for International Development, through the Regional Office of Projects for Central America and Panama Mission to Guatemala (ROCAP/Guatemala), to develop the Private Sector Initiatives Project, ROCAP/Guatemala Project No. 596-0149 with the main purpose of strengthening the capacity of the private sector of Central America, to influence the direction of the socioeconomic development and to increase the knowledge and participation of the private sector in the development process.

The agreement considers six operating areas to develop the project, as follows: a) development of female leadership skills; b) fostering of the communication and training of authorities and entrepreneurs concerning drug trafficking so that this problem does not affect the regional licit trade; c) development of financial instruments for capital mobilization, promotion of stock markets in the region and creation of an information system for investors and other related activities; d) establishment of an economic block to develop international trade with other economic sectors of the world; e) improvement of the port and highway systems of the region as a part of the goals of the area to develop the international commerce; and f) implementation of the information system of the different associations affiliated to FECEPRICAP in the region.

The total obligated amount by the ROCAP/Guatemala for the project is US\$680,000. Additionally, FEDEPRICAP has to contribute to the project as counterpart funds US\$196,600. Also, project paper amendments provide US\$600,000 of technical assistance from CARANA's experts in different areas related to the goals of the project and US\$300,000 for contracting a Private Sector Officer who will be the coordinator of all the activities of ROCAP/Guatemala related to the Project. The project assistance completion date is August 27, 1992.

C. Managing entity of the agreement

The Federation of Private Entities of Central America and Panama (FEDEPRICAP), registered in the Republic of Panama, was founded on January 31, 1987, as an autonomous association of unions and associations of the private sector of Central America and Panama, its principal purpose was to promote, develop and increase the system of private enterprises, and promote the development of the potential resources for the economic and social development of the country members.

D. Contingencies

FEDEPRICAP compensates its high ranking functionaries through professional services and not with wages. The labor relationship of these functionaries is ruled by individual contracts directly signed by every one of them, and these contract clearly specify the term of their contract, their remuneration, and their corresponding benefits such as thirteenth month, vacations, and terminal leave payments. The Income Tax Law and the Constitutive Law of the Costa Rican Social Security consider this laboral relationship as "dependent" and therefore, the amounts paid should be subject to withholding and additional payments therein described. Notwithstanding, the Federation's legal advisor considers that there is no dependency relationship for the effects of these laws, although a contingent liability could exist in the case that the tax or Social Security authorities review this matter.



PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES OF
CENTRAL AMERICA AND PANAMA (FEDEPRICAP)
ROCAP/GUATEMALA, PROJECT No.596-0149

INTERNAL CONTROL STRUCTURE REPORT

INDEPENDENT AUDITORS' REPORT

We have audited the fund accountability statement of Private Sector Initiatives Project, ROCAP/Guatemala Project No. 596-0149, managed by the Federation of Private Entities of Central America and Panama, for the period February 27, 1989 to June 30, 1990, and have issued our report thereon dated December 12, 1990.

We conducted our audit in accordance with generally accepted auditing standards and "Government Auditing Standards" (1988 Revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the fund accountability statement is free of material misstatement.

In planning and performing our audit of the fund accountability statement of Private Sector Initiatives Project, ROCAP/Guatemala Project No. 596-0149, for the period February 27, 1989 to June 30, 1990, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the fund accountability statement and not to provide assurance on the internal control structure.

The management of the Federation of Private Entities of Central America and Panama (FEDEPRICAP) is responsible for establishing and maintaining an internal control structure to manage the Project's operations. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure 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 recorded properly to permit the preparation of the fund accountability statement in accordance with the accounting basis used. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the

structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the effectiveness of the design and compliance with the policies and procedures may deteriorate.

For the purposes of this report, we have classified the significant policies and procedures in the following categories: a) fund accountability internal control; b) fund controls; c) goods and services procurement controls; d) accounting and safeguarding controls for furniture and office equipment; e) budgetary controls; f) information and communication controls.

For all of the internal control categories listed above, we obtained an understanding of the design of the relevant policies and procedures and whether they have been placed in operation, and we assessed the control risk.

We noted certain matters involving the internal control structure and its operations which we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants and "Government Auditing Standards" (1988 Revision), issued by the Comptroller General of the United States. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgement, could adversely affect the entity's ability to record, process, summarize and report financial data consistent with the assertions of management in the fund accountability statement. The reportable conditions noted are described in the findings under this section.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the fund accountability statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe that the reportable conditions corresponding to findings 1 to 6 of this report are material weaknesses.

We also noted other matters involving the internal control structure and its operation that we have reported to the management of FEDEPRICAP, in a separate letter dated December 12, 1990.

This report is intended solely for the information and use of the FEDEPRICAP and the United States 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.

Delvitté Ross Colman.

San José, Costa Rica
December 12, 1990

PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES OF
CENTRAL AMERICA AND PANAMA (FEDEPRICAP)
ROCAP/GUATEMALA, PROJECT No.596-0149

INTERNAL CONTROL STRUCTURE REPORT

FINDINGS

1. There are control deficiencies in cash management

Condition:

- A. The bank accounts in Costa Rican colones are under the name of the Executive Director, who can sign checks individually.
- B. Original checks paid by banks are not reviewed.
- C. The external accountant has not prepared any bank reconciliations of the Project since the inception date (February 1989).

Criteria:

The timely preparation of the bank reconciliations is a basic requirement for the establishment of the internal control structure for funds and must be prepared on a timely basis every month as a normal part of accounting operations. The reconciliation of cash funds according to bank statement balances and to accounting records and the combined signing of checks, are basic for good internal control of cash funds. Also, as an additional procedure to the bank reconciliations, paid checks received from banks must be reviewed to check on any possible alterations.

Cause:

The principal causes are described below:

- A. Combined signatures: FEDEPRICAP had to open the bank accounts in colones under the name of the executive director, as it had not been constituted as a legal entity in the Republic of Panama and under these circumstances the banks would not accept the opening of a bank account. If the accounts were opened under the name of a natural person banks cannot limit the access to the funds deposited, through combined signatures. Later, when the Federation obtained its legal status in Panama, it did not make the necessary changes in its bank accounts.

- B. Review of checks paid and returned by banks: Management has not paid proper attention to this procedure.
- C. Reconciliation between bank books and the accounting records: Management of FEDEPRICAP did not make the necessary follow up in order to ensure that bank reconciliations were performed periodically.

Effect:

Errors and irregularities may be occurring in handling and/or recording cash funds, which are not detected or may not be detected opportunely by the Federation. Besides, this lack of control, nullifies the independent revision of the cash balances.

Recommendation:

For the correction of these matters and to diminish the risk of errors and irregularities, FEDEPRICAP should make the following:

- A. Combined signatures: To open a dual-signature bank account under the name of the Federation of Private Entities of Central America and Panama.
 - B. Review of checks paid by banks: To review every month the paid checks returned by banks in order to note possible alterations of amounts, signatures and doubtful endorsements.
 - C. Bank accounts reconciliation: To establish proper responsibilities and require the external accountant to comply with the terms of their contract, through the updating of the bank reconciliations, including the reconciliation of the accounting records with those of the checkbook, in a period of not more than 90 days.
2. The accounting and safeguarding control of office furniture and equipment is deficient

Condition:

In this particular, the following deficiencies were found:

- A. The auxiliary record has not been summarized and has not been reconciled with the accounting books since February, 1989.
- B. It is not possible to differentiate between the assets acquired with ROCAP's funds from those bought with FEDEPRICAP's funds.

- C. The auxiliary record is not updated.
- D. The cost of the assets purchased is recorded according to the currency used, mixing colones and dollar currencies.
- E. Physical inventories of furniture and equipment are not taken periodically.

Criteria:

The auxiliary record of furniture and office equipment should be maintained duly updated, classified and reconciled with the control account, in colones and dollars. Additionally, physical inventories should be taken periodically of all furniture and equipment.

Cause:

FEDEPRICAP management has not received a satisfactory service from the external accountant in this respect.

Effect:

Assets bought under the agreement terms are not duly controlled.

Recommendation:

FEDEPRICAP should take the necessary corrective steps to establish an adequate control of the assets acquired, considering the following:

- A. To complete and update the furniture and office equipment auxiliary record with the following minimum information: number of the check drawn to acquire the asset, suppliers name, invoice number, purchase cost in colones and dollars, item number, location and useful life.
- B. To determine by the check or any other document, which assets were acquired with ROCAP and which with FEDEPRICAP funds, so as to classify and present them separately.
- C. To prepare the reconciliation between the auxiliary record and the ledger account and investigate the resulting differences, if any.
- D. To reconcile and update this auxiliary account every month.
- E. Finally, once the aforementioned matters, are resolved to assign the FEDEPRICAP'S assistant director the duty of verifying that the auxiliary records are maintained updated

and reconciled every month, taking physical inventories and comparing them with the auxiliaries quarterly.

3. Proper control procedures have not been established for the filling of documents

Condition:

As a result of our tests, we noted that some of the documents paid are not filed with the corresponding copies of checks. Additionally, when filed they do not present any cross references. For example, quotations for purchases approved and the travel expense checks not refer to the activity reports or seminars attended to by functionaries or the travels made by them. Neither do they include ROCAP's authorization approving these travels when they have not been approved through the budget.

Criteria:

All checks must be duly backed up with the documents which legitimate them; the documents must be stamped indicating the number of the check used. If the documents paid with a check are bulky and they are not filed with the check, they should be cross referenced to the corresponding check.

Cause:

The document setting out the administrative procedures, regarding filing, does not include appropriate instructions for filing and identifying the documents which should back up the checks issued and their cross-references.

Effect:

It becomes difficult and sometimes impossible to locate evidence supporting travel expenses and purchases of goods and services.

Recommendation:

FEDEPRICAP should develop specific check filing procedures, which include their identification and location. Besides, check authorizers should verify this procedure at the moment they give their authorization.

4. The fund accountability statement and the accounting records of ROCAP/Guatemala are not reconciled

Condition:

When the reconciliation of the information received from ROCAP/Guatemala related to the project disbursements was done with ROCAP's, a difference was discovered of US\$5,990 which could not be explained.

Criteria:

The fund accountability statement must be reconciled periodically with the information provided by ROCAP.

Cause:

No one has been assigned to prepare the reconciliations with the information provided by ROCAP.

Effect:

Errors could remain undiscovered if the reconciliations are not prepared regularly.

Recommendation:

FEDEPRICAP should request ROCAP/Guatemala, at least quarterly, a statement of account in order to reconcile it to the FEDEPRICAP's accounting records, including the above mentioned amount of US\$5,990. This work should be performed by the external accountant.

5. Lack of procedures to supervise the accounting records

Condition:

- A. The disbursements presented in the fund accountability statement do not include US\$11,606 which corresponds to project funds, because, even though they were correctly recorded, they were not included in the reports.
- B. As a result of the selective tests applied, disbursements paid with FEDEPRICAP's funds amounting to US\$3,616, were recorded as if they had been paid with ROCAP's funds.

Criteria:

The disbursements presented in the fund accountability statement must include all the amounts invested in the project, and at the same time they must be correctly classified according to their origin. Besides, all information originated from the accounting records must be submitted to a process of verification and supervision.

Cause:

These matters were not detected neither by the external accountant nor by the FEDEPRICAP'S assistant director.

Effect:

The information sent to ROCAP/Guatemala about disbursements made with project's funds is incorrect.

Recommendation:

FEDEPRICAP should request the external accountants to investigate these items and adjust when necessary the accounting records and the fund accountability statement. Additionally, the Federation must establish formal procedures to supervise the accounting information provided by the external accountants, holding its assistant director responsible for this.

6. The accounting conversion method of colones to dollars for reporting purposes is inadequate

Condition:

FEDEPRICAP maintains its accounting records in Costa Rican colones. Whenever it receives funds in dollars from ROCAP/Guatemala to pay its disbursements, it does not convert them totally into colones, which is only done when the funds are needed. When the funds in colones are used, they are recorded in colones and converted at the interbank purchase rate prevailing at the end of the month on which the purchase was paid, regardless the rate of exchange at which the original dollars had been converted into colones.

Criteria:

The disbursements paid in Costa Rican colones must be converted at the exchange rate needed for purchase of the dollars on that date.

Cause:

The management of FEDEPRICAP did not know the effects of this conversion method of disbursements in colones, because it maintains its records only in Costa Rican currency and, therefore, has not analyzed with the external accountant the correct method of conversion. Additionally, the fact that the entity deposits the reimbursements from USAID in a dollar bank account, converting them only when the funds are used, originated significant exchange differences.

Effect:

The disbursements presented in the fund accountability statement are shown understated and the amounts available do not correspond with the amounts of cash and its equivalents in hands of the Federation at the closing dates.

Recommendation:

FEDEPRICAP should request the external accountants to establish another system to convert the disbursements paid with funds from the Project, in such a way that the exchange differences be diminished or explained by means of this new system.



PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES OF
CENTRAL AMERICA AND PANAMA (FEDEPRICAP)
ROCAP/GUATEMALA, PROJECT No.596-0149

COMPLIANCE WITH AGREEMENT TERMS AND APPLICABLE LAWS
AND REGULATIONS REPORT

INDEPENDENT AUDITOR'S REPORT

We have audited the fund accountability statement of Private Sector Initiatives Project, ROCAP/Guatemala Project No. 596-0149, managed the Federation of Private Entities of Central America and Panama (FEDEPRICAP), for the period February 27, 1989 to June 30, 1990 and have issued our report thereon dated December 12, 1990.

We conducted our audit in accordance with generally auditing standards and "Government Auditing Standards" (1988 Revision), issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the fund accountability statement is free of material misstatement.

Compliance with agreement terms and laws and regulations, applicable to the Private Sector Initiatives Project is the responsibility of FEDEPRICAP's management. In obtaining reasonable assurance about whether the fund accountability statement is free of material misstatement, we performed tests of FEDEPRICAP's compliance with certain provisions of laws, regulations, contracts and grants terms. However, our objective was not to provide an opinion on overall compliance with such provisions.

Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in agreement statutes, or regulations, that caused us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the fund accountability statement. The results of our tests of compliance disclosed the following material instance of noncompliance matters.

As indicated in finding 1 of this section, FEDEPRICAP has not complied with the Income Tax Law and the Constitutive Law of

Costa Rican Social Security because the withholding of employees contributions from the functionaries' salaries has not been made.

We considered this material instance of noncompliance in forming our opinion on whether the fund accountability statement of the Private Sector Initiatives Project for the period February 27, 1989 to June 30, 1990 are presented fairly, in all material respects, in conformity with the accounting basis used, and this report does not affect our opinion dated December 12, 1990 on the fund accountability statement.

Except as described above, the results of our tests of compliance indicate that, with respect to the items tested, FEDEPRICAP complied, in all material respects, with the provisions referred to in the third paragraph of this report, and with respect to items not tested, nothing came to our attention that caused us to believe that FEDEPRICAP had not complied, in all material respects, with those provisions.

We noted certain immaterial instances of noncompliance, that we have reported to the management of FEDEPRICAP in a separate letter dated December 12, 1990.

This report is intended solely for the information and use of the Federation of Private Entities of Central America and Panama and the United States 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.



San José, Costa Rica
December 12, 1990

PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES OF
CENTRAL AMERICA AND PANAMA (FEDEPRICAP)
ROCAP/GUATEMALA, PROJECT No.596-0149

COMPLIANCE AGREEMENT TERMS AND APPLICABLE LAWS
AND REGULATIONS REPORT

FINDINGS

1. The Federation has not complied with the Income Tax Law nor with the Constitutive Law of the Costa Rican Social Security

Condition:

FEDEPRICAP compensates its high ranking functionaries with professional fees instead of wages. The labor relation of these persons are covered by individual contracts signed directly by the interested parties. These contracts stipulate the terms of the contract, monthly remuneration and the other benefits they are entitled to, such as thirteenth month, vacations, and terminal leave payments. These functionaries have not been subjected to income tax withholding; nor were they included in the social security payrolls; therefore FEDEPRICAP does not effect the corresponding withholding and payments.

Criteria:

The aforementioned contracts are considered by the Income Tax Law and the Social Security Law (Articles 27 and 3, respectively) as a dependency or normal relation between the employer and his employee respectively. Therefore FEDEPRICAP is obliged to be a withholding and receiving agent for these purposes. Also, according to articles 23 of the Income Tax Law and the Tax Standards and Procedures Law, the Federation is obliged to be a withholding receiving agent.

Cause:

The legal advisor of FEDEPRICAP is of the opinion that in conformance with the definitions established by the respective laws and its implications, FEDEPRICAP is not a withholding agent of any kind of taxes or social contributions because it is not a legal entity in Costa Rica and therefore the directors contracted by FEDEPRICAP are responsible before the competent authorities to file and pay the corresponding taxes. Regarding the Constitutive Law of the Costa Rican Social Security, the legal advisor sustains that the relation with the FEDEPRICAP's directors is contractual and not a direct dependence, which exempts it from withholding and paying, any social security

contributions. Based on this criteria FEDEPRICAP has not made the withholding.

Effect:

If the tax or social security authorities insist on this matter, the entity would be exposed to the obligation of making withholding payments, and paying fines and interests.

Recommendation:

FEDEPRICAP should analyze and evaluate the risk it is assuming in this matter, to make a sound decision regarding the possible obligation to pay the corresponding withholding and social security charges; or otherwise to document very well its criteria that it is not incurring in a violation of the Costa Rican laws. It is suggested that it contact high ranking functionaries of the Costa Rican Social Security and of the Income Tax Administration to obtain an official response from these entities and avoid the consequences which might occur due to this contingent liability.

PRIVATE SECTOR INITIATIVES PROJECT
MANAGED BY THE FEDERATION OF PRIVATE ENTITIES OF
CENTRAL AMERICA AND PANAMA (FEDEPRICAP)
ROCAP/GUATEMALA, PROJECT No.596-0149

LIST OF RECOMMENDATIONS

1. There are control deficiencies in cash management

For the correction of these matters and to diminish the risk of errors and irregularities, FEDEPRICAP should make the following:

- A. Combined signatures: To open a dual-signature bank account under the name of the Federation of Private Entities of Central America and Panama.
- B. Review of checks paid by banks: To review every month the paid checks returned by banks in order to note possible alterations of amounts, signatures and doubtful endorsements.
- C. Bank accounts reconciliation: To establish proper responsibilities and require the external accountant to comply with the terms of their contract, through the updating of the bank reconciliations, including the reconciliation of the accounting records with those of the checkbook, in a period of not more than 90 days.

2. The accounting and safeguarding control of office furniture and equipment is deficient

FEDEPRICAP should take the necessary corrective steps to establish an adequate control of the assets acquired, considering the following:

- A. To complete and update the furniture and office equipment auxiliary record with the following minimum information: number of the check drawn to acquire the asset, suppliers name, invoice number, purchase cost in colones and dollars, item number, location and useful life.
- B. To determine by the check or any other document, which assets were acquired with ROCAP and which with FEDEPRICAP funds, so as to classify and present them separately.
- C. To prepare the reconciliation between the auxiliary record and the ledger account and investigate the resulting differences, if any.
- D. To reconcile and update this auxiliary account every month.

E. Finally, once the aforementioned matters, are resolved to assign the FEDEPRICAP'S assistant director the duty of verifying that the auxiliary records are maintained updated and reconciled every month, taking physical inventories and comparing them with the auxiliaries quarterly.

3. Proper Control Procedures have not been established for the Filing of Documents

FEDEPRICAP should develop specific check filing procedures, which include their identification and location. Besides, check authorizes should verify this procedure at the moment they give their authorization.

4. The fund accountability statement and the accounting records of ROCAP/Guatemala are not reconciled

FEDEPRICAP should supply the information received from ROCAP/Guatemala to the external accountant so that they can prepare the respective reconciliations and explain, on a timely basis, all the existing differences, including the above mentioned amount of US\$5,990. This procedure should be consistently followed at least every three months.

5. Lack of Procedures to Supervise the Accounting Records

FEDEPRICAP should request the external accountant to investigate these items and adjust when necessary the accounting records and the fund accountability statement. Additionally, the Federation must establish formal procedures to supervise the accounting information provided by the external accountant, holding its assistant director responsible for this.

6. The accounting conversion method of colones to dollars for reporting purposes is inadequate

FEDEPRICAP should request the external accountant to establish a First In, First Out (FIFO) system to convert the disbursements paid with funds from the Project, in such a way that the disbursements paid with local currency will be calculated at the exchange rate for purchasing the dollars used for paying the disbursements, keeping for this a special control account.

7. The Federation has not complied with the Income Tax Law nor with the Constitutive Law of the Costa Rican Social Security

FEDEPRICAP should analyze and evaluate the risk it is assuming in this matter, to make a sound decision regarding the possible obligation to pay the corresponding withholding and social security charges; or otherwise to document very well its criteria

that it is not incurring in a violation of the Costa Rican laws. It is suggested that it contact high ranking functionaries of the Costa Rican Social Security and of the Income Tax Administration to obtain an official response from these entities and avoid the consequences which might occur due to this contingent liability.

EXHIBIT 1

* * *



July 3, 1991

Mr. Reginald Howard
Regional Inspector General for Audit
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT
Tegucigalpa, Honduras, C. A.

Dear Sir:

Having reviewed the External Audit Report prepared by DELOITTE ROSS TOHMATSU and discussed certain aspects of the document with the representative of RIG, Lic. María Elena Flores, we wish to make several comments that we believe are important for the future of the Project and that we hope will be accepted by you:

a. **Reconciliation of funds ROCAP - FEDEPRICAP**

Due to the fact that no periodic reports are received from ROCAP, it is not possible to concile the disbursements made by ROCAP with those received by FEDEPRICAP. Therefore, the difference of US\$5,990 can not be cleared up until these data are received from ROCAP. We are requesting these reports.

c. **Conversion of dollars to colones**

Considering that the auditing firm questions the method to convert dollars to colones, we offer to study a methodology convenient to the interest of both parties. We will be informing you about this matter in a near date.

d. **Difference of US\$3,616**

Due to an error in the codification of expenses, the amount of US\$3,616 was paid and charged to ROCAP, when it should had been recorded in the account corresponding to FEDEPRICAP's funds. We are making the corresponding reclassification. In addition, we are taking the necessary provisions to sensibly reduce the probability of committing similar error, such as having the bookkeepers visit FEDEPRICAP's offices daily.

d. **Unexplained excess difference of US\$30,034**

On page 16, of the report there is a mention of an unexplained difference of US\$30,034. We believe that once the records of ROCAP and FEDEPRICAP have been conciliated and after reclassifying the items erroneously recorded, we will justify most of, if not all the difference previously pointed out, which we suppose was mainly originated in remnants of the previous project and exchange difference. We assume the compromise to

FEDERACION DE ENTIDADES PRIVADAS DE CENTROAMERICA Y PANAMA

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conciliate these balances, at least every three months, accordingly with ROCAP's statements.

e. **Payment of professional fees to high rank functionaries**

According to the external auditors' statements, the way to contract high rank professionals establishes a labor relation of dependency, making the respective income taxable by the Income Tax Administration and the Social Security in Costa Rica. This would imply that the Federation should pay the corresponding taxes and also employer's contributions to the Social Security, which can be calculated as a 22% of the professional fees paid.

At FEDEPRICAP we do not share the auditors' opinion, because the Federation is an entity domiciled in Panama and not registered in Costa Rica. Therefore, neither the Costa Rican Laboral Legislation or its Income Tax Laws are applicable. Second, we consider that signing contracts individually with each professional, does not constitute a laboral or even a dependency relation. Third, ROCAP would not be acquiring any compromise related to the Social Security contributions, because the only responsible entity would be FEDEPRICAP, which is the juridical person that contracts these professionals. On the other hand, it is difficult to affirm that this income is obtained in Costa Rica, due to the international character of FEDEPRICAP's activities. This is important to have it in mind because the Costa Rican Legislation only assesses income earned locally.

All the other remarks stated in the auditor's report have been corrected.

Hoping that the aforementioned comments will be of your entire satisfaction, we remain sincerely yours,

Mr. Carlos M. Echeverría E.
Executive Director



cc: Dr. Albert Zucca
Private Sector Office ROCAP/AID

Lic. Danilo Villalta, Partner
Deloitte Ross Tohmatsu

Lic. Guillermo Smith, Manager
C&C Consultores, S. A.

Lic. Marco Vinicio Alvarez A.
Director Adjunto, Administración y Comunicaciones

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APPENDIX

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