

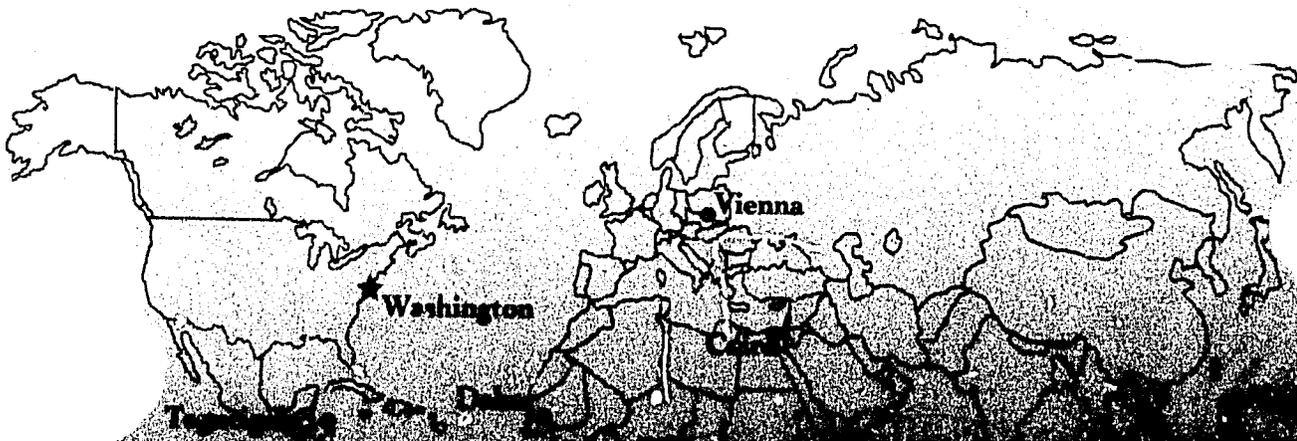
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Regional Inspector General for Audit
Tegucigalpa, Honduras

**Audit of USAID/El Salvador's
Agrarian Reform Financing Project
Managed by the Central Reserve Bank of El Salvador
August 1, 1989 to July 31, 1991**

**Audit Report No. 1-519-93-10-N
January 25, 1993**



**INSPECTOR
GENERAL**

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

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AGENCY FOR INTERNATIONAL DEVELOPMENT

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

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January 25, 1993

MEMORANDUM

TO: D/USAID/El Salvador, John Sanbrailo

FROM: RIG/A/T, Lou Mundy *Lou Mundy*

SUBJECT: Audit of USAID/El Salvador's Agrarian Reform Financing Project, Managed by the Central Reserve Bank of El Salvador, August 1, 1989 to July 31, 1991

This report presents the results of a financial audit of the Agrarian Reform Financing Project (Project), USAID/El Salvador Project No. 519-0307, managed by the Central Reserve Bank of El Salvador (Bank) for the period August 1, 1989 to July 31, 1991. The audit firm of Deloitte Touche Tohmatsu prepared the report dated November 25, 1992.

The purpose of the Project is to increase the availability and productive use of credit in the agrarian reform sector. To accomplish this objective, the Bank established a rediscount line of credit for lending to intermediate credit institutions. The Project is scheduled for completion in July 1993 and has a total budget of \$67.0 million (A.I.D. grant funds of \$50.0 million and \$17.0 million from the Government of El Salvador). During the period under audit, the Bank received and disbursed \$10.0 million of A.I.D. grant funds.

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

The auditors concluded that the fund accountability statement presents fairly, in all material respects, the Bank's funds received and the disbursements made during the period audited. The auditors reported

a

questionable costs of \$110,236 (equivalent to El Salvadoran ₡700,000) which did not affect their opinion on the fund accountability statement.

The auditors identified four material weaknesses in the Bank's internal control structure for Project activities. They reported that: (1) accounting records at one cooperative were not current and thus, loans made under the Project could not be confirmed; (2) there were a series of control deficiencies in the Bank's Electronic Data Processing Department; (3) field supervision reports, which report on the use of the funds loaned by the participating financial institutions, were incomplete; and (4) the Bank and participating financial institutions utilized inconsistent interest computation methods.

With respect to the Bank's compliance with agreement terms and applicable laws and regulations, the auditors found two material instances of noncompliance. The auditors found that: (1) the Bank had not repaid an advance to the Project on a timely basis, and (2) all interest earned had not been recapitalized as required by the Project Agreement.

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

Recommendation No. 1

We recommend that USAID/El Salvador resolve the questionable costs of \$110,236 (all questioned) identified in the Deloitte Touche Tohmatsu audit report dated November 25, 1992 and recover from the Central Reserve Bank all amounts determined to be unallowable.

Recommendation No. 2

We recommend that USAID/El Salvador obtain evidence that the Central Reserve Bank of El Salvador has established procedures to: (1) require that participating financial institutions have implemented controls to obtain periodic financial statements from their client cooperatives and to confirm and verify the accounting records of the cooperatives on a timely basis; (2) correct the various deficiencies in its Electronic Data Processing Department as described on pages 17 to 18 of the Deloitte Touche Tohmatsu audit report; (3) ensure that the participating financial institutions maintain adequate field supervision files; (4) standardize the method for computing interest rates applied under the Project; (5) repay advances on a timely basis; and (6) reconcile interest earned and capitalized and capitalize to the Project any additional amounts required.

The audit report indicates that the questionable costs identified in

Recommendation No. 1 were repaid by the Bank subsequent to the cut-off date of the audit. Recommendation No. 1 can be resolved and closed when the Mission provides documentation concerning the amount of funds reimbursed. Recommendation No. 2 can be resolved when the Mission presents an acceptable firm plan of action to correct the reported deficiencies and can be closed upon presentation of acceptable evidence that procedures to correct the deficiencies have been established.

The report was discussed with the Bank's management officials who expressed general agreement with its contents. Management's comments are included in each finding.

This final audit report is being transmitted to you for your action. Please advise this office within 30 days of actions planned or taken to resolve and close the recommendations.

**Regional Inspector General for Audit
Tegucigalpa, Honduras**

**Audit of USAID/El Salvador's
Agrarian Reform Financing Project
Managed by the Central Reserve Bank of El Salvador
August 1, 1989 to July 31, 1991**

**Audit Report No. 1-519-93-10-N
January 25, 1993**

f.

**Deloitte Touche
Tohmatsu**



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AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

**Deloitte Touche
Tohmatsu
International**

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AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

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Deloitte Touche Tohmatsu



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November 25, 1992

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

Dear Mr. Mundy:

This report presents the results of our financial audit of the Agrarian Reform Financing USAID/El Salvador Project No. 519-0307, managed by the Central Reserve Bank (BCR), for the period from August 1, 1989 to July 31, 1991.

BACKGROUND

On July 31, 1986, the Government of El Salvador (GOES), through the Ministry of Social and Economic Development Planning and Coordination, and the Ministry of Agriculture and Livestock, signed agreement No. 519-0307 for US\$50,000,000 with the United States Government through the Agency for International Development (USAID/El Salvador). The project assistance completion date was extended to July 31, 1993.

The purpose of the project is to increase the availability and productive use of credit in the agrarian reform sector. To accomplish this objective, the Central Reserve Bank will establish a rediscount line of credit for on-lending to intermediate credit institutions.

For the implementation of the project, the Central Reserve Bank (BCR) created the Agrarian Reform Financial Technical Unit (UTFRA), which is responsible for the administration of the Rediscount Line component, by means of the approval and supervision of the credits granted to the Agrarian Reform beneficiaries, through the participating institutions.

The agreement was approved to increase the availability and productive use of credit in the reformed sector. The principal elements of this project are the following: a rediscount line in



the Central Reserve Bank (BCR) for production and investment loans to the reformed sector; a training program for agricultural loan officers; a series of policy studies; a pilot rural savings mobilization program; and administrative support and evaluation. All funds provided for the rediscount line in the BCR to be permanent addition to BCR resources.

As of July 31, 1991, all funds available under the project had been obligated as follows:

<u>Line Item</u>	<u>Grant (US\$ Thousands)</u>
Rediscount line	\$46,111
Long term technical assistance	758
Training	2,012
Studies	641
Saving mobilization	75
A.I.D. Project Administration	232
Evaluation	59
Contingency/Inflation	<u>112</u>
Total	\$50,000 =====

The Government of El Salvador agreed to provide counterpart funds for a total equivalent to \$17.0 million; of this amount, \$1.0 million are to be provided by the participating institutions.

During the period from January 1987 to June 30, 1992, credits amounting to C532.9 millions were contracted by the participant institutions with the Central Bank for the agrarian reform and charged to the funds of the Project USAID No. 519-0307; an amount of C433.6 millions was rediscounted; C363.3 millions were paid and there was a balance amounting to C64.3 millions.

From the total of C532.9 millions, 92.9% has been granted to cooperatives and the remaining 7.1% for individual beneficiaries. 77% of the total granted has been for short term credits and 23% for medium and long term credits.

Short term credits have been used mainly for coffee crops, basic grains and non-traditional products export. The medium and long term credits have been used for the purchase of machinery and agricultural equipment (29.5%), livestock projects (12.2%), the remaining (21.3%) has been used for coffee crop cultivation, infrastructure and other cultivations for exporting purposes.

The record of payment from the beneficiaries of the agrarian reform, Project USAID No. 519-0307 shows the following results:



as of June 30, 1992, participant institutions reported 5% aging, and the level of loans recovery was 98%

This rate indicates the percentage effectively recovered in comparison with the total that has to be collected up date.

OBJECTIVES AND SCOPE

We were engage to perform a financial audit of USAID/El Salvador's Agrarian Reform Financing Project No. 519-0307, managed by the Central Reserve Bank for the period August 1, 1989 to July 31, 1991. Our audit was performed in accordance with generally accepted auditing standards and U. S. Comptroller General's "Government Auditing Standards", and accordingly included such tests of the accounting records and other auditing procedures as we considered necessary under the circumstances.

The general objective was to perform a financial audit of the Agrarian Reform Financing USAID/El Salvador Project No. 519-0307, activities managed by BCR, our audit was performed to determine whether:

- a) The fund accountability statements for the project activities present fairly, in all material respects, the financial situation of the project, managed by the Central Reserve Bank (BCR) from August 1, 1989 to July 31, 1991 and costs reported as incurred and reimbursed by USAID/El Salvador during the period are allowable, allocable, and reasonable in accordance with agreement terms, and applicable laws and regulations.
- b) The internal control structure of the BCR is adequate to manage the Project's operations.
- c) BCR complied with agreement terms, and applicable laws and regulations which may affect the project's goals and incurred costs.

The scope of our work consisted of:

1. Audit the fund accountability statement of the project to:
 - a) Examine the fund accountability statement including the budgeted amounts by Category and major items; the costs reported by BCR as incurred during the period covered by the audit and the revenues received from USAID/El Salvador for that period.
 - b) Examine whether the fund accountability statement included all USAID/El Salvador direct assistance funds identified by each specific project, grant, loan, etc.



- c) Examine whether the revenues received from USAID/El Salvador less the costs incurred, reconciled with the balance in the bank accounts at the end of the period.
 - d) Our work also included evaluations of project implementation actions and accomplishments to determine that costs incurred are allowable, allocable and reasonable under the agreement terms, and to identify areas where fraud, waste, abuse and mismanagement exist or could exist as a result of inadequate controls.
2. Review and evaluate the BCR's internal control structure related with the operations of credit disbursed, making tests of controls to determine that established procedures and controls are working as designed.
 3. Determine whether BCR has complied with the contract's terms, project implementation letters, and applicable laws and regulations, and identify those aspects of noncompliance which could directly and significantly affect the fund accountability statement.

Direct USAID/El Salvador disbursements were not covered in the scope of the audit.

RESULTS OF THE AUDIT

Fund Accountability Statement

The result of our audit indicate that the fund accountability statement for the Agrarian Reform Financing USAID/El Salvador Project No. 519-0307, managed by the BCR, presents fairly, in all material respects the financial operations of the project.

Our review disclosed questionable costs of C700,000 as described in Note D, this advance was repaid by the BCR subsequent to the cut-off date of the audit.

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 in accordance with the 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 judgement, could adversely affect the BCR's capacity to record, process, summarize, and report financial data consistent with the assertions of management in the fund accountability statement. The reportable conditions, which we considered material were the following:

1. Credit balance without direct confirmation obtained.
2. Deficiencies in the electronic data processing.
3. Lack of agricultural supervision report on credit files.
4. Differences in the interest computing base.

Compliance with Agreement Terms, 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 our tests to assure that the BCR complied with the agreement terms and applicable laws and regulations which may affect the funds received from USAID and the credits disbursed by the BCR.

Our tests of compliance disclosed the following instances of noncompliance:

1. Advance payment for C700,000 not repaid, on the date established.
2. Interests for C36,509 not capitalized opportunely.

The result of our tests of compliance indicate that, for examined entries, except for the above mentioned, the BCR has complied, in all important aspects, with the agreement terms and with the applicable laws and regulations. For the entries not examined, nothing called our attention to any matter which would lead us to believe that the BCR has not complied, in all significant aspects, with the contract terms and with laws and regulations which could affect the funds received from USAID and the credits granted by the BCR.

MANAGEMENT COMMENTS

A copy of this draft report was submitted to the Central Reserve Bank (BCR) and discussed with them on October 9, 1992. Based on the comments and support documentation provided by the management of the BCR, it was modified and the final report was accepted.



The management comments are included in each finding.

DELOITTE TOUCHE TOHMATSU

A handwritten signature in black ink, appearing to read 'Rolando Lara Leiva', written over the printed name below it.

Lic. Rolando Lara Leiva



AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

REPORT ON THE FUND ACCOUNTABILITY STATEMENT
INDEPENDENT AUDITORS' REPORT

We have audited the accompanying fund accountability statement of the Agrarian Reform Financing USAID/El Salvador Project No. 519-0307, managed by the Central Reserve Bank (BCR), for the period from August 1, 1989 to July 31, 1991. This fund accountability statement is the responsibility of the Central Reserve Bank's management. Our responsibility is to express an opinion on this fund accountability statement based on our audit.

Except as discussed in the next 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 misstatement. Our audit included 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 the management, as well as evaluating the overall fund accountability statement. We believe that our audit provides a reasonable basis for our opinion.

We did not have an external quality control review by an unaffiliated audit organization as required in paragraph 46 chapter 3 of Government Auditing Standards, since no such quality review project is offered by professional organizations in Guatemala. We believe that the effect of this departure from the financial audit requirements of Government Auditing Standards is not material, because we participate in the Deloitte Touche Tohmatsu International worldwide internal quality control program which requires the Deloitte Touche Tohmatsu Guatemala office to be subjected, every three years, to an extensive quality control review by partners and managers from other Deloitte Touche Tohmatsu offices.



As described in Note A-2, the Fund Accountability Statement was prepared on the basis of cash which is a comprehensive basis of accounting other than generally accepted accounting principles.

In our opinion, the fund accountability statement referred to above, presents fairly, in all material respects, the funds received and the disbursements made by the Agrarian Reform Financing USAID/El Salvador Project No. 519-0307, for the period from August 1, 1989 to July 31, 1991, in accordance with the accounting basis described in Note A.

Our review disclosed some questionable costs for the amount of C700,000, as described in Note D., this advance was repaid by BCR subsequent to the cut-off day of the audit.

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

Deloitte Touche Tohmatsu.

June 2, 1992
San Salvador, El Salvador

AUDIT OF THE AGRARIAN REFORM FINANCING
 USAID/EL SALVADOR PROJECT No. 519-0307
 MANAGED BY CENTRAL RESERVE BANK
 FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

FUND ACCOUNTABILITY STATEMENT

	<u>Budget</u>	Total Project Disbursements	Not Audited July 31, 1989	Audited July 31, 1991	Questionable Costs
<u>Incomes</u>	C230,000,000	C137,092,702	C73,410,726	C63,681,976	C700,000
<u>Expenses</u>					
<u>Banks</u>					
Salvadoreño		39,024,650	17,806,296	21,218,354	
Cuscatlán		23,773,607	13,997,313	9,776,294	
Agrícola Co- mercial		16,329,536	7,912,291	8,417,245	
Capitalizador		16,288,972	8,514,883	7,774,089	
Hipotecario		14,385,698	10,628,936	3,756,762	
De Comercio		10,095,846	5,323,164	4,772,682	
De Crédito					
Popular		6,513,644	3,708,571	2,805,073	
Mercantil		5,201,690	2,625,566	2,576,124	
Financiero		2,858,786	1,341,900	1,516,886	
Desarrollo e Inversión		<u>2,620,273</u>	<u>1,551,806</u>	<u>1,068,467</u>	
Total	C137,092,702	C137,092,702	C73,410,726	C63,681,976	C700,000
	=====	=====	=====	=====	=====
Available	C92,907,298				
	=====				

The enclosed notes are an integral part of this report.

AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

NOTES TO THE FUND ACCOUNTABILITY STATEMENT

A. Summary of the Most Relevant Accounting Policies

1. Reporting Basis - The enclosed fund accountability statement included only those disbursements for credits disbursed by the Central Reserve Bank corresponding to the agreement rediscount line.
2. Accounting Base - The project's fund accountability statement is prepared on a cash basis, in which funds received from USAID for credits previously disbursed by the Central Reserve Bank of El Salvador to the Banks of the system are recorded.

As of July 31, 1991 USAID/El Salvador had not reimbursed the Central Reserve Bank C22,529,675 in credits granted to the Agrarian Reform Sector through the participating Banks.

B. Grant Agreement

On July 31, 1986, the Government of El Salvador (GOES), through the Ministry of Social and Economic Development Planning and Coordination, and the Ministry of Agriculture and Livestock, signed agreement No. 519-0307 for US\$50,000,000 with the United States Government through the Agency for International Development (USAID/El Salvador). The project assistance completion date was extended to July 31, 1993.

The purpose of the project is to increase the availability and productive use of credit in the agrarian reform sector. To accomplish this objective, the Central Reserve Bank will establish a rediscount line of credit for on-lending to intermediate credit institutions.

For the implementation of the project, the Central Reserve Bank (BCR) created the Agrarian Reform Financial Technical Unit (UTFRA), which is responsible for the administration of the Rediscount Line component, by means of the approval and supervision of the credits granted to the Agrarian Reform beneficiaries, through the participating institutions.

The agreement was approved to increase the availability and productive use of credit in the reformed sector. The principal elements of this project are the following: a rediscount line in the Central Reserve Bank (BCR) for production and investment loans to the reformed sector; a training program for agricultural

loan officers; a series of policy studies; a pilot rural savings mobilization program; and administrative support and evaluation. All funds provided for the rediscount line in the BCR to be permanent addition to BCR resources.

As of July 31, 1991, all funds available under the project had been obligated as follows:

<u>Line Item</u>	<u>Grant (US\$ Thousands)</u>
Rediscount line	\$46,111
Long term technical assistance	758
Training	2,012
Studies	641
Saving mobilization	75
A.I.D. Project Administration	232
Evaluation	59
Contingency/Inflation	<u>112</u>
 Total	 \$50,000 =====

The Government of El Salvador agreed to provide counterpart funds for a total equivalent to \$17.0 million; of this amount, \$1.0 million are to be provided by the participating institutions.

C. Counterpart Funds

The grant agreement requires the Government of El Salvador to provide counterpart funds to the Agrarian Reform Financing Project for an amount of \$17,000,000; of this amount \$1,000,000 must be provided by the participating institutions. To the date of this audit, the Government had made available C65.0 million (approximately \$10.9 million) as counterpart to the project. Participating institutions had provided C7.5 million (approximately \$1.3 million) in counterpart to the project.

Direct USAID/El Salvador disbursements were not covered in the scope of the audit.

D. Questionable Costs

An advance payment has not been recapitalized in the Project. Letters of implementation No. 12 and 19, authorized to withdraw an advance payment from 1989 collected interest to be reimbursed until the interest from the credit were collected. This amount was used to cover UTFRA Project expenses. (Equivalent to US\$110,236)

C700,000
=====

This advance was repaid by BCR on March 1992, subsequent to the cut-off day of the audit.

E. Monetary Unit

The fund accountability statement and its notes are expressed in Colones, monetary unit of El Salvador. The Central Reserve Bank (BCR) through the Monetary Board, with agreement No. 18/89, of July 11, 1989, established among its exchange policies, two types of markets to carry out foreign exchange transactions; the fixed market type is the one which is set to the exchange rate of C5.00:US\$1.00; and the banking market, whose type of exchange is flexible and reflects conditions of foreign exchange fluctuation of that market. To July 31, 1991, the rate of exchange was C7.99:US\$1.00.



AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

INTERNAL CONTROL STRUCTURE
INDEPENDENT AUDITORS' REPORT

We have audited the fund accountability statement of the Agrarian Reform Financing Project activities managed by the Central Reserve Bank, USAID/El Salvador Project No. 519-0307, for the period from August 1, 1989 to July 31, 1991, and have issued our report thereon dated June 2, 1992.

Except for not conducting an external quality control review by an unaffiliated organization as further described in our report on the fund accountability statement, we conducted our audit in accordance with generally accepted auditing standards and "Government Audit 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 the Agrarian Reform Financing Project, agreement No. 519-0307 USAID/El Salvador, for the period from August 1, 1989 to July 31, 1991, we considered internal control structure applied by the Central Reserve Bank, in order to determine the auditing procedures necessary for us to express our opinion on the fund accountability statement, and not to provide assurance on the internal control structure.

The management of the Central Reserve Bank (BCR) is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgements 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 allow the preparation of the fund accountability statement in accordance with generally accepted accounting principles. 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 operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories; Books, records and reports, reimbursement (contribution) by AID, and concession and approval of credits.

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

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. 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 judgment, 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.

As described in findings No. 1 through No. 4 of this report, a cooperative did not provide balance confirmation of a credit; deficiencies in the electronic data processing; lack of agricultural supervision reports on credit files; and differences in the interest computing base.

A material weakness is a reportable condition in which the design or operation of the specific elements in the internal control structure 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 reportable conditions described in findings No. 1 through 4 described above are material weaknesses.

This report is intended solely for the information and use of the Central Reserve Bank (BCR) and the U. S. Agency for International Development. This restriction is not intended to limit the distribution of this report, which upon acceptance by the office of the Inspector General, is a matter of public record.

Deloitte Touche Tohmatsu.

June 2, 1992
San Salvador, El Salvador

AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

INTERNAL CONTROL STRUCTURE
FINDINGS

1. Credit Balance without Direct Confirmation Obtained

Condition:

From a test of 23 credits, it was not feasible to obtain the loan confirmation inquiry from Cooperativa El Tránsito, loan disbursed by Banco Capitalizador, due to the fact that the accounting records were updated till March 1992.

Criteria:

Annex II, Section B.5 of the agreement establishes that the Cooperative must keep books and records according to generally accepted accounting principles. These records must be updated so that they may be opportunely reconciled with the bank records.

Cause:

The Cooperative did not employ a full time accountant in the beginning; this person only comes once or twice a week. Additionally, the bank only requires financial statements when it disburses the loan.

Effect:

The lack of updated accounting records from the cooperative originated that the balance could not be confirmed nor determined as correct. The lack of an updated record did not allow an adequate supervision from the Bank officials.

Recommendation:

- A. The Central Reserve Bank (BCR) must request that the participant institutions, as part of the supervision performed through the agronomists, to include balances confirmation and verification of the accounting records of the cooperatives.
- B. The participant institutions must request the cooperatives to keep their records current obtaining periodic financial statements from the cooperatives, and reporting the cases where there is noncompliance to the BCR.

- C. Request the Banco Capitalizador to obtain the confirmation of this cooperative for 1992.

Comments of the Bank:

The management agreed with the delay in preparing accounting reports by some cooperatives pertaining to the reformed sector; but did not consider that this fact could affect the rediscount line.

2. Deficiencies in the Electronic Data Processing

Condition:

We found the following deficiencies in the evaluation of the Central Reserve Bank's Electronic Data Processing Department:

- A. There is no audit trail to determine the personnel who input, review and authorize the information to the credit software.
- B. The credit software also allows automatic updating of transactions into the system manually (not generated by the system), to any one of the users.
- C. There is no rotation of passwords to the credit software. The key is assigned when the credit department requests it from the EDP department, without changing it periodically. Some passwords were authorized in 1987 and 1989 (users code 90 and 030401).
- D. The passwords are not restricted to specific areas into the system.
- E. Physical access to terminals used by the credit department is not restricted.
- F. There is no contingency plan to safeguard the information in case of disaster. The systems department keeps the backup data files in its own installations.
- G. The EDP department of the BCR offers no physical safety for the Bank's hardware or software.
- H. There is no restriction on the number of reports issued.

Criteria:

An adequate internal control structure includes the control environment and the control systems in an electronic data processing environment which provides a reasonable safety that the information is safeguarded against loss through use or unauthorized disposition, and that all the recorded transactions are valid.

Cause:

Generally, there are no EDP policies or procedures which cover the internal control matters in the credit department. The software does not allow certain changes, such as establishing access levels for users, and the installations in the BCR building were not designed to be used for EDP.

Effect:

Weaknesses in EDP may cause errors or irregularities without their being detected, mainly by access to information by unauthorized personnel, and through loss of information that cannot be recovered.

Recommendation:

The Central Reserve Bank (BCR) should establish appropriate controls in its EDP department to protect the contract's records. The changes in the system must include at least:

- A. Documentation procedures to indicate who inputs, reviews, and authorizes each data processing operation.
- B. Make changes in the credit software to include access levels according to the transactions, characteristics and limiting access for manual transactions.
- C. Policies on the rotation of passwords.
- D. A formal recovery plan for the information and safety measures in case of disaster.
- E. Improve the physical safety for the EDP department, and for the physical access to credit department terminals.
- F. Number of copies of each report to be made, and authorized destination of each.

Comments of the Bank:

The Bank is currently working in the EDP area, to modify and implement a new system according with the Bank requirements.

3. Lack of Agricultural Supervision Reports on Credit Files

Condition:

During our review it was not feasible to find field supervision report files of the following credit files:

Capitalizador	CP/0208/FRA	ACRA-EL TRANSITO	C 496,090
	LP/0099/FRA	ACRA-EL SOCORRO	450,000
Mercantil	LP/0092/FRA	ACRA-SAN RAFAEL	
		LA PARADA	<u>651,550</u>
			C1,597,640
			=====

Criteria:

The supervision report is necessary to support the follow-up on the use of funds received by the cooperatives, therefore the adequate use of the credits.

Cause:

Inadequate controls by the intermediary participant institutions originated that the reports were not filed in the respective files.

Effect:

The funds could be used for purposes different from than the established in the agreement.

Recommendation:

The Central Reserve Bank (BCR) is the responsible for the use of funds, should give instructions to the participant institutions about the documentation required to be filed on each record granted under the rediscount line, to support the credits adequately.

Comments of the Bank:

These reports are not filed because the participant institutions are going into liquidation. This could be the reason that the reports are not filed or filed incorrectly by the person responsible, in any case these are investment credits and there exist supervision from Agrarian Reform Financial Technical Unit (UTFRA).

4. Differences in the Interest Computing Base

Condition:

The Central Reserve Bank (BCR) applied a 365 days basis to compute interest calculation. The participant institutions applied a 360 days basis. These calculation were performed for the period between August 1, 1989 through July 31, 1991. It was not possible to estimate the accrued effect.

Criteria:

The same basis of calendar days must be used by the whole banking system to compute interest.

Cause:

As of August 1, 1991, the use of 360 days to compute interest became a policy of the department, without any written authorization being available to support this change.

Effect:

The BCR received less income from interest, while the intermediary bank received more in its collections from the final user, originating differences.

Recommendation:

The Central Reserve Bank (BCR) must establish a policy for the computing of interest, and mechanisms to supervise their compliance. The policy should include standardization with the participant institutions to base computing of interest on 360 days.

Comments of the Bank:

The credit department had applied a 360 days basis for a long time. Starting August 1, 1991 such basis was changed. A recomputation should demand many additional resources due to long period of time transurred.



AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

COMPLIANCE WITH AGREEMENT TERMS, AND
APPLICABLE LAWS AND REGULATIONS REPORT
INDEPENDENT AUDITORS' REPORT

We have audited the fund accountability statement of Agrarian Reform Financing Project activities managed by the Central Reserve Bank, USAID/El Salvador Project No. 519-0307, for the period from August 1, 1989 to July 31, 1991, and have issued our report thereon dated June 2, 1992.

Except for not conducting an external quality control review by an unaffiliated organization as further described in our report on the fund accountability statement, we conducted our audit in accordance with generally accepted auditing standards and "Government Audit 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 agreement No. 519-0307 USAID/El Salvador, is the responsibility of the Central Reserve Bank's management. As part of obtaining reasonable assurance about whether the fund accountability statement is free of material misstatement, we performed tests of Central Reserve Bank's compliance with certain provisions of laws, regulations, contracts and agreement terms. However, our objective was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

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 instances of noncompliance matters.



As described in findings No. 1 and No. 2 of this report, an advance of C700,000 and interests amounting to C36,509 were not capitalized timely.

We considered these material instances of noncompliance in forming our opinion on whether the fund accountability statement of the Agrarian Reform Financing Project for the period from August 1, 1989 to July 31, 1991 is presented fairly, in all material respects, in conformity with the accounting basis used, and this report does not affect our opinion dated June 2, 1992 on the fund accountability statement.

Except as described above, the results of our test of compliance indicate that, with respect to the items tested, Central Reserve Bank 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 Central Reserve Bank had not complied, in all material respects, with those provisions.

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

Deloitte Touche Tohmatsu

June 2, 1992
San Salvador, El Salvador

AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

COMPLIANCE WITH AGREEMENT TERMS, AND
APPLICABLE LAWS AND REGULATIONS REPORT

FINDINGS

1. Advance Payment not Repaid

Condition:

An advance payment of C700,000 was not recapitalized timely in the project; these funds were used for the Agrarian Reform Financial Technical Unit (UTFRA) expenses.

Criteria:

Letter of implementation No. 12 issued in 1989, which was substituted for letter of implementation No. 19, authorized that from 1989 interest an advance payment of C700,000 could be taken, and need not be reimbursed until the interest from the credit are collected.

Cause:

This advance payment was not recapitalized since it was transferred to the UTFRA expense budget for the subsequent years, it was impossible to determine whether this amount has been repaid.

Effect:

Noncompliance with agreement requirements through lack of recapitalization of this advance. Furthermore, the funds could have been used for purposes different from those of the project.

Recommendation:

In future projects the Central Reserve Bank (BCR) must perform opportunely the conditions established in the implementation letters, to avoid penalties from the grantee.

Comments of the Bank:

This advance was recapitalized on February 17, 1992 according to liquidation submitted by the Central Reserve Bank (BCR) and approved by USAID as per implementation letter No. 32, dated March 25, 1992.

2. Interests not Capitalized

Condition:

In the capitalization of interest received to December 31, 1989, there is a difference of C36,509 which was not explained.

Criteria:

According to letter No. 003014 of June 7, 1990, sent by the Central Reserve Bank to AID, and letter of implementation No. 19 of July 12, 1990, the interest which should be capitalized to December 31, 1989, was C5,032,838 and not C4,996,329.

Cause:

The difference of C36,509 not capitalized opportunely is due to the fact that there was no reconciliation of the capitalized amount with the amount indicated in the letter of implementation.

Effect:

Noncompliance with the contract through lack of capitalization of interest, which does not establish a sanction for this noncompliance.

Recommendation:

The Central Reserve Bank (BCR) must establish procedures to assure the compliance with agreement terms, in all operations resulting from project implementation.

Comments of the Bank:

These interests were capitalized on February 17, 1992 according to liquidation submitted by the Central Reserve Bank (BCR) and approved by USAID as per implementation letter No. 32, dated March 25, 1992.

AUDIT OF THE AGRARIAN REFORM FINANCING
USAID/EL SALVADOR PROJECT No. 519-0307
MANAGED BY CENTRAL RESERVE BANK
FOR THE PERIOD FROM AUGUST 1, 1989 TO JULY 31, 1991

LIST OF REPORT RECOMMENDATIONS

INTERNAL CONTROL STRUCTURE

1. Credit Balance without Direct Confirmation Obtained

Recommendation:

- A. The Central Reserve Bank (BCR) must request that the participant institutions, as part of the supervision performed through the agronomists, to include balances confirmation and verification of the accounting records of the cooperatives.
- B. The participant institutions must request the cooperatives to keep their records current obtaining periodic financial statements from the cooperatives, and reporting the cases where there is noncompliance to the BCR.
- C. Request the Banco Capitalizador to obtain the confirmation of this cooperative for 1992.

2. Deficiencies in the Electronic Data Processing

Recommendation:

The Central Reserve Bank (BCR) should establish appropriate controls in its EDP department to protect the contract's records. The changes in the system must include at least:

- A. Documentation procedures to indicate who inputs, reviews, and authorizes each data processing operation.
- B. Make changes in the credit software to include access levels according to the transactions, characteristics and limiting access for manual transactions.
- C. Policies on the rotation of passwords.
- D. A formal recovery plan for the information and safety measures in case of disaster.
- E. Improve the physical safety for the EDP department, and for the physical access to credit department terminals.
- F. Number of copies of each report to be made, and authorized destination of each.

3. Lack of Agricultural Supervision Reports on Credit Files

Recommendation:

The Central Reserve Bank (BCR) is the responsible for the use of funds, should give instructions to the participant institutions about the documentation required to be filed on each record granted under the rediscount line, to support the credits adequately.

4. Differences in the Interest Computing Base

Recommendation:

The Central Reserve Bank (BCR) must establish a policy for the computing of interest, and mechanisms to supervise their compliance. The policy should include standarization with the participant institutions to base computing of interest on 360 days.

COMPLIANCE WITH AGREEMENT TERMS, AND APPLICABLE LAWS AND REGULATIONS

1. Advance Payment not Repaid

Recommendation:

In future projects the Central Reserve Bank (BCR) must perform opportunely the conditions established in the implementation letters, to avoid penalties from the grantee.

2. Interests not Capitalized

Recommendation:

The Central Reserve Bank (BCR) must establish procedures to assure the compliance with agreement terms, in all operations resulting from project implementation.

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