PD-ABG-330

Regional Inspector General for Audit
Tegucigalpa, Honduras

Audit of USAID/Honduras' Small Business II Project Managed by the National Association of Industrialists September 1, 1988 to July 31, 1992

Audit Report No. 1-522-93-26-N
July 16, 1993

Financial information contained in this report may be privileged. The restrictions of 18 USC 1905 should be considered before any information is released to the public.

AGENCY FOR INTERNATIONAL DEVELOPMENT

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

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

TELEPHONES:
32-9987 - 32-3120
FAX No. (504) 31-4465

July 16, 1993

MEMORANDUM

TO: D/USAID/Honduras, Marshall Brown

FROM: RIG/A/T, Lou Mundy

SUBJECT: Audit of USAID/Honduras' Small Business II Project, Managed by the National Association of Industrialists, September 1, 1988 to July 31, 1992

This report presents the results of a financial audit of the Small Business II Project, USAID/Honduras Project No. 522-0241 (Project), managed by the National Association of Industrialists (Association) for the period September 1, 1988 to July 31, 1992. The audit firm of Ernst & Young prepared the report dated June 3, 1993.

The Project budget totals $5.9 million, $4.6 million from A.I.D. funds and $1.3 million from Association counterpart funds. The objectives of the Project were to improve the Association's ability to offer training and technical assistance to client organizations which in turn provide credit, training, and technical assistance directly to entrepreneurs and to enable the Association to broaden its coordination and information network functions among organizations serving small scale enterprises. The Project is scheduled for completion on September 30, 1995. During the period audited, the Association disbursed A.I.D. funds of $1.8 million under the Project.

The objectives of the audit were to determine whether: (1) the Association's fund accountability statements for A.I.D. and counterpart funds, present fairly, in all material respects, the financial position of the Project for the period audited, (2) the Association's internal control structure was adequate to manage the Project, and (3) the Association had complied with agreement terms and applicable laws and regulations. The scope of the audit included

an examination of the Association's activities and transactions to the extent considered necessary to issue a report thereon for the period audited.

Ernst & Young concluded that the fund accountability statements for both A.I.D. funds and for the Association's counterpart funds, present fairly, in all material respects, the Project's receipts and expenditures for the period audited.

Regarding the Association's internal control structure, the auditors identified two material weaknesses. Specifically, the auditors reported that the Association did not: (1) maintain accounting records conducive to an accurate preparation of the fund accountability statements and (2) maintain a separate bank account for A.I.D. Project funds.

With respect to the Association's compliance with agreement terms and applicable laws and regulations, the auditors identified one material instance of noncompliance. The auditors reported that the Association's subagreements with private development organizations were not amended to require annual audits in accordance with the Grant Agreement.

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

Recommendation No. 1

We recommend that USAID/Honduras obtain evidence that the National Association of Industrialists has: (a) developed a control mechanism to prepare accurate fund accountability statements which accurately reflect disbursements made during each reporting period, (b) established policies requiring that A.I.D. Project funds be maintained in a separate account and not commingled with funds from other sources, and (c) amended its subagreements under the Project to ensure annual audits of A.I.D. funds are performed as required by the Grant Agreement.

Recommendation No. 1 can be resolved upon the Mission's presentation of an acceptable firm plan of action to correct the reported deficiencies, and can be closed when it presents acceptable evidence that the required actions have been taken.

b

Regional Inspector General for Audit
Tegucigalpa, Honduras

Audit of USAID/Honduras' Small Business II Project Managed by the National Association of Industrialists September 1, 1988 to July 31, 1992

Audit Report No. 1-522-93-26-N
July 16, 1993

- C'

AUDIT OF THE SMALL BUSINESS II PROJECT
USAID/HONDURAS PROJECT NO. 522-0241.01
MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS
DURING THE PERIOD SEPTEMBER 1, 1988 TO JULY 31, 1992

-d-

AUDIT OF THE SMALL BUSINESS II PROJECT
USAID/HONDURAS PROJECT NO. 522-0241.01
MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS
DURING THE PERIOD SEPTEMBER 1, 1988 TO JULY 31, 1992

TABLE OF CONTENTS

Transmittal Letter and Summary

Background	1
Audit objectives and scope	2
Results of audit	7
Management comments	8

Fund Accountability Statements

Independent Auditor's Report	9
Fund Accountability statement - A.I.D. grant funds	11
Fund accountability statement - Counterpart funds	12
Notes to the fund accountability statements	13

Internal Control Structure

Independent Auditor's Report	17
Findings	21

Compliance with Agreement Terms and Applicable Laws and Regulations

Independent Auditor's Report	25
Findings	28
List of Report Recommendations	30

Appendix I - Management Comments

-Q'

ERNST & YOUNG

Contadores Públicos Autorizados
Apartado 6-891 El Dorado
Panamá, Rep. de Panamá

Teléfonos: 64-2633 - 64-2129
Telefax: 63-7719 - 64-8984

Tegucigalpa, M.D.C.
June 3, 1993

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 USAID/Honduras' Small Business II Project No. 522-0241.01, activities managed by the National Association of Industrialists for the period September 1, 1988 to July 31, 1992.

BACKGROUND

On August 31, 1988, the National Association of Industrialists (ANDI) signed a grant agreement with the Agency for International Development, Honduras Mission (USAID/Honduras) to finance the Small Business II, USAID/Honduras Project No. 522-0241.01.

The purpose of this Project is to strengthen and expand the Small and Microbusiness Program (PYME). ANDI had previously established the PYME to provide institutional support to other Honduran organizations serving small and micro enterprises. Although PYME is part of ANDI and is under ANDI's Board of Directors, PYME has its own committee. This committee is responsible for the Program's direction.

Specific Project objectives are to improve ANDI/PYME's ability to offer training and technical assistance to client organizations which in turn provide credit, training, and technical assistance directly to entrepreneurs, and to enable ANDI/PYME to broaden its coordination and information network functions among the organizations serving small scale enterprises.

Initially, the term for this Project was from September 1, 1988 to July 28, 1993; however according to Amendment No. 6, this term has been extended to September 30, 1995.

The total estimated amount for this Project is $5,943,200. USAID/Honduras was to provide $4,600,000 as grant funds and ANDI $1,343,200 as counterpart funds.

OBJECTIVES AND SCOPE OF THE AUDIT

We were engaged to conduct a financial audit of the activities of the Small Business II Project No. 522-0241.01 managed by the National Association of Industrialists (ANDI) for the period from September 1, 1988 to July 31, 1992.

Our audit was performed in accordance with generally accepted auditing standards and the "Government Auditing Standards" of the U.S. Comptroller General. Therefore, before initiating the field work, our examination included the review of documentation, accounting records, internal control structure and such other auditing procedures as we considered necessary to determine whether they were adequate to conduct our audit and to formulate our auditing approach strategy.

Our audit work included verification of the accounting records to determine whether:

A. The Fund Accountability Statements of A.I.D. grant funds and counterpart funds present fairly, in all material respects, the financial situation of the Project activities managed by ANDI from September 1, 1988 to July 31, 1992, and whether the costs reported as incurred and reimbursed by USAID/Honduras during the period are allowable, allocable, and reasonable in accordance with the terms of the Agreement and applicable laws and regulations.

B. The internal control structure of ANDI is adequate to manage the Project's operations.

C. ANDI complied with agreement terms and applicable laws and regulations that could affect the incurred costs and the Project's goals.

While we planned our examination and prepared the audit programs we were alert to the possible existence of errors or irregularities in accordance with the Statements on Auditing Standards Nos. 53 and 54 of the American Institute of Certified Public Accountants, and to situations or transactions that could be indicative of fraud, abuse, and illegal expenditures and acts.

The major audit procedures applied during our examination were the following:

RECEIPTS

- We confirmed directly with USAID/Honduras the grant funds provided to the Project from July, 1, 1988 to July 31, 1992.

- We verified counterpart contributions from July 1, 1988 to July 31, 1992.

- We analyzed income coming from sources other than those that are part of the Agreement.

- We confirmed directly with the banks the bank account balances as of July 31, 1992.

- We reviewed the bank account reconciliations and followed up of reconciliation items on subsequent months.

- We made a comparative analysis of income to budgeted amounts and obtained explanations on differences.

INSTITUTIONAL SUPPORT

- We verified payrolls through selective sampling.
- We verified the compliance of the Project's Engagement Regulations and promotion and salary increases in accordance with the policies established in the operative plans for each period.
- We made global estimates of salaries for the period under review.
- We verified, through payroll summarization, that actual payroll expenses were included in the implementation reports.

OPERATIONAL EXPENSES

- We evaluated policies and procedures on operational expenses and minor purchases, as well as their review and approval.
- We verified that expenses were made in accordance with the terms of the Agreement and the operational plan.
- We made comparative analyses of actual expenses versus expenses budgeted in the operational plan, and obtained explanations on significant differences.
- We verified on the adequacy of the accounting records.

PROCUREMENT OF FURNITURE AND EQUIPMENT

- We verified the adequacy of the Project's accounting records with relation to procurement costs in comparison with the cost of assets granted, to be sure of correct valuations.
- We reviewed supporting documentation on the procurement of equipment and verified that disbursements were duly authorized and followed the requirements established in the Agreement.

- Through specific tests we verified the compliance with policies established for the accounting of fixed assets as well as for their control and custody.
- On a selective basis we identified Project fixed assets through physical inspections.

TRAINING

- We conducted an evaluation on the procedures and controls applied to this item and on the information network, levels of reviews, authorization and adequate accounting records.
- We examined the supporting documentation for expenditures in this component for amounts higher than L.5,000.
- We examined and verified counterpart contributions.
- We verified that expenditures are in accordance with the terms of the Agreement and the operational plan.

SUPPORT TO PROJECTS

- We examined the agreements and the compliance with the established requirements as well as the levels of review and approval of grant funds.
- We reviewed liquidations submitted by Private Development Organizations (PDO's) on grant funds.
- We examined the correct recording of grant funds in the form of liquidated expenses and advances.
- We analyzed disbursement plans and their compliance.
- We confirmed amounts disbursed to PDO's; however, we could not reconcile differences noted, as PDOs' accounting records were not always reliable.
- We investigated the existence of legal demands or other legal matters pending resolution.

TECHNICAL ASSISTANCE EVALUATION

- We reviewed the manuals and other systems prepared under the technical assistance provided to the Project by the firm Robert Nathan and Associates Inc. These manuals were in the areas of marketing, credit systems, management, administration, information systems and training programs, as well as on the firm's advisory services on the implementation of strategies for small scale enterprises.
- We visited the most important Private Development Organizations (PDO's) receiving funds under the Project and verified the existence and use of handbooks and/or documentation prepared by the Project's Technical Unit as well as the existence and use of software (where applicable) developed by the Project's Technical Unit for these PDOs.
- Through interviews with PDOs' key personnel we obtained information about courses, consulting services or training assistance received from the Project's Technical Unit and/or ANDI/PYME.

RESULTS OF AUDIT

Fund Accountability Statements

In our opinion the Fund Accountability Statements of A.I.D. Grant Funds and Counterpart Funds of the National Association of Industrialists, USAID/Honduras Project No. 522-0241.01 present fairly, in all material respects, the Project's income and expenditures for the period from September 1, 1988 to July 31, 1992, in accordance with the terms of the respective Agreement.

Internal Control Structure

In planning and performing our audit of the Fund Accountability Statements, we considered ANDI's internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the Fund Accountability Statements and not to provide assurance on the internal control structure.

During our audit we observed three reportable conditions involving the internal control structure and its operation. We consider two of these conditions to be material weaknesses.

We also observed certain nonreportable conditions with relation to the control structure that we have communicated to the entity in our letter to management dated January 8, 1993.

Compliance with the Agreement Terms and Applicable Laws and Regulations

As part of obtaining reasonable assurance about whether the Fund Accountability Statements of the National Association of Industrialists, USAID/Honduras Project No. 522-0241.01 from September 1, 1988 to July 31, 1992, are free of material misstatements, we performed tests on whether the entity had complied with the Agreement terms and applicable laws and regulations.

The results of our tests did disclose one material instance of noncompliance that might have an effect on the Project's Fund Accountability Statements.

MANAGEMENT COMMENTS

The entire text of the National Association of Industrialists' comments is included in Appendix I. Those comments exclusively refer to actions taken by the National Association of Industrialists to implement the recommendations of this report.

Ernst & Young

ERNST & YOUNG

Contadores Públicos Autorizados
Apartado 6-891 El Dorado
Panamá, Rep. de Panamá

Teléfonos: 64-2633 - 64-2129
Telefax: 63-7719 - 64-8984

AUDIT OF THE SMALL BUSINESS II
USAID/HONDURAS PROJECT No. 522-0241.01
MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS
DURING THE PERIOD FROM
SEPTEMBER 1, 1988 TO JULY 31, 1992
FUND ACCOUNTABILITY STATEMENTS
INDEPENDENT AUDITOR'S REPORT

We have audited the Fund Accountability Statements of A.I.D. Grant Funds and Counterpart Funds of USAID/Honduras' Small Business II, Project No. 522-0241.01 managed by the National Association of Industrialists (ANDI) from September 1, 1988 to July 31, 1992. These Fund Accountability Statements are the responsibility of ANDI's management. Our responsibility is to express an opinion on these Fund Accountability Statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and except for the matters discussed in the following paragraph, with the United States Controller General's Government Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statements are free of material misstatement. An 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 provides a reasonable basis for our opinion.

We did not have an external quality control review by an unaffiliated audit organization as required by paragraph 46 of

Chapter 3 of the Government Auditing Standards, since no such quality review program is offered by professional organizations in Honduras. 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 Ernst & Young worldwide internal quality control program which requires that Morales Palao William y Asociados, Ernst & Young International be subjected, every three years, to an extensive quality control review by audit partners and managers from other Ernst & Young offices.

As described in Note 1, the Fund Accountability Statements were prepared on the basis of cash received and disbursed, which is a comprehensive accounting basis different to the established by generally accepted accounting principles.

In our opinion, the Fund Accountability Statements of A.I.D. Grant Funds and Counterpart Funds of USAID/Honduras' Small Business II, Project No. 522-0241.01 managed by the National Association of Industrialists present fairly, in all material respects, the Project's receipts and expenditures for the period from September 1, 1988 to July 31, 1992, in accordance with the terms of the respective Agreement.

This report is intended solely for the use of the U.S. Agency for International Development and the National Association of Industrialists. 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.

Ernst & Young

November 27, 1992

AUDIT OF THE SMALL BUSINESS II
USAID/HONDURAS PROJECT No. 522-0241.01
MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS
SMALL AND MICROBUSINESS PROGRAM
DURING THE PERIOD FROM SEPTEMBER 1, 1988 TO JULY 31, 1992

FUND ACCOUNTABILITY STATEMENT
AID GRANT FUNDS
In Lempiras - (Note 1)

RECEIPTS		Budgeted (Note 3)		Executed		Available
Grant Agreement AID 522-0241.01	L.	9,413,615	L.	5,948,550	L.	3,465,065
DISBURSEMENTS						
COORDINATION						
Salaries	L.	1,577,562	L.	1,128,727	L.	448,835
Social benefits		316,518		181,050		135,468
Other administrative exp.		518,370		438,995		79,375
Equipment		84,150		70,229		13,921
DEVELOPMENT OF ENTREPRENEURIAL ASSISTANCE		6,385,250		3,616,849		2,768,401
PDO's RESOURCE TRAINING						
Professional fees		160,000		51,083		108,917
Teaching supplies		74,750		42,768		31,982
Room and board, and snacks		41,500		20,495		21,005
Rent of sites for events		8,200		1,666		6,534
Overtime				6		(6)
Support equipment		16,000		16,309		(309)
Entrepreneurs and Instructors Transportation		7,000				7,000
INSTITUTIONAL INFORMATION NETWORK						
Publications		104,040		104,546		(506)
Data bank		14,500		7,615		6,885
Promotion radio program		27,775		25,062		2,713
EVALUATION AND MONITORING		70,000		28,600		41,400
ENTREPRENEURIAL ASSISTANCE ADVISORY SERVICES		8,000		-		8,000
Total Disbursements		9,413,615		5,734,000		3,679,615
Excess of Receipts over Expenses (Note 4)	L.	-	L.	214,550	L.	(214,550)

AUDIT OF THE SMALL BUSINESS II
USAID/HONDURAS PROJECT No. 522-0241.01

MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS
SMALL AND MICROBUSINESS PROGRAM
DURING THE PERIOD FROM SEPTEMBER 1, 1988 TO JULY 31, 1992

FUND ACCOUNTABILITY STATEMENT
COUNTERPART FUNDS
In Lempiras - (Note 1)

	Budgeted	Executed	Available
Initial Balance	L. -	L. 14,378	L. (14,378)
INCOME			
Income from interest	-	15,549	(15,549)
Income from courses	152,300	79,736	72,564
Income from overhead	633,555	255,295	378,260
Other income	-	31,206	(31,206)
Income from Directories sales	128,650	75,677	52,973
Income from Fair	221,100	315,305	(94,205)
Income from Handbook sales	61,200	7,225	53,975
Assets replacement	-	9,100	(9,100)
Entrepreneurial advisory and assistance services	894,382	572,412	321,970
Contributions from other institutions	1,056,430	833,157	223,273
Total income	3,147,617	2,209,040	938,577
EXPENSES			
Coordination	1,216,082	1,071,427	144,655
Training	318,700	92,088	226,612
Information Network	210,185	33,864	176,321
Entrepreneurial advisory and assistance services	1,393,650	802,865	590,785
Evaluation and monitoring	9,000	1,101	7,899
	3,147,617	2,001,345	1,146,272
Cash available	L. -	L. 207,695	L. (207,695)

AUDIT OF THE SMALL BUSINESS II

USAID/HONDURAS PROJECT No. 522-0241.01

MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS

SMALL AND MICROBUSINESS PROGRAM

DURING THE PERIOD FROM SEPTEMBER 1, 1988 TO JULY 31, 1992

NOTES TO THE FUND ACCOUNTABILITY STATEMENTS

Note 1. SUMMARY OF ACCOUNTING POLICIES

The Fund Accountability Statements of USAID Grant funds and Counterpart funds of USAID/Honduras' Small Business II, Project No. 522-0241.01 managed by the National Association of Industrialists (ANDI) from September 1, 1988 to July 31, 1992 were prepared for the purpose of complying with Section G.3 of the Grant Agreement between USAID/Honduras and ANDI.

The National Association of Industrialists uses the fund accountability system and budgetary execution to report the progress of the Small and Microbusiness Program's (PYME) operations; the significant accounting policies adopted by ANDI/PYME are summarized as follows:

Basis for preparing the financial statements. The attached financial statements have been substantially prepared on a cash basis to record receipts and disbursements, which are recognized when they are received or disbursed, respectively.

Severance compensation to employees. According to the Honduran Labor Code every company and/or institution is subject to pay severance compensation to employees discharged under certain circumstances. ANDI follows the policy of paying according to the Law's stipulations; therefore, disbursements of this nature are recognized as expenses on the dates they are paid.

Monetary unit. The accounting records of ANDI are kept in Honduran Lempiras, the official currency of the Republic of Honduras. The official exchange rate of two Lempiras for one United States Dollar (L. 2.00 = US$ 1.00) had remained constant for many years. In Honduras all foreign exchange transactions have to be channelled through national private banks and/or authorized exchange houses, existing for this purpose an interbank exchange rate, which as of July 31 and November 27, 1992 was L. 5.55 and L. 5.92 for US$ 1.00, respectively.

Note 2. HISTORY AND OPERATIONS OF THE PROJECT

On August 31, 1988, the National Association of Industrialists (ANDI) signed a grant agreement with USAID/Honduras to finance the Small Business II, USAID/Honduras Project No. 522-0241.01.

The purpose of this Project is to strengthen and expand the Small and Microbusiness Program (PYME). ANDI had previously established the PYME to provide institutional support to other Honduran organizations serving small and micro enterprises. Although PYME is part of ANDI and is under ANDI's Board of Directors, PYME has its own committee. This committee is responsible for the Program's direction.

Specific Project objectives are to improve ANDI/PYME's ability to offer training and technical assistance to client organizations which in turn provide credit, training, and technical assistance directly to entrepreneurs, and to enable ANDI/PYME to broaden its coordination and information network functions among the organizations serving small scale enterprises.

Initially, the term for this Project was from September 1, 1988 to July 28, 1993; however according to Amendment No. 6 to the Agreement, this term has been extended to September 30, 1995.

The total estimated amount for this Project is $5,943,200. USAID/Honduras was to provide $4,600,000 as grant funds and ANDI $1,343,200 as counterpart funds. Our audit covered disbursements of grant funds for L.5,734,000 ($1,768,383) and of counterpart funds for L. 2,001,345, through July 31, 1992.

Note 3. BUDGET

Budgeted amounts shown in the Fund Accountability Statements, represent amounts budgeted to December 31, 1992. Our audit, however, covers receipts and expenditures to July 31, 1992.

Counterpart funds of L. 3,147,617 were jointly programmed by USAID/Honduras and the National Association of Industrialists to support the Small and Microbusiness Program for the period September 1, 1988 to July 31, 1992. As shown in the Fund Accountability Statement for Counterpart funds, contributions for this same period amount to L.2,209,040.

Note 4. EXCESS OF RECEIPTS OVER DISBURSEMENTS (A.I.D. GRANT FUNDS)

Excess of the Project receipts over disbursements, as of July 31, 1992, is represented by net assets on the books of the Project as follows:

	LEMPIRAS
Assets:	
Banks	L. 141,068
Outstanding advances	80,582 *
Total assets	L. 222,550
Liabilities:	
Accounts payable	L. 8,000 **
Net assets	L. 214,550

* Amount corresponding to funds delivered in cash to Private Development Organizations unsettled as of the date of the Fund Accountability Statement.

** Amount corresponding to counterpart funds deposited in A.I.D.'s grant fund bank account.

ERNST & YOUNG

Contadores Públicos Autorizados
Apartado 6-891 El Dorado
Panamá, Rep. de Panamá

Teléfonos: 64-2633 - 64-2129
Telefax: 63-7719 - 64-8984

AUDIT OF THE SMALL BUSINESS II

USAID/HONDURAS PROJECT No. 522-0241.01

MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS

SMALL AND MICROBUSINESS PROGRAM

DURING THE PERIOD FROM SEPTEMBER 1, 1988 to JULY 31, 1992

INTERNAL CONTROL STRUCTURE

INDEPENDENT AUDITOR'S REPORT

We have audited the Fund Accountability Statements of A.I.D. Grant funds and Counterpart funds for USAID/Honduras' Small Business II, Project No. 522-0241.01 managed by the National Association of Industrialists from September 1, 1988 to July 31, 1992, and have issued our report thereon dated November 27, 1992.

We conducted our audit in accordance with generally accepted auditing standards and except for not conducting an external quality control review by an unaffiliated audit organization, as described further in our opinion of the fund Accountability Statements, with the United States Controller General's Government Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statements are free of material misstatement.

In planning and performing our audit of the Fund Accountability Statements of A.I.D. Grant funds and Counterpart funds for USAID/Honduras' Small Business II, Project No. 522-0241.01 managed by the National Association of Industrialists from September 1, 1988 to July 31, 1992, we considered the institution's internal control structure in order to determine our auditing procedures for the purpose of expressing our

opinion on the Fund Accountability Statements and not to provide assurance on the internal control structure.

The management of the National Association of Industrialists 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 permit the preparation of Fund Accountability Statements in accordance with generally accepted accounting principles and agreement terms. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projections of any evaluation of the structure to future periods is subject to the risk that procedures might 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 in the following categories:

- Accounting process
- Budgetary process
- Payroll procedures
- Receipts and disbursements
- Fixed assets system

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 have 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 judgement, could adversely affect ANDI's ability to record, process, summarize, and report financial data consistent with the assertions of management in the Fund Accountability Statements. The reportable conditions noted are described under findings Nos. 1 through 3 in the following pages.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure element 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 statements 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 findings Nos. 1 and 2 are material weaknesses.

We also noted other matters involving the internal control structure and its operation which we consider nonreportable

conditions. We have communicated these matters to the management of ANDI in a separate letter dated November 27, 1992.

This report is intended solely for the use of the U.S. Agency for International Development and the National Association of Industrialists. 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.

Ernst & Young

November 27, 1992

AUDIT OF THE SMALL BUSINESS II

USAID/HONDURAS PROJECT No. 522-0241.01

MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS

SMALL AND MICROBUSINESS PROGRAM

DURING THE PERIOD FROM SEPTEMBER 1, 1988 TO JULY 31, 1992

INTERNAL CONTROL STRUCTURE

FINDINGS

1. Accounting records are not conducive to an accurate preparation of the Fund Accountability Statements.

Condition:

During the performance of our auditing work we observed that the Program's accounting records do not show accurately the accumulated expenditures for the period being audited.

Criteria:

Point C., Section 1., Paragraph 2 of Annex 2 to the Grant Agreement, establishes that ANDI shall be responsible for the overall accounting of grant funds and for the submission to USAID/Honduras of proper financial documentation.

Cause:

For reporting purposes, the accounting records showed as expenditures, amounts which have been paid during the reporting period. However, if cash received or disbursed for services rendered or received in prior periods, these expenditures or income are not currently reported.

Effect:

As a result, since the financial reports are prepared on a cash basis of accounting, disbursements made during the reporting period, covering prior period expenditures are not reported.

Recommendation:

ANDI should develop a mechanism of control in order to prepare Fund Accountability Statements capable of showing in an accurate manner all disbursements made by the Program during each reporting period.

2. Project funds are commingled with funds coming from other source.

Condition:

According to the Grant Agreement, the approved method of payment is "cash advances" from USAID/Honduras. During our audit we found that ANDI had deposited into the Project's separate bank account established for A.I.D. funds, amounts representing counterpart contributions.

Criteria:

Standard provisions to the Grant Agreement, section 14.A (a) require that when cash advances are approved, all A.I.D. funds provided to the Project should be maintained in a separate bank account.

Cause:

According to ANDI representatives, due to delays in obtaining reimbursements from USAID/Honduras, funds have had to be "borrowed" from the counterpart account, in order to cover Project expenditures.

Effect:

Project funds are commingled with funds coming from other sources, which prevents the prompt determination of Project funds available for Project implementation.

Recommendation:

ANDI should establish policies requiring that Project funds (A.I.D. grant funds), be maintained in a separate account and not commingled with funds coming from other sources.

3. Certain labor contracts were not signed by both the employee and ANDI

Condition:

Certain personnel contracts were not signed by the employee and/or an ANDI official. The following are examples of this condition:

Date	Description	Deficiency
1988	Marta María Salgado	Not signed by the employee
1991	César Iván Gallardo	Not signed by the employee
1991	Joaquín Medina O.	Not signed by either party
1991	María Leonilda Varela	Not signed by ANDI
1992	Rigoberto Sánchez	Not signed by the employee

Criteria:

ANDI's hiring policies and procedures establish that labor contracts should be signed by both parties (employer and employee) as evidence of acceptance of the contractual stipulations thereby established.

Cause:

ANDI did not fulfill the procedures established for hiring personnel.

Effect:

The lack of signatures on labor contracts of either contracting party could nullify the contracts.

Recommendation:

ANDI should control the timely compliance of contracting procedures governing the employer/employee relationship. (The above mentioned condition has already been rectified by ANDI as of the time of this report, through the rectification of all personnel contracts which were in this condition.)

ERNST & YOUNG

Contadores Públicos Autorizados
Apartado 6-891 El Dorado
Panamá, Rep. de Panamá

Teléfonos: 64-2633 - 64-2129
Telefax: 63-7719 - 64-8984

AUDIT OF THE SMALL BUSINESS II
USAID/HONDURAS PROJECT No. 522-0241.01

MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS
SMALL AND MICROBUSINESS PROGRAM
DURING THE PERIOD FROM SEPTEMBER 1, 1988 TO JULY 31, 1992

COMPLIANCE WITH THE TERMS OF THE AGREEMENT
AND APPLICABLE LAWS AND REGULATIONS

INDEPENDENT AUDITOR'S REPORT

We have audited the Fund Accountability Statements of A.I.D. Grant funds and Counterpart Funds of USAID/HONDURAS' Small Business II, Project No. 522-0241.01 managed by the National Association of Industrialists Program from September 1, 1988 to July 31, 1992, and we have issued our report thereon dated November 27, 1992.

We conducted our audit in accordance with generally accepted auditing standards and except for not conducting an external quality control review by an unaffiliated audit organization, as described further in our opinion of the fund Accountability Statements, with the United States Controller General's Government Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statements are free of material misstatement.

Compliance of laws, regulations, contracts, agreements and mandatory policies and procedures applicable to the National Association of Industrialists is the responsibility of management. As part of obtaining reasonable assurance about whether the Fund Accountability Statements are free of material

misstatement, we performed tests of the National Association of Industrialists' compliance with certain provisions of laws, regulations, contracts, agreements and mandatory policies and procedures. However, our objective was not to provide an opinion on overall compliance with such terms and provisions. Accordingly, we do not express such an opinion.

Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in statutes, regulations, contracts, or grants that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the fund accountability statements. The results of our tests of compliance disclosed one material instance of noncompliance as explained in finding No. 1 in this section.

We considered this material instance of noncompliance in forming our opinion on whether the Fund Accountability Statements of National Association of Industrialists for the period September 1, 1988 to July 31, 1992 is presented fairly, in all material respects, in conformity with the basis of accounting used, and this report does not affect our report dated November 27, 1992.

Except as described above, the results of our tests of compliance indicated that, with respect to the terms tested, the National Association of Industrialistsc complied, in all material respects, with the provisions referred to in the third paragraph of this report. With respect to items not tested, nothing came to our attention that caused us to believe that the National Association of Industrialists has not complied, in all material aspects, with those provisions.

This report is intended solely for the use of the U.S. Agency for International Development and the National Association of Industrialists. 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.

Ernst & Young

November 27, 1992

AUDIT OF THE SMALL BUSINESS II

USAID/HONDURAS PROJECT No. 522-0241.01

MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS

SMALL AND MICROBUSINESS PROGRAM

DURING THE PERIOD FROM SEPTEMBER 1, 1988 TO JULY 31, 1992

REPORT ON COMPLIANCE

FINDINGS

1. Sub-agreements with Private Development Organizations have not been amended to require audits in accordance with Government Auditing Standards.

Condition:

Even though sub-agreements with Private Development Organizations contain a clause indicating that ANDI/PYME and USAID/Honduras have the right to inspect the project's books and records, these agreements have not been amended to require that these sub-recipients be audited annually.

Criteria:

The A.I.D. standard grant provision covering audits, as modified in Fiscal Year 1992, requires that all sub-recipients receiving project funds for $25,000 or more per year, be subject to annual audits in accordance with the standard provision and the "Guidelines for Financial Audits Contracted by Foreign Recipients". This modified standard provision was incorporated into the Agreement by Amendment No. 4 dated April 13, 1992.

Cause:

Lack of an adequate control system over Agreement provisions concerning sub-recipients.

Effect:

Even though some sub-recipients may have periodic audits, these audits are not being performed in accordance with the A.I.D. requirements, therefore, there is no assurance that sub-recipients are complying with agreement terms.

Recommendation:

ANDI should amend its agreements with sub-recipients to require that periodic audits of Project funds are performed, and that these audits comply with A.I.D. requirements.

AUDIT OF THE SMALL BUSINESS II
USAID/HONDURAS PROJECT No. 522-0241.01
MANAGED BY THE NATIONAL ASSOCIATION OF INDUSTRIALISTS
SMALL AND MICROBUSINESS PROGRAM
DURING THE PERIOD FROM SEPTEMBER 1, 1988 TO JULY 31, 1992
LIST OF REPORT RECOMMENDATIONS

RECOMMENDATIONS ON THE INTERNAL CONTROL STRUCTURE

Recommendation No.1

ANDI should develop a mechanism of control in order to prepare Fund Accountability Statement capable of showing in an accurate manner all disbursements made by the Program during each reporting period.

Recommendation No.2

ANDI should stablish policies requiring that the Project funds (A.I.D. grant funds), be maintained in a separate account and not commingled with funds coming from other sources.

Recommendation No. 3

ANDI should control the timaly compliance of contracting procedures governing the employer/employee relationship. (The above mentioned condition has already been rectified by ANDI as of the time of this report, through the rectification of all personnel contracts which were in this condition.)

RECOMMENDATIONS ON COMPLIANCE

Recommendation No.1

ANDI should amend its agreements with sub-recipients to require that periodic audits of Project funds are performed, and that these audits comply with A.I.D. requirements.

APPENDIX I - MANAGEMENT COMMENTS

Asociación Nacional de Industriales de Honduras

TEGUCIGALPA, D. C., HONDURAS, C. A

TELEFONOS: 32-5731 - 32-2221
DIRECCION CABLEGRAFICA: "ANDI"
APARTADO POSTAL 3447
FAX: 31-3520
TELEX: 1632 ANDI HO

NOTA PYME NO.178/93

Junio 14, 1993

Señores
Morales Palao William y Asociados
PRESENTE

Estimados Señores:

Hemos recibido el borrador de la auditoria financiera y hallazgos de la estructura de control interno del programa PYME correspondiente al periodo 1 de septiembre de 1988 al 31 de julio de 1992, mismos que han sido discutidos en la reunión sostenida en las oficinas de USAID conjuntamente con personeros de esa institución, asesores del programa y auditores del RIG sobre el informe encuentran las siguientes observaciones:

Hallazgos No.1

Los registros contables dificultan la preparación oportuna de los Estados de rendición de cuentas.

Observación al hallazgo No.1

El programa cuenta con un sistema de contabilidad mediante el cual se registran partidas y movimiento de cuentas bancarias, generándose los mayores, balance general, estado de resultado consolidado y por fondos y ejecución presupuestaria; la información se obtiene mensualmente bajo un periodo presupuestario anual (12 meses).
La información anterior sirve de base para la preparación mensual de los reportes financieros que son presentados a USAID, requisito indispensable para liquidar valores anticipados por parte de la Agencia, ya que trabajamos en base a anticipos, mismos que son descargados mediante liquidaciones. En cada uno de estos reportes se presenta un resumen de ingresos y egresos que cubre la vida del proyecto PYME II etapa a través de la cual se refleja la situación total de los fondos de donación.

Durante la auditoría realizada por la firma MORALES PALAO WILLIAM Y ASOCIADOS para el período septiembre/88 a julio/92 se solicitó un Estado de Rendición de cuentas acumulado para el período auditado tanto de los fondos USAID como de fondos de contraparte, información que se preparó para ambos fondos, mostrándose cierto grado de dificultad para los fondos de contraparte ya que ésta nunca había sido preparada y la dificultad encontrada se generó al momento de consolidar dicha información.

Lo anterior ha servido de experiencia para la administración del PYME, ya que a partir de 1993 se prepararán estados de rendición de cuenta anuales por fondo con el propósito de facilitar esta labor a futuras auditorías o informes requeridos por la Agencia donante, de existir algún otro tipo de reportes aceptable por USAID, que faciliten esta labor les agradeceremos nos lo den a conocer para ser implementados en el proyecto.

2. <u>Hallazgos No.2</u>

Uso inapropiado de la cuenta bancaria destinada para fondos de donación de USAID.

<u>Observaciones al Hallazgo No.2</u>

Desde que el Programa PYME II (etapa) inició operaciones se procedió a la apertura de una cuenta bancaria para uso exclusivo de los fondos USAID y los fondos de contraparte se manejan en cuentas diferentes. La administración del programa se ha visto forzada a efectuar transferencias en calidad de **"préstamos interfondos"** de los fondos propios a la cuenta de fondos de USAID debido a que trabajamos en base a anticipos por parte de USAID y estos requieren como mínimo 30 días para ser entregados al PYME, el proyecto a su vez debe liquidar los fondos ya anticipados para que sean descargados y tener derecho a un nuevo anticipo situación que alarga el perído de disponibilidad de fondos en la cuenta y motiva que se soliciten préstamos a otros fondos para no parar las actividades propias del proyecto.

Consideramos que no es prudente efectuar gastos de otras cuentas y que corresponden a partidas que son sufragadas por USAID ya que estas no podrían ser reportadas a USAID hasta que ésta desembolse y a su vez nosotros reintegremos sino a la cuenta que generó el préstamo, lo anterior mostraría una situación que no es real en los fondos de USAID y en los fondos propios.

Consideramos que la recomendación emanada por esa firma no es aplicable ya que no es a través de reglamentos que solucionaremos la causa del problema ya que es producto del sistema de operación de los fondos USAID al cual estamos sujetos.

3. Hallazgo No.3

Ciertos contratos laborales no fueron firmados por empleados ni por ANDI.

Observaciones al Hallazgo No.3

Esta recomendación ya fue enmendada.

Asimismo damos respuesta al hallazgo de cumplimiento según se describe así:

Hallazgo

Los subconvenios firmados con las organizaciones Privadas de Desarrollo no han sido modificadas según los requerimientos de acuerdo con normas de auditoría gubernamental.

Observación

De acuerdo a los convenios firmados entre las OPDs y ANDI-PYME existe la cláusula No.11.3.9 que textualmente dice:

"Para asegurar el cumplimientos de los requisitos del convenio incluyendo los costos, la OPD deberá mantener registros adecuados concernientes a las transacciones bajo el convenio y los pondrá a disposición de los respectivos representates autorizados de la ANDI y/o AID para su inspección y auditoría durante el término del convenio y hasta por un período de 3 años después de la fecha del último pago de convenio".

Adicionalmente a la cláusula anterior incluida en cada convenio se incluye en las **"cartas de compromiso"** que son firmadas entre personeros de la Junta Directiva y Directores de cada OPD, un punto en el que se comprometen a ser auditados sus estados financieros en su conjunto además de los fondos del proyecto, esta estipulación ha venido siendo implementada a partir del año 1992.

Los requerimientos adicionales por parte de USAID, a lo señalado anteriormente serán aplicados a las auditorías correspondientes al año 1993.

Esperamos que con la información aquí ofrecida se aclaren los hallazgos derivados de la revisión financiera realizada por esa firma al Programa PYME de la ANDI.

Atentamente,

ANDI
Programa PYME

LIC. DORCAS C. DE GONZALEZ
DIRECTORA EJECUTIVA
PROGRAMA ANDI/PYME

c.c.: Lic. Bernai Velarde
AID

Ing. Felipe Peraza
Presidente Comité PYME

Lic. Hilario Hooker
UTP

Administración PYME

arch.

MVL/emr

APPENDIX I

REPORT DISTRIBUTION

U.S. Ambassador to Honduras	1
D/USAID/Honduras	5
AA/LAC	2
LAC/CEN	1
XA/PR	1
LEG	1
GC	1
AA/OPS	1
AA/FA	1
FA/FM	1
POL/CDIE/DI	1
FA/MC	1
IG	1
AIG/A	1
AIG/I&S	1
IG/A/PPO	2
IG/LC	1
IG/RM/GS	5
IG/A/FA	1
IG/A/PSA	1
RIG/A/EUR/W	1
RIG/A/Bonn	1
RIG/A/Cairo	1
RIG/A/Dakar	1
RIG/A/Nairobi	1
RIG/A/Singapore	1