

PD-ABL-928

**Regional Inspector General for Audit
San José, Costa Rica**

**Audit of USAID/Peru's
Upper Huallaga Area Development Project
Activities Managed by the
Upper Huallaga Special Project Office
April 1, 1990 to December 31, 1992**

**Audit Report No. 1-527-95-16-N
September 18, 1995**



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
OFFICE OF THE REGIONAL INSPECTOR GENERAL
SAN JOSE, COSTA RICA

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September 18, 1995

MEMORANDUM

TO: Director USAID/Peru, George Wachtenheim

FROM: RIG/A/San Jose, *Richard B. Howard*
Wayne J. Watson
WJW

SUBJECT: Audit of USAID/Peru's Upper Huallaga Area Development Project Activities, Managed by the Upper Huallaga Special Project Office, April 1, 1990 to December 31, 1992

This report presents the results of a financial audit of the Upper Huallaga Area Development Project, USAID/Peru Project No. 527-0244, managed by the Upper Huallaga Special Project Office (the Office) of the Government of Peru, for the period April 1, 1990 to December 31, 1992. The accounting firm of Hansen-Holm, Alonso & Co. prepared the report dated December 20, 1994.

The purpose of the project is to develop and apply agricultural production packages and to strengthen public sector agricultural support services in coordination with the Peruvian coca eradication program in the Upper Huallaga region. The project finances activities in the areas of research, extension, training, agricultural credit, agricultural production services, resources information, road maintenance, and community development.

The objectives of the audit were to determine whether: (1) the fund accountability statement presents fairly, in all material respects, the financial situation of the project activities managed by the Office for the period April 1, 1990 to December 31, 1992; and expenses reported as incurred and reimbursed by USAID/Peru are allowable, allocable, and reasonable in accordance with agreement terms, and applicable laws and regulations, (2) the internal control structure of the Office was adequate to manage the project's activities, and (3) the Office complied, in all material respects, with agreement terms and applicable laws and regulations which

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may have a material affect on the project's goals and incurred costs. The scope of the audit included an examination of the Office's activities and transactions to the extent considered necessary to issue a report thereon for the period audited. The audit included coverage of \$5,504,189 of USAID/Peru disbursements to the project during the audited period as well as \$175,512 in commodities and technical assistance directly procured by USAID/Peru.

Hansen-Holm, Alonso & Co. was of the opinion that the fund accountability statement presents fairly, in all material respects, the financial position of the project for the audit period.

With respect to the Office's internal control structure, the auditors identified three reportable conditions: (1) insufficient controls over fixed assets and inventories, (2) lack of directives for compliance with USAID regulations, and (3) non-implementation of budget and financial controls.

Regarding compliance with agreement terms and applicable laws and regulations, the auditors noted no material instances of noncompliance.

The draft report was discussed with representatives from the Office who expressed concurrence with the audit findings and recommendations.

The project ended December 31, 1993, and according to USAID/Peru officials, the entity was dissolved upon completion of the project. Therefore, we are not recommending any action to correct procedural deficiencies identified by the auditors with respect to the Office's internal control structure.

This final audit report is being transmitted to you for your information.

**Regional Inspector General for Audit
San José, Costa Rica**

**Audit of USAID/Peru's
Upper Huallaga Area Development Project
Activities Managed by the
Upper Huallaga Special Project Office
April 1, 1990 to December 31, 1992**

**Audit Report No. 1-527-95-16-N
September 18, 1995**

**AUDIT OF THE
UPPER HUALLAGA AREA DEVELOPMENT PROJECT
USAID/Peru Project No. 527-0244
ACTIVITIES MANAGED BY
THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
April 1, 1990 to December 31, 1992**

**AUDIT OF THE
UPPER HUALLAGA AREA DEVELOPMENT PROJECT
USAID/Peru Project No. 527-0244
ACTIVITIES MANAGED BY
THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
April 1, 1990 to December 31, 1992**

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January 16, 1995

Mr. Coinage N. Gothard
REGIONAL INSPECTOR GENERAL FOR AUDIT
UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT
San Jose, Costa Rica

Dear Mr. Gothard:

This report presents the results of our financial audit of the Upper Huallaga Area Development Project, USAID/Peru Project No. 527-0244, managed by Upper Huallaga Special Project Office for the period April 1, 1990 to December 31, 1992.

BACKGROUND

On September 15, 1981, the Government of the United States of America, acting through the Agency for International Development Mission to Peru (USAID/Peru), and the Government of Peru (GOP), represented by its Ministry of Economy, Finance and Commerce, signed an agreement to develop the Upper Huallaga Area Development Project.

On December 1981, an office named the Upper Huallaga Special Project Office (PEAH) was created for its implementation. This office manages and coordinates the project activities and resources.

PEAH operates under the authority of the National Development Institute (Instituto Nacional de Desarrollo - INADE) and the Ministry of the Presidency of the Government of Peru.

The purpose of the project is to develop and apply agricultural production packages and to strengthen public sector agricultural support services in coordination with the Peruvian coca eradication program in the Upper Huallaga region.

Because the project is being implemented in a coca-based economy, it has experienced a number of implementation obstacles, including the difficult security situation in the Upper Huallaga Valley. These factors have caused some reduction or limitation in the presence of public institutions in the valley, thereby forcing PEAH to assume the role of main implementor.

PEAH has six offices: a central office located in Tingo Maria, four offices located in Aucayacu, Juanjuí, Tarapoto and Tocache, and a coordination and linking office located in Lima.

SUBAGREEMENTS

To develop the project's activities, PEAH has signed agreements with different public entities providing them financial resources in order to strengthen their operative capacity according to project objectives.

PERIOD OF THE AGREEMENT

The period of the agreement is from September 15, 1981 to December 31, 1993.

FINANCIAL PLAN

The financial plan of the project is the following:

(Expressed in US\$ 000)

	<u>LOAN</u>	<u>GRANT</u>	<u>COUNTER-PART</u>	<u>TOTAL</u>
Research	1,452	1,838	2,056	5,346
Extension	2,207	2,793	2,848	7,848
Training	912	1,087	723	2,722
Agricultural credit	3,013	175	1,200	4,388
Agricultural production services	784	299	254	1,337
Resources information	300	501	474	1,275
Road Maintenance	3,792	2,880	3,601	10,273
Community development	732	2,071	1,260	4,063
Project office	1,808	1,060	575	3,443
Audit evaluation	-	196	-	196
Others	-	-	867	867
	<u>15,000</u>	<u>12,900</u>	<u>13,858</u>	<u>41,758</u>

Research

The project finances activities designed to develop the human resources of institutions involved in agricultural research, extension, and training in the project area.

Extension

The extension component facilitates the adoption of new farming methods developed under the research program.

Training

The objective of the training program is to strengthen the capacity of the National Agrarian University of the Jungle (UNAS) to train professionals with appropriate skills for employment in the Upper Huallaga Valley.

Agricultural credit

The project establishes an agricultural credit program for the project area implemented through the Agrarian Bank and BANCOOP (a cooperative rural financial institution).

Farm production services

The project finances activities in land registration, input and output marketing, and agroindustrial promotion.

Resources information

The objective of this component is to provide a continual flow of information to project managers to assist them in implementation.

Road maintenance

The objective of this component is to maintain and repair roads in the project area.

Community development

The community development component supports the improvement of essential community services in the project area. These services include potable water systems, small irrigation canals, health care and public markets.

Project Office

Comprises the establishment and operation of the Special Project Office in Tingo María (until 1992, the PEAH was based in an encampment in the Aucayacu zone) including the purchase of equipment and personnel expenses.

AUDIT OBJECTIVES AND SCOPE

OBJECTIVES

We were engaged to perform a financial audit of the Upper Huallaga Area Development Project, USAID/Peru Project No. 527-0244, activities managed by the Upper Huallaga Special Project Office (PEAH) for the period April 1, 1990 to December 31, 1992. Our audit was performed in accordance with generally accepted auditing standards and the "Government Auditing Standards" issued by the Comptroller General of the United States. Accordingly, it included such tests of the accounting records and such other auditing procedures as we considered necessary to determine whether:

- The fund accountability statement presents fairly, in all material respects, the financial situation of the project activities managed by PEAH for the period April 1, 1990 to December 31, 1992; and expenses reported as incurred by PEAH and reimbursed by USAID/Peru during this period are allowable, allocable, and reasonable in accordance with the agreement terms and applicable laws and regulations.
- The internal control structure of PEAH is adequate to manage its operations under the project.
- PEAH complied, in all material respects, with agreement terms and applicable laws and regulations that could have a material effect on the project's goals and incurred costs.
- PEAH has taken adequate corrective actions on recommendations from prior audits.

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

SCOPE

The scope of our work consisted of the following activities:

Obtaining project information

In this stage we obtained a sufficient understanding of the project's activities, control environment, accounting system and controls, information system, agreement terms, and laws and regulations applicable to the project.

For that purpose we held working meetings with officers in charge of the project and reviewed the following documents:

- The "Project Paper".
- Project agreement between USAID/Peru and Government of Peru including amendments and mandatory standard provisions.

- Subagreements between PEAH and other institutions.
- Contracts and subcontracts with third parties.
- Annual operating plans.
- Budgets, liquidations, project implementation letters, and written procedures approved by USAID/Peru to manage the project.
- Reports of evaluation and physical and financial progress of the project.
- Office of Management and Budget (OMB) Circulars A-110 and A-122.
- Federal and A.I.D. Acquisition Regulations.
- A.I.D. Handbook 13, "Grants".
- A.I.D. Handbook 11 "Country Contracting", Chapter 4.
- PEAH's chart of accounts, organization charts, and procedures for reception, storage and distribution of materials and equipment.

Examination of the fund accountability statement

Our examination of the fund accountability statement was performed in accordance with generally accepted auditing standards and the "Government Auditing Standards" of the Comptroller General of the United States and, accordingly, included such tests of the accounting records and other auditing procedures as we considered necessary in the circumstances.

We applied tests as we considered appropriate for the purpose of expressing our opinion on the fund accountability statement. For this purpose we paid special consideration to the effectiveness of the accounting and internal control procedures established by the project's management, emphasizing the following aspects:

- Review the budgeted amounts by category and major items; the costs reported as incurred by PEAH during the period April 1, 1990 to December 31, 1992, and the amounts received from USAID/Peru during that period.
- Evaluate project implementation actions and accomplishments to determine whether costs incurred are allowable, allocable and reasonable under the agreement terms and to identify areas where inadequate controls could exist.
- Identify and quantify questionable costs, which are presented in two separate categories: (1) questioned costs which are explicitly ineligible because they are not project related, unreasonable or prohibited by the agreement or applicable laws and regulations, and (2) unsupported costs that are not supported with adequate documentation or did not have required prior approvals or authorizations.
- Determine that amounts received from USAID/Peru less the costs incurred, after considering any accruals, reconcile with the balance in banks.
- Determine if counterpart contributions have been provided in accordance with the agreement.

- Verify that direct A.I.D. procurement is accounted for and control procedures exist to adequately safeguard such assets.

Review and evaluation of the internal control structure

We reviewed and evaluated PEAH's internal control structure to obtain a sufficient understanding of the design of relevant control policies and procedures and whether those policies and procedures have been placed in operation.

The evaluated categories include but are not limited to the adequacy of the accounting and information systems, legal and regulatory aspects, receipts and custody of funds, controls on liquidations related to the procurement and payment of goods and services, fixed assets controls, and controls to assure that charges to the project are proper and supported.

In obtaining our understanding of the internal control structure and assessing control risk, we followed, at a minimum, the AICPA statements on auditing standards Nos. 55 and 60.

Compliance with agreement terms and applicable laws and regulations

We determined whether PEAH has complied, in all material respects, with agreement terms, project implementation letters, and applicable laws and regulations. For this purpose, we followed, at a minimum, AICPA statement on auditing standards No. 68.

Follow-Up on prior audit recommendations

We evaluated the actions taken on findings and recommendations reported in prior audits to determine whether prompt and appropriate corrective actions have been taken by PEAH officials.

Results of the audit

• Fund accountability statement

The fund accountability statement was prepared on the basis of cash receipts and disbursement, which is a comprehensive basis of accounting other than generally accepted accounting principles. In our opinion, the fund accountability statement for the period April 1, 1990 to December 31, 1992 presents fairly, in all material respects, the financial situation of the project activities managed by the Upper Huallaga Special Project Office (PEAH); and the costs reported as incurred by PEAH and reimbursed by USAID/Peru during the period are allowable, allocable, and reasonable in accordance with agreement terms and applicable laws and regulations which may affect the project's goals and incurred costs.

- **Internal control structure**

In planning and performing our audit of the fund accountability statement, we considered the internal control structure implemented by PEAH to determine our auditing procedures for the purpose of expressing an opinion on the fund accountability statement.

Our evaluation of the internal control structure included the control systems of the following categories:

- Legal and regulatory aspects
- Accounting and financial aspects
- Treasury (receipt and custody of funds)
- Liquidations (including procurement and payment for goods and services)
- Payrolls
- Fixed assets

We noted certain matters involving the internal control structure and its operation which we consider reportable conditions under standards established by the American Institute of Certified Public Accountants:

- Insufficient controls over fixed assets and inventories.
- No directives for compliance with USAID regulations.
- Non-implementation of budget and financial controls.

Also, we noted other matters involving the internal control structure and its operation that we have reported to the management of PEAH in a separate letter.

- **Compliance with agreement terms and applicable laws and regulations**

As part of obtaining reasonable assurance as to whether the fund accountability statement is free of material misstatement, we performed tests to obtain reasonable assurance that PEAH complied with agreement terms and applicable laws and regulations which may affect the project's goals and incurred costs.

The results of our tests of compliance indicate that, with respect to the items tested, PEAH complied, in all material respects, with agreement terms and applicable laws and regulations that could affect the project's goals and incurred costs. With respect to items not tested, nothing came to our attention that caused us to believe that PEAH had not complied, in all material respects, with those provisions. However, we observed some immaterial instances of noncompliance which were presented to the management of PEAH in a separate letter.

- **Follow up on recommendations from previous audits**

Our review determined that PEAH has implemented recommendations from the previous audit of its activities under the project covering the period September 15, 1981 to March 31, 1990.

Management comments

This report has been discussed with PEAH's Executive Direction, which is in general agreement with the contents of this report.

PEAH's Executive Direction made the following comment:

"We have received your final draft with regard to the financial audit of Upper Huallaga Area Development Project USAID/PERU No.527-0244. We have read this report thoroughly and we agree with its contents".



Eduardo Villalobos D. (Partner)
Peruvian Public Accountant
Matriculation No. 852



**AUDIT OF THE UPPER HUALLAGA AREA DEVELOPMENT PROJECT
ACTIVITIES MANAGED BY THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
USAID/Peru Project No. 527-0244**

**Report on the Fund Accountability Statement
for the period April 1, 1990 to December 31, 1992**

INDEPENDENT AUDITORS' REPORT

We have audited the fund accountability statement of the Upper Huallaga Area Development Project, USAID/Peru Project No. 527-0244, activities managed by the Upper Huallaga Special Project Office (PEAH) for the period April 1, 1990 to December 31, 1992. The fund accountability statement is the responsibility of the management of the Upper Huallaga Special Project Office. Our responsibility is to express an opinion on the 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 the "Government Auditing Standards" issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the fund accountability statement is free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the fund accountability statement, and 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.

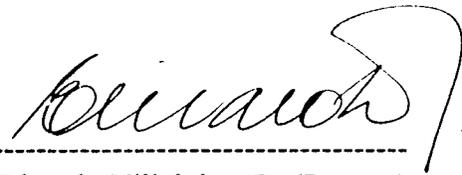
We did not have an external quality control review of our audit work by an unaffiliated audit organization as required by paragraph 46 of chapter 3 of "Government Auditing Standards" since no such quality review program is offered by professional organizations in Peru. We believe that the effect of this departure from the financial audit requirements of the "Government Auditing Standards" is not material because we participate in the Coopers & Lybrand worldwide internal quality control program which requires our office in Peru to be subjected, each three years, to an extensive quality control review by partners and managers from other Coopers & Lybrand Offices.

As described in Note 2, the fund accountability statement was prepared on the basis of cash receipts and disbursements which is a comprehensive basis of accounting other than generally accepted accounting principles.

In our opinion, the fund accountability statement audited by us presents fairly, in all material respects, the income received and the costs incurred by the Upper Huallaga Special Project Office and reimbursed by USAID/Peru, and the commodities and technical assistance directly procured by USAID/Peru under the Upper Huallaga Area Development Project for the period April 1, 1990 to December 31, 1992, in accordance with the basis of accounting described in Note 2.

This report is intended for the information of the Upper Huallaga Special Project Office and the United States Agency for International Development. However, upon acceptance by the USAID Office of the Inspector General, this report becomes a matter of public record and its distribution is not limited.

December 20, 1994



Eduardo Villalobos D. (Partner)
Peruvian Public Accountant
Matriculation No. 852



**AUDIT OF THE UPPER HUALLAGA AREA DEVELOPMENT PROJECT
 ACTIVITIES MANAGED BY THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
 USAID/Peru Project No. 527-0244**

**Fund Accountability Statement
 for the period April 1, 1990 to December 31, 1992
 (Expressed in US dollars)**

	BUDGET	ACTUAL	AVAILABLE	QUESTIONED COSTS	
				INELIGIBLE	UNSUPPORTED
REVENUE					
Loan	351,882	351,882	-		
Grant	5,152,307	5,152,307	-		
Total revenue	<u>5,504,189</u>	<u>5,504,189</u>	<u>-</u>		
INCURRED COSTS					
Research					
Loan	-	-	-	-	-
Grant	148,445	148,445	-	-	-
	<u>148,445</u>	<u>148,445</u>	<u>-</u>	<u>-</u>	<u>-</u>
Extension					
Loan	17,500	17,500	-	-	-
Grant	2,097,920	2,089,856	(8,064)	-	-
	<u>2,115,420</u>	<u>2,107,356</u>	<u>(8,064)</u>	<u>-</u>	<u>-</u>
Training					
Loan	-	-	-	-	-
Grant	205,031	204,755	(276)	-	-
	<u>205,031</u>	<u>204,755</u>	<u>(276)</u>	<u>-</u>	<u>-</u>
Farm production services					
Loan	-	-	-	-	-
Grant	20,333	20,333	-	-	-
	<u>20,333</u>	<u>45,870</u>	<u>-</u>	<u>-</u>	<u>-</u>
Resource information					
Loan	-	-	-	-	-
Grant	113,128	113,077	(51)	-	-
	<u>113,128</u>	<u>113,077</u>	<u>(51)</u>	<u>-</u>	<u>-</u>
Road Maintenance					
Loan	334,382	334,382	-	-	-
Grant	1,593,269	1,593,269	-	-	-
	<u>1,927,651</u>	<u>1,927,651</u>	<u>-</u>	<u>-</u>	<u>-</u>

**AUDIT OF THE UPPER HUALLAGA AREA DEVELOPMENT PROJECT
 ACTIVITIES MANAGED BY THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
 USAID/Peru Project No. 527-0244**

**FUND ACCOUNTABILITY STATEMENT (cont'd)
 for the period April 1, 1990 to December 31, 1992
 (Expressed in US dollars)**

	<u>BUDGET</u>	<u>ACTUAL</u>	<u>AVAILABLE</u>	<u>QUESTIONED COSTS</u>	
				<u>INELIGIBLE</u>	<u>UNSUPPORTED</u>
Community development					
Loan	-	-	-	-	-
Grant	791,525	791,525	-	-	-
	<u>791,525</u>	<u>791,525</u>	<u>-</u>	<u>-</u>	<u>-</u>
Project office					
Loan	-	-	-	-	-
Grant	182,656	182,656	-	-	-
	<u>182,656</u>	<u>182,656</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total incurred costs	<u>5,504,189</u>	<u>5,495,798</u>			
Outstanding fund balance (Note 5)		<u>8,391</u>	(8,391)	-	-
<u>COMMODITIES/TECHNICAL ASSISTANCE</u>					
<u>DIRECTLY PROCURED BY AID</u>					
Technical assistance					
Loan	-	-	-	-	-
Grant		129,642		-	-
		<u>129,642</u>		<u>-</u>	<u>-</u>
Equipment (Note 4)					
Loan		12,473		-	-
Grant		33,397		-	-
		<u>45,870</u>		<u>-</u>	<u>-</u>
Total commodities/technical assistance procured by AID		<u>175,512</u>			
Total questioned costs				<u>-</u>	<u>-</u>

**AUDIT OF THE UPPER HUALLAGA AREA DEVELOPMENT PROJECT
 ACTIVITIES MANAGED BY THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
 USAID/Peru Project No. 527-0244**

**SCHEDULE OF COUNTERPART CONTRIBUTIONS
 from April 1, 1990 to December 31, 1992
 (Expressed in US dollars)**

<u>COMPONENTS</u>	<u>BUDGET</u>	<u>ACTUAL</u>	<u>QUESTIONED</u>
Research	193,578	193,578	
Extension	1,524,513	1,524,513	
Training	247,926	247,926	
Agricultural credit	2,010,960	2,010,960	
Farm production services	263,725	263,938	
Resource information	335,083	334,866	
Road maintenance	4,113,488	4,113,488	
Community development	1,329,981	1,329,981	
Project Office	889,521	889,525	
Total	<u>10,908,775</u>	<u>10,908,775</u>	<u>-</u>

**AUDIT OF THE UPPER HUALLAGA AREA DEVELOPMENT PROJECT
ACTIVITIES MANAGED BY THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
USAID/Peru Project No. 527-0244**

**Notes to the Fund Accountability Statement
for the period April 1, 1990 to December 31, 1992**

1. NATURE OF ACTIVITIES

The Upper Huallaga Special Project Office (PEAH), is the responsible entity for the management of the project's activities and resources. Project activities are developed directly by PEAH, as well as by different public entities which have signed agreements with PEAH.

2. SIGNIFICANT ACCOUNTING PRACTICES

Except for an insignificant amount (US\$ 25,171) of expenses as reflected in Note 5, which expenses were recorded in advance of their actual cash expenditure, the fund accountability statement was prepared on the basis of cash receipts and disbursements.

In accordance with Peruvian legislation, the accounting transactions are recorded in local currency. The amounts in US dollars shown in the fund accountability statement are translated on a first-in-first-out basis applying the exchange rate in force at the date of the applicable remittance of funds. These translated amounts have been compared with the accounting records of USAID/Peru, resulting some insignificant differences, attributable to the exchange rates used by each entity, considering the date of recording the transactions.

3. EXCHANGE RATES

The exchange rates used to translate the amounts reported in the fund accountability statement are the following:

Months	Monthly average exchange rates Nuevos Soles for US\$		
	Años		
	1990 *	1991	1992
January	-	0.54	1.00
February	-	0.55	0.98
March	-	0.56	0.96
April	0.03	0.64	1.03
May	0.04	0.80	1.14
June	0.07	0.85	1.19
July	0.12	0.83	1.24
August	0.32	0.80	1.29
September	0.43	0.80	1.38
October	0.44	0.92	1.56
November	0.44	1.03	1.62
December	0.50	1.00	1.64

* During 1990, the local currency was the Inti(1,000,000 intis = 1 nuevo sol).

4. EQUIPMENT DIRECTLY PROCURED BY USAID/PERU IN THE PERIOD APRIL 1, 1990 TO DECEMBER 31, 1992 BUT ACCOUNTED FOR DURING SUBSEQUENT YEARS

	US\$	COMMENT
<u>Loan fund</u>		
. Equipment and supplements G. and V. Export	12,253	Accounted for in 1994
. Transformers, AUDAX S.A.	220	Accounted for in 1994
	<u>12,473</u>	
<u>Grant fund</u>		
. 5 computers with printers, software and supplements, G. and V. Export	25,265	Accounted for in 1993
. 2 computers with software and supplements, PC Business Solution	8,082	Accounted for in 1994
. Spare parts PC, Comercial de sistemas	50	Accounted for in 1994
	<u>33,397</u>	

5. RECONCILIATION OF FUND ACCOUNTABILITY STATEMENT BALANCE AT DECEMBER 31, 1992 WITH CASH ON HAND AND IN BANKS

	<u>US\$</u>
Balance in Banco de la Nacion account No.490-001972 at 12.31.92	33,562
<u>Expenses of zone offices recorded in advance of their cash payment:</u>	
"Tocache" zone	(15,000)
"Mariscal Caceres" zone	(6,000)
"Leoncio Prado" zone	(4,171)
	<u>8,391 (*)</u>

* Transferred to 1993 budget with Execution Letter No. 99 of September 7, 1993.

6. LIFE OF PROJECT COUNTERPART CONTRIBUTIONS THROUGH DECEMBER 31, 1992

The Government of Peru's cumulative life of project counterpart contributions to the Upper Huallaga Area Development Project as of December 31, 1992 were as follows:

(Expressed in US dollars)

Components	Periods		Total
	15/09/81 to 31/03/90	01/04/90 to 31/12/92	
Research	1,294,883	193,578	1,488,461
Extension	1,796,313	1,524,513	3,320,826
Training	638,530	247,926	886,456
Agricultural credit	40,527	2,010,960	2,051,487
Farm Production Services	313,044	263,938	576,982
Resource information	441,145	334,866	776,011
Road maintenance	2,565,205	4,113,488	6,678,693
Community development	1,272,876	1,329,981	2,602,857
Project office	1,745,363	889,525	2,634,888
	<u>10,107,886</u>	<u>10,908,775</u>	<u>21,016,661</u>

**7. CUMULATIVE FUND ACCOUNTABILITY STATEMENT (USAID FUNDS) FOR
THE PERIOD SEPTEMBER 15, 1981 TO DECEMBER 31, 1992**

For the periods September 15, 1981 through March 30, 1990
and April 1, 1990 through December 31, 1992
(Expressed in US dollars)

	<u>BUDGET</u>	<u>ACTUAL</u>	<u>AVAILABLE</u>
<u>REVENUE</u>			
Loan	11,428,061	11,428,061	-
Grant	6,623,938	6,623,938	-
Total revenue	<u>18,051,999</u>	<u>18,051,999</u>	<u>-</u>
<u>INCURRED COSTS</u>			
<u>RESEARCH</u>			
Loan	1,172,042	1,172,042	-
Grant	153,965	153,965	-
	<u>1,326,007</u>	<u>1,326,007</u>	<u>-</u>
<u>EXTENSION</u>			
Loan	1,448,038	1,448,038	-
Grant	2,426,528	2,418,464	(8,064)
	<u>3,874,566</u>	<u>3,866,502</u>	<u>(8,064)</u>
<u>TRAINING</u>			
Loan	770,341	770,341	-
Grant	211,359	211,083	(276)
	<u>981,700</u>	<u>981,424</u>	<u>(276)</u>
<u>AGRICULTURAL CREDIT</u>			
Loan	3,005,824	3,005,824	-
Grant	-	-	-
	<u>3,005,824</u>	<u>3,005,824</u>	<u>-</u>
<u>FARM PRODUCTION</u>			
<u>SERVICES</u>			
Loan	611,185	611,185	-
Grant	20,333	20,333	-
	<u>631,518</u>	<u>631,518</u>	<u>-</u>
<u>RESOURCE INFORMATION</u>			
Loan	255,542	255,542	-
Grant	116,104	116,053	(51)
	<u>371,646</u>	<u>371,595</u>	<u>(51)</u>

CUMULATIVE FUND ACCOUNTABILITY STATEMENT (cont'd)

For the periods September 15, 1981 through March 30, 1990
and April 1, 1990 through December 31, 1992

	<u>BUDGET</u>	<u>ACTUAL</u>	<u>AVAILABLE</u>
<u>ROAD MAINTENANCE</u>			
Loan	1,861,555	1,861,555	-
Grant	<u>1,927,287</u>	<u>1,927,287</u>	-
	3,788,842	<u>3,788,842</u>	-
<u>COMMUNITY DEVELOPMENT</u>			
Loan	649,847	649,847	-
Grant	<u>1,585,706</u>	<u>1,585,706</u>	-
	2,235,553	<u>2,235,553</u>	-
<u>PROJECT OFFICE</u>			
Loan	1,653,687	1,653,687	-
Grant	<u>182,656</u>	<u>182,656</u>	-
	1,836,343	<u>1,836,343</u>	-
Total incurred costs	<u>18,051,999</u>	<u>18,043,608</u>	
Outstanding fund balance (Note 6)		<u>8,391 (1)</u>	<u>(8,391)</u>

(1) Transferred to 1993 budget with Execution Letter N^o 99 of September 7, 1993.

**AUDIT OF THE UPPER HUALLAGA AREA DEVELOPMENT PROJECT
ACTIVITIES MANAGED BY THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
USAID/Peru Project No. 527-0244**

**Report on the Internal Control Structure
for the period April 1, 1990 to December 31, 1992**

INDEPENDENT AUDITORS' REPORT

We have audited the fund accountability statement of the Upper Huallaga Area Development Project, USAID/Peru Project No. 527-0244, activities managed by the Upper Huallaga Special Project Office (PEAH) for the period April 1, 1990 to December 31, 1992 and have issued our report thereon dated December 20, 1994. Also, we have reviewed the Schedule of Counterpart Contributions, presented separately, to determine if the contributions were provided and recorded in accordance with agreement terms.

Except for not having an external quality review by an unaffiliated audit organization as described further in our report on the fund accountability statement, we conducted our audit in accordance with generally accepted auditing standards and the Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the fund accountability statement is free of material misstatement.

In planning and performing our audit of the fund accountability statement of the Upper Huallaga Area Development Project activities managed by the Upper Huallaga Special Project Office for the period April 1, 1990 to December 31, 1992, we considered PEAH's internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the fund accountability statement and not to provide an opinion on the internal control structure. Also, we considered the internal controls applicable to the counterpart contributions provided by PEAH during the audited period.

The management of the Upper Huallaga Special Project Office is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that the assets are safeguarded against loss from unauthorized use or disposition; transactions are executed in accordance with management's authorization and in accordance with the terms of the agreement;

and transactions are recorded properly to permit the preparation of the fund accountability statement in conformity with the basis of accounting described in Note 2 to the fund accountability statement. 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 into the following categories:

- Legal and regulatory aspects
- Accounting and financial aspects
- Treasury (receipt and custody of funds)
- Liquidations (including procurement and payment for goods and services)
- Payrolls
- Fixed Assets

For all 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 judgment, could adversely affect PEAH's ability to record, process, summarize, and report financial data consistent with the assertions of management in the fund accountability statement and schedule of counterpart contributions.

Following are the reportable conditions we found, which are mainly related to fixed assets of the project:

1. Insufficient controls over fixed assets and inventories.
2. No directives for compliance with USAID regulations.
3. Non-implementation of budget and financial controls.

These reportable conditions are detailed in the Annex of the Report on the Internal Control Structure.

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

Our considerations of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe none of the reportable conditions described above is a material weakness.

We also noted other matters involving the internal control structure and its operation that we have reported to the management of Upper Huallaga Special Project Office in a separate letter dated March 10, 1994.

This report is intended for the information of the Upper Huallaga Special Project Office and the United States Agency for International Development. However, upon acceptance by the USAID Office of the Inspector General, this report becomes a matter of public record and its distribution is not limited.

December 20, 1994



Eduardo Villalobos D. (Partner)
Peruvian Public Accountant
Matriculation No. 852

Idauser Robly, Alonso P.C.

UPPER HUALLAGA SPECIAL PROJECT OFFICE (PEAH)

Reportable Conditions Annex of the Report on the Internal Control Structure, for the period April 1, 1990 to December 31, 1992

1. Insufficient controls over fixed assets and inventories

- a. Condition : • Established controls over fixed assets and inventories are not sufficient.
- The Buildings, Machinery and Equipment account on books has not been reconciled with the physical inventories taken in December 31, 1993; likewise, by the information provided by the Administration of PEAH, it has been determined that during the life of the project, several physical inventories were taken before 12/31/93, and that these inventories were not carried out entirely. These inventories were taken only partially and a final amount was not reconciled. There is not supporting documentation.
 - The Accounting Unit depreciated fixed assets which had already been fully depreciated.
 - We observed that there are controls, but these controls do not cover all fixed assets. There are documents to control asset use, but they are not properly completed nor maintained to facilitate the verification of the proper use of the project fixed assets.
 - PEAH's Internal Control Office observed that the pick-ups, motorcycles and cars belonging to the project are not kept, at the end of the workday, in the project's storehouses.
- b. Criteria : • Controls established by PEAH on fixed assets and inventories should be sufficient.
- The Buildings, Machinery and Equipment account reflected on the books should reconcile with the results of the inventory as of December 31, 1993. Also, the inventories should have supporting documentation.
 - Fixed assets which have already been fully depreciated, should not be depreciated as established by the accounting principles related to the depreciation of assets.

- Established controls over fixed assets should cover all fixed assets; the related documentation should be properly completed and maintained to facilitate the verification of the proper use of the project fixed assets.
 - The pick-ups, motorcycles and cars belonging to the project should be kept, at the end of the workday, in the project's storehouses.
- c. Cause :
- PEAH has not established directives for the sufficient control over fixed assets and inventories.
 - For lack of the necessary personnel for completing the stock takings, their results have not been reconciled with the Buildings, Machinery and Equipment account reflected on the Project's Books.
 - For ignorance, the accounting personnel in charge of the depreciation of assets, depreciated fixed assets which had already been fully depreciated.
 - For lack of the necessary personnel to control fixed assets, these controls did not cover all assets, and the documents to control asset use were not properly completed nor maintained for subsequent verification.
 - PEAH does not have a Directive establishing that vehicles assigned to the Project be maintained in PEAH's storehouses at the end of the working day.
- d. Effect :
- Because the project does not have an adequate internal control structure, it has not been possible to establish controls to ensure that fixed assets, procured with project funds, are properly safeguarded, recorded, inventoried, and used for project purposes.
- e. Recommendation:
- It is necessary that PEAH establish sufficient controls over fixed assets and inventories.
 - It is necessary that PEAH reconcile balances in books with the physical inventory of Buildings, Machinery and Equipment account, and perform the necessary adjustments, if any.

- It is necessary that the accounting area perform the depreciation analysis and verification so the financial statements do not present distortions due to the overdepreciation of project assets.
- It is necessary that existing controls cover all fixed assets. The existing documents to control asset use should be properly completed and maintained to facilitate the verification of the proper use of the project fixed assets.
- We recommend that PEAH's Administration issue a Directive or Regulation to control the use of the project's vehicles, when they need to be used during non-working hours.

f. Management comments : We will reconcile the Buildings, Machinery and Equipment account as soon as possible. Fixed asset depreciations, in excess, will be adjusted. Land value will be updated in accordance with the tariff value. We have established control, over vehicles assigned to the project, to have them kept in PEAH's storehouses when they are not going to be used for project purposes.

2. No directives for compliance with USAID regulations

- a. Condition : There are no directives for PEAH's compliance with USAID regulations.
- b. Criteria : Directives for PEAH's compliance with USAID regulations should exist.
- c. Cause : PEAH has not issued the directives that indicate the control procedures to comply with USAID requirements and that these controls should be applied during the whole life of the project.
- d. Effect : Because the project does not have directives for compliance with USAID regulations, it has not been possible to establish specific controls to ensure that fixed assets, procured with project funds, are properly safeguarded, recorded, inventoried, and used for project purposes.
- e. Recommendation : It is necessary that PEAH issue a Directive that specifies the control procedures that Projects should apply to comply with AID requirements for the proper use of project fixed assets during its life.

f. Management comments : It will be taken into account for future projects, because this project ended on December 31, 1993.

3. Non-implementation of budget and financial controls

a. Condition : The Project has not implemented budget and financial controls over the sub-projects that it manages.

b. Criteria : The project should have implemented budget and financial controls over the sub-projects it manages to allow PEAH determine the actual cost of each of the completed sub-projects.

c. Cause : The project has not implemented budget and financial control over the sub-projects it manages for lack of specialized personnel in the financial and technical areas.

d. Effect : PEAH has not determined the actual cost of each one of the finished sub-projects; the Work in Progress account in the financial statements only details the amount spent each year.

e. Recommendation : It is necessary that PEAH design a technical commission to prepare the technical documentation of the finished sub-projects at actual costs and have them activated as public foundation and transferred to the sectors that are using them when USAID/PERU authorizes it.

f. Management comments : We have made coordinations with INADE in order to hire the necessary professionals for assessing the finished sub-projects.

**AUDIT OF THE UPPER HUALLAGA AREA DEVELOPMENT PROJECT
ACTIVITIES MANAGED BY THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
USAID/Peru Project No. 527-0244**

**Report on Compliance with Agreement Terms and Applicable Laws and Regulations
for the period April 1, 1990 to December 31, 1992**

INDEPENDENT AUDITORS' REPORT

We have audited the fund accountability statement of the Upper Huallaga Area Development Project, USAID/Peru Project No. 527- 0244, activities managed by the Upper Huallaga Special Project Office (PEAH) for the period April 1, 1990 to December 31, 1992, and have issued our report thereon dated December 20, 1994. We also reviewed the separate Schedule of Counterpart Contributions to determine whether they were provided and accounted for in accordance with the terms of the agreement.

Except for not having an external quality control review by an unaffiliated audit organization as described further in our report on the fund accountability statement, we conducted our audit in accordance with generally accepted auditing standards and the Government Auditing Standards 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 Upper Huallaga Area Development Project is the responsibility of Upper Huallaga Special Project Office's management. As part of obtaining reasonable assurance about whether the fund accountability statement is free of material misstatement, we performed tests of Upper Huallaga Special Project Office's compliance with significant agreement terms and applicable laws and regulations. However, the objective of our audit of the fund accountability statement was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion. We also performed tests of the Upper Huallaga Special Project Office's compliance with certain provisions of agreement terms and laws and regulations applicable to the provision of counterpart contributions.

The results of our tests indicate that, with respect to the items tested, the Upper Huallaga Special Project Office complied, in all material respects, with the agreement's terms and applicable laws and regulations. With respect to items not tested, nothing came to our attention that caused us to

believe that the Upper Huallaga Special Project Office had not complied, in all material respects, with those provisions.

We noted certain immaterial instances of noncompliance that we have reported to the management of the Upper Huallaga Special Project Office in a separate letter dated March 10, 1994.

This report is intended for the information of the Upper Huallaga Special Project Office and the United States Agency for International Development. However, upon acceptance by the USAID Office of the Inspector General, this report becomes a matter of public record and its distribution is not limited.

December 20, 1994



Eduardo Villalobos D. (Partner)
Peruvian Public Accountant
Matriculation No. 852

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**AUDIT OF THE UPPER HUALLAGA AREA DEVELOPMENT PROJECT
ACTIVITIES MANAGED BY THE UPPER HUALLAGA SPECIAL PROJECT OFFICE
USAID/Peru Project No. 527-0244**

**Follow up on Recommendations from the Prior Audit of the Project
for the Period September 15, 1981 to March 31, 1990**

Following we present the situation of the recommendations resulting from the last financial audit of the project.

<u>OBSERVATION</u>	<u>SITUATION OF RECOMMENDATION</u>
1. Payrolls are financed with other resources not considered in the agreement. (Finding was included in Management Letter.)	Recommendation implemented. The Executive Director has disposed the corrective measures to prevent execution of these kinds of actions.
2. Contracted personnels' salaries are paid in their entirety with project funds. (Issue was reported as a questionable cost in the fund accountability statement.)	Recommendation implemented. PEAH has returned these funds in an amount of US\$43,000 after request of USAID/Peru.
3. Control related to the physical location of project's fixed assets is not adequate. (Finding was included in Management Letter.)	Recommendation implemented. PEAH has implemented a Patrimonial Control Form, in which changes of location of fixed assets are recorded, with the Patrimony Area authorization and countersigned by the Supplies Unit.

To Executive Director
Upper Huallaga Special Project

Dear Sir:

As part of the examination of the fund accountability statement of the Upper Huallaga Area Development Project, USAID/Peru Project No. 527-0244, managed by the Upper Huallaga Special Project Office (PEAH) for the period April 1, 1990 to December 31, 1992, we have studied and assessed the Institution's accounting internal control system as we considered necessary to determine the nature, opportunity and extent of the audit procedures for the purpose of expressing our opinion on the fund and accountability statement.

In planning and performing our audit of the Upper Huallaga Area Development Project managed by the Upper Huallaga Special Project Office, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the fund accountability statement and not to provide assurance on the Institution's internal control structure taken as a whole.

However, we noted certain immaterial matters involving the internal control structure and its operation which are described in the following pages.

This report is intended for the use of the Upper Huallaga Special Project Office and the United States Agency for International Development and should not be used for any other purpose.

March 10, 1994



Eduardo Villalobos D. (Partner)
Peruvian Public Accountant
Matriculation No. 852

Hansen-Holm, Alonso & Co.

UPPER HUALLAGA SPECIAL PROJECT OFFICE (PEAH)
MEMORANDUM OF RECOMMENDATIONS ON INTERNAL
CONTROL MATTERS
MARCH 1994

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UPPER HUALLAGA SPECIAL PROJECT OFFICE (PEAH)

MEMORANDUM OF RECOMMENDATIONS ON INTERNAL
CONTROL MATTERS
MARCH 1994

1. An individual separate from the treasury functions should verify that the inflow of funds balances with the bank deposits
 - a. Condition : Confirmation that the inflow of funds balances with the bank deposits is performed by the treasurer.
 - b. Criteria : An individual separate from the treasury functions should verify that the inflow of funds balances with the bank deposits.
 - c. Cause : Confirmation that the inflow of funds balances with the bank deposits is performed by the treasurer, because of the lack of personnel.
 - d. Effect : Lack of segregation of responsibilities regarding the verification that funds received have been deposited into the bank results in an increased opportunity that funds received will not be timely deposited.
 - e. Recommendation : An individual separate from the treasury function should verify that the inflow of funds balances with the bank deposits, to permit a control of deposits in its opportunity and verify its integrity.
 - f. Management comments : In order to implement this recommendation, PEAH's Management Office, with Memorandum No. 042-94-PEAH-INADE-6630, has disposed the General Accountant to designate an individual from the Accounting Unit to carry out the control of bank deposits and verify that they are recorded in the auxiliary bank records and reported in the financial statements.

2. Issued checks should be protected
 - a. Condition : Measures to protect issued checks have not been taken.

- b. Criteria : It should be established the use of a check protector machine or adhesive tape in order to protect issued checks.
 - c. Cause : Lack of a check protector machine or the instruction to use adhesive tape, does not allow issued checks to be protected.
 - d. Effect : Not having a check protector machine or the instruction to use adhesive tape to protect issued checks, exposes them to possible adulterations.
 - e. Recommendation: It is necessary to establish a system to protect issued checks with a check protector machine or using adhesive tape.
 - f. Management comments : Management Office has disposed the procurement of a check protector machine, in order to avoid adulteration of amounts indicated.
3. Bank reconciliations should be prepared by an individual separate from the treasury area
- a. Condition : Bank reconciliations are prepared monthly by the treasurer.
 - b. Criteria : Bank reconciliations should be prepared by an individual separate from the treasury area.
 - c. Cause : Bank reconciliations are prepared by the treasurer because of the lack of personnel in other areas that could be in charge of reconciliations.
 - d. Effect : If the treasurer prepares the bank reconciliations, it is allowing a duplicity of functions.
 - e. Recommendation: It is convenient that an individual separate from the treasury area, could be from the accounting area, prepares the bank reconciliations.
 - f. Management comments : Bank reconciliations have been carried out in the treasury area due to lack of personnel in the Accounting Unit caused by budget limitations that do not permit the hiring of support personnel. However, as a control action, it has been disposed that all bank reconciliations are to be carried out in the accounting area, which is causing a work overload for the personnel of this area.

4. Auxiliary records of the different fixed assets do not allow their easy location

- a. Condition : Auxiliary records of the different fixed assets do not allow their easy location.
- b. Criteria : In the auxiliary records of the different fixed assets should appear each item's location, clearly and accurately.
- c. Cause : Lack of an instruction that establishes that in the auxiliary records of the different fixed assets there should be clear and accurate information of the items' location.
- d. Effect : If the location of the different fixed assets does not appear, clearly and accurately, in the auxiliary records, an inadequate use of the fixed assets could occur and not be timely detected.
- e. Recommendation : It should be established in an instruction that the auxiliary records of the different fixed assets show their location, clearly and accurately.
- f. Management comments : Although auxiliary cards are not duly updated, as of this day, assets have been verified according to the General Supplies Standards SA.07, and these standards have been implemented through the methodology of work applied with Informative Note No. 92A-93-PEAH-INADE-6330.03, whose results will allow us to update our records. This work will be carried out sequentially due to lack of personnel in the Patrimony Area (one person) caused by budget limitations that do not permit the hiring of support personnel.

5. Financing source for the procurement of fixed assets should appear in the auxiliary records

- a. Condition : In the auxiliary records of fixed assets does not appear the financing source of their procurement.
- b. Criteria : The financing source for the procurement of fixed assets should appear in the auxiliary records.
- c. Cause : Lack of an instruction that establishes that the financing source for the procurement of fixed assets should appear in the auxiliary records.
- d. Effect : Because the financing source for the procurement of fixed assets does not appear in the auxiliary records, these records cannot be

analyzed to identify the amount of assets procured by financing source.

- e. Recommendation: An instruction should be established requiring that auxiliary records of fixed assets include information on the financing source of each item.

- f. Management comments : Up to 1992, asset inventories were prepared without taking into account financing sources since the accounting reports were presented without taking into account the financing source. As of this day, in order to implement our records and to present the information required by USAID, PEAH's Management Office, with Memorandum No. 093-94-PEAH-INADE-6330, has disposed the same commission formed for stocktakings of patrimony be in charge of the review of all documentation on files in order to locate the financing sources of assets.

As of this day, this work has been finished and the fixed assets classification in accordance with the financing source is reflected in the inventory at 12/31/93.

6. Computer equipment, office and sundry equipment should be insured

- a. Condition : Computer equipment, office and sundry equipment are not insured.

- b. Criteria : Computer equipment, office and sundry equipment should be insured.

- c. Cause : Computer equipment, office and sundry equipment are not insured because of the Institution's policies.

- d. Effect : Having the computer equipment, office and sundry equipment not insured could make it impossible to recover the assets' value in case they are stolen or destroyed.

- e. Recommendation: Computer equipment, office and sundry equipment should be insured in order to recover the assets' value in case of a disaster.

- f. Management comments : Considering that PEAH has many fixed assets that were procured 8 or more years ago, and due to their use are in regular condition; in some cases, due to revaluation and depreciation they are with residual value. The Management Office though has taken an

insurance policy for the computer equipment (Policies No. 011672 and 127333), Power Unit (Policies No. 011671 and 127334), and vehicles which have recently been acquired (Policy No.068881). Due to budget limitations all of our assets cannot be insured. However, this Office will seek budget reconsideration in order to insure the rest of our assets.

7. Lack of archives to keep the original bills of fixed assets procurements

- a. Condition : The Institution lacks archives to keep the original bills of fixed assets procurements.
- b. Criteria : The person in charge of the fixed assets should have an archive to keep the original bills of fixed asset procurements.
- c. Cause : The person in charge of the fixed assets was unaware that the original bills of fixed assets procurements must be kept in an archive to support their cost an ownership.
- d. Effect : Not having an archive that contains the original bills of fixed assets procurements leads to not maintaining the information for determining the cost and ownership of those assets.
- e. Recommendation: As a control measure of the ownership and cost of fixed assets, it is necessary to keep an archive that contains the original bills of fixed asset procurements.
- f. Management comments : The Patrimony Area does not have archives to keep the original bills of fixed assets procurements due to the methodology that PEAH is applying in the documents archives. Each area is responsible for the documentation that it handles. The supporting documents of the payment receipts, which are responsibility of the Treasury Area, are filed in this area.

8. Payroll is reviewed by the same individual who prepares it

- a. Condition : The individual who prepares the payroll is the same one that reviews it before payment, as regards to amounts, calculations, taxes computations, and social security.
- b. Criteria : The payroll should be reviewed before payment, as regards to amounts, calculations, taxes computations, and social security.

However an individual different from the one that prepares the payroll should make this review.

- c. Cause : Payroll is not reviewed by an individual different to the one who prepares it because of a lack of personnel to be in charge of that review.
- d. Effect : Not having an individual in charge of the payroll review different to the one who prepares it does not allow for detecting mistakes in amounts, calculations, taxes computations and social security.
- e. Recommendation: It is convenient that an individual different from the one in charge of payroll preparation be in charge of its review.
- f. Management comments : With respect to this observation, it is necessary to mention that for payment of remunerations, the Personnel Unit previously prepares the monthly requirement of funds in coordination with the Planning and Budget Office. Subsequently, before processing the payrolls of salaries and wages, a report to Administration is prepared for its review. This report contains various data such as hirings and retirements of personnel, adaptations to legal provisions in force, withholdings and/or discounts, etc.

However, in order to implement the recommendation to this observation, the Management Office with Memorandum No. 044-94-PEAH-INADE-6330 has disposed to designate the person in charge of Previous Control to carry out the review of payrolls before its assignment and respective payment.

9. Equipment directly procured by USAID for account of the Project are not timely recorded in the accounting records

- a. Condition : Equipment directly procured by USAID for account of the Project have been received during the period audited and have not been recorded in the accounting records of that period (Reference to Note 4 to the Fund Accountability Statement).
- b. Criteria : Assets should be recorded in the accounting records at the date of receipt.
- c. Cause : Equipment directly procured by USAID is not timely recorded in PEAH's accounting records because of a lack of communication between USAID and PEAH about these procurements.

- d. Effect : If equipment directly procured by USAID is not timely recorded in PEAH's accounting records, then it is not possible to exercise an effective control on the Project's fixed assets.
- e. Recommendation: Communication between USAID and PEAH referring to equipment directly procured by USAID should provide information to timely account for the equipment in PEAH's accounting records.
- d. Management comments : Equipment directly procured by USAID for account of the loan agreement generate all an administrative process from the requirement until the arrival of goods at Callao Port. These goods stay a significant time in Callao until accomplishing all the administrative process of customs clearance.

The supporting documents (bills) are remitted with posteriority to the entry of goods to PEAH's warehouses, which causes a significant delay in their accounting.

On the other hand, another cause of the delay in accounting for the equipment directly procured by USAID is that when the bills are obtained the corresponding schedule is not available, causing the request in the MEF (Public Budget) of an additional credit or schedule extention for the following months and just then account for presupuestary and financially according to accounting principles (accounting parallelism).

However, goods procured by USAID are permanently controlled from the moment they come in to PEAH and there is no possibility of loss or misuse.

To Executive Director
Upper Huallaga Special Project

Dear Sir:

As part of our examination of the fund accountability statement of the Upper Huallaga Area Development Project, USAID/Peru Project No.527-0244, managed by the Upper Huallaga Special Project Office (PEAH) for the period April 1, 1990 to December 31, 1992, we performed tests to obtain reasonable assurance that PEAH complied with agreement terms and applicable laws and regulations which might affect the project goals and incurred costs. Our tests were for the purpose of expressing an opinion on the fund accountability statement and were not sufficient to provide an opinion on PEAH's overall compliance with the mentioned provisions.

The results of our tests indicate that, with respect to the items tested, the Upper Huallaga Special Project Office, complied, in all material respects, with the agreement's terms and applicable laws and regulations. With respect to items not tested, nothing came to our attention that caused us to believe that PEAH had not complied, in all material respects, with those provisions. However, we noted certain immaterial instances of noncompliance that we describe in the following pages.

This report is intended for the information of Upper Huallaga Special Project Office and the United States Agency for International Development and should not be used for any other purpose.

March 10, 1994



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UPPER HUALLAGA SPECIAL PROJECT OFFICE (PEAH)

**MEMORANDUM OF RECOMMENDATIONS ON COMPLIANCE
WITH AGREEMENT TERMS AND APPLICABLE LAWS AND REGULATIONS
MARCH 1994**

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MEMORANDUM OF RECOMMENDATIONS ON COMPLIANCE
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1. Payments of taxes (General Sales Tax) are made with USAID funds

- a. Condition : Purchases, whose bills include the Sales General Tax (IGV), were made with USAID funds, and were deducted from the liquidations of the project by USAID/Peru, and accounted for in the counterpart's funds
- b. Criteria : Taxes costs for received goods should not be paid with USAID funds, As it is established in Article B, Section B.4.(c) in Combined Loan and Grant Project Agreement Standard Provisions Annex 2.
- c. Cause : Payment of IGV tax included in bills, is done because it is not possible to put the goods cost in a bill and the tax cost in another because of peruvian legislation.
- d. Effect : Paying the IGV tax, with USAID funds, violates the Article B, section B.4.(c) in Combined Loan and Grant Project Agreement Standard Provisions Annex 2.
- e. Recommendation: Payment of the IGV tax with USAID funds should be avoided.
- f. Management comments : Currently, taxes (IGV) are not paid with USAID funds, when acquiring goods and services.

2. Feeding costs are paid with USAID funds

- a. Condition : Feeding expenses were made with USAID funds, and were deducted from the liquidations of the project by USAID/Peru, and accounted for in the counterpart's funds.
- b. Criteria : Feeding costs should not be paid with USAID funds, as it is established in the Implementation Letter, No.1 of November 2, 1981 chapter IV Disbursement.

- c. Cause : These costs were paid with USAID funds, because PEAH considered that feeding expenses were allowed by the agreement.
- d. Effect : Paying feeding costs with USAID funds, violates the Implementation Letter No.1 of November 2, 1981 chapter IV Disbursement.
- e. Recommendation: Payment of feeding costs with USAID funds should be avoided.
- f. Management comments : It is disposed that feeding costs be paid with counterpart funds from the Central Government.

3. Activities financed with USAID funds are executed out of the Project area

- a. Condition : We noted in PEAH's internal auditor report dated August 21, 1990 that some activities financed with Project's funds had been performed out of the Campanilla zone, that is, in Juanjui.
- b. Criteria : Activities financed with USAID funds should be carried out in the Project area where they are required to operate, as established by Implementation Letter No. 88.
- c. Cause : Because the contour of the Campanilla zone was not timely delimited, some activities were carried out in Juanjui.
- d. Effect : Carrying out activities financed with USAID funds out of the Campanilla zone violates Implementation Letter No. 88. that establishes that activities financed with USAID funds can not be executed out of the Project area.
- e. Recommendation : The boundary line of the Project's office should be defined in a timely manner in order to accomplish the requeriments of Implementation Letter No. 88.
- f. Management comments : For security and for social problems (terrorism and drug traffic), the Zone Office of PEAH in Campanilla moved to Juanjui and because of the various requests for support by the rural sectors, activities were scheduled in the limits of the province of Mariscal Caceres. The Executive Director of PEAH decided, meanwhile, to attend the sectors and places adjacent to PEAH's limits in Campanilla and approved in the 1990 Operative Plan that was remitted to USAID, and receiving the communication with Execution Letter No. 82 in which they found satisfactory the

general terms of the Plan in accordance with the terms of the Project Agreement.
