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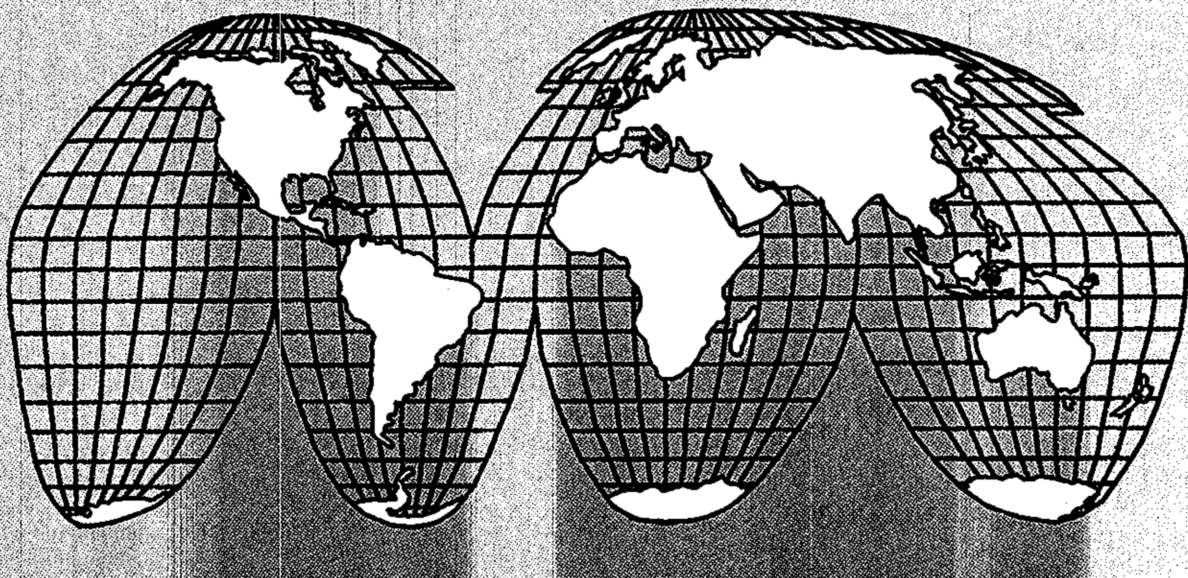
OFFICE OF INSPECTOR GENERAL

Audit of USAID/Honduras-Financed Credit Activities Under the Central America and the Caribbean Emergency Disaster Recovery Fund

Audit Report No. 1-522-02-001-P

October 1, 2001



U.S. Agency for International Development
Regional Inspector General / San Salvador

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U.S. Agency for
INTERNATIONAL
DEVELOPMENT

RIG/San Salvador

October 1, 2001

MEMORANDUM

FOR: USAID/Honduras Director, Timothy M. Mahoney

FROM: RIG/San Salvador, Timothy E. Cox Timothy E. Cox

SUBJECT: Audit of USAID/Honduras-Financed Credit Activities Under the Central America and the Caribbean Emergency Disaster Recovery Fund (Report No. 1-522-02-001-P)

This memorandum is our report on the subject audit. Your comments on the draft report have been included, in their entirety, in Appendix II.

This report does not contain any recommendations for your action. I appreciate the cooperation and courtesy extended to my staff during the audit.

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Summary of Results

As part of its fiscal year 2001 audit plan, the Regional Inspector General/San Salvador performed this audit to determine whether USAID/Honduras-financed credit activities were on schedule to achieve planned outputs and whether the mission implemented an adequate monitoring system for its credit activities (see page 4).

We found that USAID/Honduras-financed credit activities were on schedule to achieve planned outputs. We also found that the mission had implemented an adequate monitoring system for its credit activities (see pages 5 - 6).

Management concurred with the findings in our draft report (see page 6).

Background

In October 1998, Hurricane Mitch swept across Honduras. Its devastation and associated flooding, which continued through January 1999, resulted in the deaths of thousands of Hondurans, left nearly a million people homeless, and caused incalculable crop, equipment, infrastructure, and other losses.

The capacity to pay current loans disappeared with the lost harvest, while the capacity to earn future income vanished when floods washed away the productive infrastructure. As default rates soared with the collapse of many businesses, unemployment in agricultural and non-agricultural sectors increased.

In May 1999, Congress passed the Emergency Supplemental Appropriations Act, creating the Central America and the Caribbean Emergency Disaster Recovery Fund, which provided a total of $621 million in reconstruction assistance for countries hit by Hurricanes Mitch and Georges and for Colombia for earthquake damages. Of the $621 million, Honduras received $291 million.

Using this funding provided by Congress, USAID/Honduras and the Honduran Ministry of Finance signed a special objective grant agreement for the *Hurricane Reconstruction Program*, dated June 9, 1999, to achieve the joint special objective "*Critical Hurricane Reconstruction Needs Met.*" Under this agreement, an element entitled *Agricultural Credit* funds the credit activities. In addition, to start these programs before Congress passed the Emergency Supplemental Appropriations Act; USAID/Honduras used $3 million of Development Assistance funds for hurricane reconstruction credit activities.

USAID/Honduras planned to spend $38.3 million on credit programs by December 31, 2001. The following chart lists the four credit activities audited and, as reported by USAID/Honduras' financial accounting system, obligations and accrued expenditures for these activities as of March 31, 2001.

Names	**Obligations 3/31/01 (unaudited)**	**Accrued Expenditures 3/31/01 (unaudited)**
Agricultural Cooperative Development International/Volunteers in Overseas Cooperative Assistance (ACDI/VOCA)	$5,000,000	$4,467,522
Honduran Federation of Credit Unions (FACACH)	6,000,000	5,100,954
Jose Maria COVELO Foundation (COVELO)	10,438,996	7,344,014
National Fund for Production and Housing (FONAPROVI) [1]	16,817,691	10,994,410
	$38,256,687	$27,906,900

Audit Objectives

As part of its fiscal year 2001 audit plan, the Regional Inspector General/San Salvador performed the audit to answer the following questions:

- Are USAID/Honduras-financed credit activities on schedule to achieve planned outputs?
- Has USAID/Honduras implemented an adequate monitoring system for its credit activities?

The audit scope and methodology is presented in Appendix I.

[1] For the FONAPROVI activity, USAID contracted with Barents Group LLC to oversee the program and provide technical assistance to FONAPROVI. Obligations of $1,831,691 and accrued expenditures of $1,000,000 are included in the amounts listed for this contract with Barents Group LLC.

Audit Findings

Are USAID/Honduras-financed credit activities on schedule to achieve planned outputs?

USAID/Honduras-financed credit activities were on schedule to achieve planned outputs. The following chart summarizes the key outputs planned and achieved as of March 31, 2001.

Implementer—Output Description	Outputs Planned[2] as of 3/31/01	Actual Outputs Achieved by 3/31/01	Percentage of Planned Outputs Completed as of 3/31/01
ACDI/VOCA—Funds disbursed for loans	$1,634,615	$2,054,849	126%
FACACH—Funds disbursed for loans	$2,782,857	$4,431,133	159%
COVELO—Funds disbursed for loans	$7,265,455	$7,127,947	98%
FONAPROVI—Funds disbursed for loans	$8,563,429	$9,797,810	114%
	$20,246,356	$23,411,739	116%

Based on the percentage of planned outputs completed as of March 31, 2001,[3] which were validated by our audit tests, we concluded that USAID/Honduras-financed credit activities were on schedule to achieve planned outputs.

Has USAID/Honduras implemented an adequate monitoring system for its credit activities?

USAID/Honduras implemented an adequate monitoring system for its credit activities.

We defined an adequate monitoring system as one that complied with the monitoring methods described in USAID policy; Title 22 of the U.S. Code of Federal Regulations, Section 226.51, entitled *Monitoring and Reporting Program Performance;* and the agreements between the four implementers and USAID/Honduras. Based on these documents, we determined through interviews and a review of supporting documentation that required monitoring procedures were performed for each of the four

[2] Planned outputs are estimated as of March 31, 2001 by allocating life-of-activity targets on a straight-line basis over the life of each activity.

[3] As discussed in Appendix I, we considered an activity to be on schedule if at least 90 percent of the planned outputs were completed by March 31, 2001.

credit activities. See Appendix I for details on required procedures reviewed.

Specifically, we found that USAID/Honduras:

- Maintained regular contact with the implementers through meetings, phone calls and correspondence.
- Reviewed quarterly and/or semi-annual financial and performance reports.
- Performed regular site visits to several activity locations for all activities.
- Monitored the quality and timeliness of key outputs as indicated through activity managers' reviews of progress reports and detailed knowledge about achievements.
- Reviewed the deliverables for the contract with Barents Group LLC (the other organizations operated under cooperative agreements).
- Performed the appropriate monitoring procedures as specified in the implementing agreements. For example, we found that activity managers approved implementers' workplans and key personnel.

Management Comments and Our Evaluation

USAID/Honduras, in its comments on our draft report, concurred with all audit findings. Its comments are included, in their entirety, in Appendix II.

Scope and Methodology

Scope

We audited USAID/Honduras-financed credit activities in accordance with generally accepted government auditing standards. According to USAID/Honduras, total obligations and accrued expenditures as of March 31, 2001 totaled $38.3 million and $27.9 million, respectively. We did not include in our scope the $0.9 million credit activity implemented by Katalysis Partnership, Incorporated. Although USAID/Honduras funded this activity, USAID/Washington managed it.

We conducted the audit at USAID/Honduras, the offices of several implementing organizations, and various sites throughout Honduras. We conducted the audit from June 5, 2001 to July 31, 2001 and covered the period from April 8, 1999 (the inception of the first of the audited activities) to March 31, 2001.

The audit focused on whether the credit activities were on schedule to achieve their planned outputs and whether USAID/Honduras implemented an adequate monitoring system. Although there were several planned outputs, USAID/Honduras officials stated that the key outputs were the loans provided to recipients. In addition, the majority (almost 90 percent) of the budgeted funding was directly linked to the achievement of these outputs. Therefore, we limited our site visits to the verification of these outputs and did not verify the achievements reported on outputs other than loans provided to beneficiaries. Out of the $27.9 million in accrued expenditures listed above, $23.4 million related to the key outputs tested. Of this $23.4 million, loans selected for sampling totaled $1.6 million.

We assessed the Mission's management controls related to monitoring and reporting on the credit activities. Specifically, we assessed its controls for approving workplans, monitoring and evaluation plans, and sub-awards; reviewing progress and financial reports; performing site visits; and monitoring the quality and timeliness of key outputs.

Methodology

To answer the audit objectives, we reviewed documentation at USAID/Honduras, which included project design documents and implementing agreements between parties. These were the documents that provided the activities' planned outputs and funding. In addition, we reviewed implementing organizations' progress reports and workplans.

To answer the first audit objective, we interviewed responsible officials at USAID/Honduras and the implementing entities. In addition, we reviewed relevant documentation obtained from these organizations. We confirmed the actual progress by performing 44 site visits. During these site visits, we interviewed both the borrowers of the loans and the banks/organizations that provided the loans to ensure that: 1) the borrower existed and 2) the amount of the loan provided agreed with amounts reported by the implementing organization. We used a random sampling methodology (using the dollar value of loans disbursed) to select the loans reviewed so that we could make conclusions on the accuracy of the total loans disbursed.

Since most activities did not have time-phased work plans that showed when outputs were expected to be completed at the time of our audit, we developed other criteria for determining whether the activities were on schedule. Therefore, we allocated life-of-activity output targets on a straight-line basis over the life of each activity. USAID/Honduras did not dispute this methodology, and nothing came to our attention during audit fieldwork to suggest that a straight-line allocation method was not a reasonable measure of progress.

We considered that an activity was on schedule if at least 90 percent of the planned key outputs (defined, as discussed above, as the amount of loans disbursed) as of March 31, 2001 had been achieved as of that date. This threshold reflected our judgements about the level of performance that was practical and achievable for the audited activities.

To answer the second audit objective, we first determined what monitoring mechanisms were established in the implementing agreements, then identified other monitoring methods as defined by USAID's Automated Directives System (ADS) and activity manager training manuals, and 22 CFR 226.51, entitled *Monitoring and Reporting Program Performance*. Specifically, by interviewing USAID/Honduras officials and reviewing supporting documentation or obtaining other corroborating support, we answered the following six questions for each of the activities:

1. Was regular contact maintained with the implementers (Managing for Results Training Material, Unit 2, Lesson 7, entitled Assistance Administration[4])?

2. Did the activity manager review performance and financial reports from the implementers (ADS 202.3.4.1 and 22 CFR 226.51)?

[4] Whereas the training manual did not contain mandatory monitoring procedures, we believe that maintaining regular contact with implementers is a key mechanism for adequately monitoring activities.

3. Did the activity manager perform site visits (Managing for Results Training Material, Unit 2, Lesson 7, entitled Assistance Administration and 22 CFR 226.51)?

4. For contracts, did the activity manager review deliverables (ADS 202.3.4.1)?

5. Did the activity manager monitor the quality and timeliness of key outputs (ADS 202.3.4 and 22 CFR 226.51)?

6. Did the activity manager perform the required monitoring procedures as stated in the acquisition and/or assistance agreement (contract and/or cooperative agreements)?

Management Comments

USAID/HONDURAS
MEMORANDUM

USAID

DATE : September 4, 2001

TO : Tim Cox, RIG/SS

FROM : Timothy Mahoney, Mission Director TM

SUBJECT : **DRAFT AUDIT REPORT Nº 1-522-01-00X-P**
Audit of USAID/Honduras-Financed Credit Activities Under the Central America and the Caribbean Emergency Disaster Recovery Fund

This memorandum represents USAID/Honduras concurrence with the contents of the draft report of the audit of USAID/Honduras-Financed Credit Activities Under the Central America and the Caribbean Emergency Disaster Recovery Fund No. 1-522-01-00X-P.

USAID/Honduras would like to comment that this Mission is committed to achieve planned outputs and is making all necessary efforts to do it as scheduled. Also, we would like to express our appreciation to the RIG's auditors for all the information provided through the audit which has been very useful for the better implementation of the financed credit activities.