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USAID/DOMINICAN REPUBLIC'S MONITORING OF AND CONTROLS OVER DOLLAR AND LOCAL CURRENCY RESOURCES PROVIDED UNDER ECONOMIC RECOVERY AND PL 480 TITLE I PROGRAMS

MEMORANDUM SURVEY REPORT NO. 1-517-85-11
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USAID/DOMINICAN REPUBLIC'S MONITORING OF AND CONTROLS OVER DOLLAR AND LOCAL CURRENCY RESOURCES PROVIDED UNDER ECONOMIC RECOVERY AND PL 480 TITLE I PROGRAMS

SUMMARY

USAID/Dominican Republic (USAID) and the Government of the Dominican Republic (GODR) undertook the above programs for balance-of-payments support to promote financial stability and economic recovery. The USAID had disbursed $133.0 million in loans and one grant under the Economic Recovery Program since its inception on September 30, 1982 through April 12, 1985. These transfers produced RD$246.5 million in local currency (pesos), of which RD $68.3 million had been disbursed at the time of our review in May 1985. The GODR had received $81.0 million in PL 480 Title I commodities during approximately the same period. Proceeds from the sale of those commodities generated RD $124 million, of which nearly RD $54 million (equivalent to $52.6 million) had been disbursed.

The purpose of our survey was to determine the effectiveness of program controls and monitoring over the resources provided by AID and local currency generated by those resources. The USAID Controller and the Capital Resources Development Office were generally providing the necessary monitoring and oversight to ensure that both programs achieve their goals. We discussed the results of the survey with USAID officials during an exit conference held on May 16, 1985. Their comments were considered in preparing this report.

BACKGROUND

Economic Recovery Program - Caribbean Basin Initiative

On September 30, 1982, AID started a financial assistance program to the GODR for balance-of-payments support and to promote financial stability and economic recovery. As of April 12, 1985 AID had transferred $133.0 million under this program to the GODR in loans ($83.0 million) and one grant ($50.0 million), as follows:

Agreement/Date	Grant	Loans (Million)	Total Disbursed	Date Disbursed
517-K-039 9/30/82		$41.0	$41.0	10/19/82
517-K-039A 9/30/83		8.0	8.0	11/29/83
517-K-039B 5/2/84		34.0	20.0	08/30/84
			14.0	09/06/84
517-0227 12/26/84	$50.0		50.0	12/26/84
Totals	$50.0	$83.0	$133.0	

One condition to the use of the dollar funds was that the GODR make available an equivalent amount of foreign exchange in the 12-month period following their disbursement to import raw materials, intermediate goods and capital goods from the United States for private sector industry and agriculture. Another condition was that an equivalent amount in local currency (counterpart funds) was to be deposited into a special account at the Central Bank of the Dominican Republic (Central Bank) not later than 30 days after grant disbursement or 60 days after the disbursement of loan funds. As of April 12, 1985 the GODR had deposited the equivalent of $122.0 million in local currency in special non-interest-bearing accounts with the Central Bank, of which the equivalent of $68.3 million had been disbursed. Of the $122.0 million deposited $83.0 million was from the loans' proceeds and $39.0 million was from the grant. The USAID granted the GODR an extension to November 30, 1985 to deposit the local currency equivalent of the remaining $11.0 million from the grant. The funds were programmed to support development activities as follows:

Activity	Funding Programmed ($000,000)	($ equivalent) 1/ Approved (000,000 pesos)	%	Disbursed (000,000 pesos)	%
1. Agro-Industry and Export Credit	35.0	35.0	100%	35.0	100%
2. Productive Infrastructure	27.0	23.1	86%	21.8	94%
3. Institutional Support and Development	21.0	12.4	59%	11.5	93%
Sub-totals	83.0	70.5	85%	68.3	82%
4. Available for new programs but not yet programmed		(12.5)			
Totals	83.0	70.5	85%	68.3	82%

The grant agreement also requires that the GODR establish a trust fund account using a portion of the counterpart in an amount not to exceed RD $15.0 million. The funds were to be used to promote U.S. economic assistance programs in the Dominican Republic including certain USAID administrative and implementation costs.

The Technical Secretariat of the Presidency of the GODR, jointly with USAID, planned and programmed the uses of the counterpart generated under the grant and loan agreements. The Secretariat was also responsible for providing USAID

1/ Exchange rate at the time: RD$1.00 = US$1.00

a detailed report on the progress the GODR was making in carrying out the activities financed with the pesos generated under the agreements by December 31 of each calendar year. In addition, the Secretariat was to submit quarterly reports and end-of-year status reports for each subproject, as well as any other reports that USAID might reasonably request.

The Central Bank was responsible for:

1. Attributing eligible import transactions to cash transfers within 12 months from the date of each agreement.

2. Maintaining the special accounts for the local currency generated under the program.

3. Informing the Secretariat and USAID of all deposits of local currency generated by the dollars made available under the agreements and submitting any financial information that USAID might reasonably request.

PL 480 Title I Program

AID authorized the GODR to import $83.5 million in wheat, wheat flour, rice, corn, sorghum and edible/vegetable oil under four Title I agreements signed between February 20, 1981 and January 13, 1984.

The proceeds from the sale of commodities financed by AID were to be used for financing self-help measures in the agriculture and public health sectors in a manner designed to increase the access of the poor to an adequate, nutritious, and stable food supply. Also, in the use of the proceeds from the sale of commodities, emphasis was to be placed on directly improving the lives of the poorest people and their capacity to participate in the development of their country.

The National Planning Office (ONAPLAN), within the Technical Secretariat of the Presidency, was the implementing unit for the PL 480 Title I Program. The Secretariat, jointly with USAID, was responsible for programming the uses of and accounting for the local currency disbursed to development projects financed with Title I sale proceeds. ONAPLAN, through the Secretariat, was to submit for the USAID's approval a detailed work plan for each sub-project to be financed with the sales proceeds.

ONAPLAN's financial division acted as the coordinating unit for the ESF/PL 480 Title I Programs. This unit was established in 1980 and was staffed with 10 professionals and one secretary. The unit was responsible for controlling and monitoring ESF/PL 480 Title I funds, following-up on projects financed under the two programs, programming the utilization of ESF/PL 480 Title I resources, and preparing quarterly financial reports.

The National Price Stabilization Institute (INESPRE) was responsible for purchasing and selling the commodities imported under the program as well as for collecting the sales proceeds and depositing them into a special account at the Central Bank.

The status of accounts for the PL 480 Title I Program in the Dominican Republic since 1981 through April 12, 1985 was as follows:

	US$ (millions)	RD$ (millions)
Total authorized	83.5	--
Total shipped	81.0	--
Total sales proceeds	81.0	123.9 2/
Total deposited	75.8	110.8 3/
Total programmed	66.2	66.2
Total disbursed	52.6	54.3 4/

PURPOSE AND SCOPE

A survey of the Economic Stabilization and Recovery Program (ESR) and the PL 480 Title I Program was made from April 17 through May 17, 1985. Our principal objective was to determine the effectiveness of program controls and USAID/Dominican Republic's monitoring of the dollar resources provided as well as the local currency generated in connection with the transfer of these resources. We did not make an in-depth audit of these programs. With the exception of those items reported below, nothing came to our attention that would indicate program controls were not generally satisfactory. We interviewed key officials at USAID, the National Planning Office, the National Price Stabilization Institute, and the Central Bank of the Dominican Republic, and reviewed pertinent records at those institutions. Our survey covered dollar transfers totalling $133 million, commodity shipments valued at $81 million, and local currency disbursements of $68.3 million equivalent generated by transfer of economic support funds and $52.6 million equivalent from the sale of Title I commodities.

SURVEY FINDINGS AND RECOMMENDATIONS

Economic Stabilization and Recovery Program

Central Bank Fiduciary Role

As of May 1, 1985, the Central Bank had not disbursed RD $3,832,820 (pesos) to support more than 17 projects under the ESF and P.L. 480 Title I Programs, as requested by the Technical Secretary of the Presidency and approved by USAID.

The disbursement procedures established in Operational Letter No. 2 required that "The Technical Secretary of the Presidency will authorize the Central Bank, with the approval of USAID, the disbursement of funds for each individual project. The Central Bank will deposit in the National Treasury the amount requested."

2/ Amount had not been confirmed. Exchange rate: RD$1.00 ($53.3 m) and RD$2.55 ($27.7 m)

3/ Exchange rate: RD$2.55 ($22.5 m) and RD$1.00 ($53.3 m)

4/ Exchange rate: RD$1.00 ($51.4 m) and RD$2.55 ($1.2m)

The Central Bank claimed that it was trying to maintain the dollar exchange rate at acceptable levels and that the release of these funds would have upset the exchange rate. As a result of the action taken by the Central Bank, several Economic Support Fund and PL 480 Title I projects were stalled and some workers had been laid-off. Also, the intent of Operational Letter No. 2 had been thwarted.

During our exit conference USAID officials advised us they were aware of this problem and were taking the following corrective actions:

-- Internal USAID discussions were held to define the problem and develop approaches and solutions.

-- Meetings took place with the Technical Secretary to the President who shares the responsibility with AID of programming and managing these funds.

-- The Secretariat was provided a memorandum outlining the problem. The Secretariat contacted the Governor of the Central Bank to verify if the Central Bank was indeed not disbursing funds. The Governor advised the Secretariat that the Central Bank was no longer withholding disbursements and would direct his staff to meet with USAID and the Secretariat to resolve any outstanding issues.

In view of the actions initiated by the USAID, no recommendation is deemed necessary at this time. Also, the Mission stated in an August 2, 1985 response to a draft of this report that "As of July 17, 1985, checks were issued by the Central Bank for all requests for disbursement and were deposited with the GODR National Treasurer. Thus the Central Bank is no longer withholding disbursements."

Calculation of Local Currency Generated by Grant

Local currency generated by a December 1984 $50 million grant to be deposited in the pertinent special account at the Central Bank in our opinion should have produced RD $163.5 million instead of the RD $155.5 million, as calculated by the Central Bank.

The grant agreement required the grantee (GODR) to deposit all counterpart (pesos) generated by the transfer of dollars made available under the agreement in a special account established in the Central Bank no later than 30 days after the dollar transfer was made. The amount of counterpart currency that was to be provided would be calculated using the average market rate, as determined by the Central Bank, for the previous 30-day period.

The Central Bank calculated the generations from grant funding at the rate of RD $3.11 = US $1.0. However, the average rate for the previous 30-day period was actually RD $3.27. The latter rate was telephonically verified by the Central Bank to the USAID Controller's Office at our request. The Central Bank claimed that the RD $3.11 rate was a discounted rate that included a banking service charge. No banking service fee had been charged in the past. The Central Bank realized that it could not charge AID a banking service fee and that the discounted rate of RD $3.11 it had used was a mistake. The application of the RD $3.11 rate would have created a shortfall of RD $8.0 million when the total local currency generations were actually deposited in the special account.

The USAID stated that a letter outlining the problem had been sent to the Secretariat which identified a discrepancy amounting to approximately RD $8.0 million in the calculation of the amount of local currency to be generated from the cash transfer of US $50 million. We were informally advised by the Secretariat that the correct amount of pesos would be deposited. The USAID reaffirmed these actions in its August 2, 1985 response to a draft of this report.

In view of the action taken by USAID in this matter, we are not making a recommendation at this time.

Local Currency Generated by AID Loans

The GODR received additional Economic Support Fund loan funding when the original loan agreement was amended in May 1984. The additional amount of funds to be transferred to the GODR under loan 517-K-039B was $34.0 million to be disbursed in two separate tranches once the GODR had complied with certain conditions precedent. The first tranche of $20.0 million was transferred by AID and the appropriate amount of pesos was deposited by the GODR in the special account. However, as of May 15, 1985, the GODR had not deposited the total amount of pesos that could potentially have been generated by the second loan tranche of $14.0 million, and the USAID had not been officially informed as to how many pesos had been generated. A condition in the loan agreement provided that local currency (counterpart funds) be deposited in the special account at the Central Bank no later than 60 days after the disbursement of AID loan funds.

By September 14, 1984, the GODR deposited RD $14.0 million which it had apparently determined to be the appropriate amount of local currency to be deposited. Thus, the local currency generation was evidently calculated at the "official" exchange rate of one peso for one dollar instead of at the then current parallel market 5/ rate of RD $2.80 to US $1.00, which would have generated RD $39.2 million. However, as best we have been able to recreate the events at the time, it would appear from the record, and especially from a letter dated September 14, 1984 from the then USAID Director to the Secretariat, that the Mission expected an exchange rate other than the "official" one-to-one rate to be used for disbursement of this loan tranche.

Our inquiries with the Central Bank resulted in their advice to the effect that they felt they were obliged to use the "official" rate at the time because the Central Bank, and not a commercial bank, was designated as depository of the counterpart funds generated by the ESF loan. At the time of our review, the USAID agreed with the Central Bank's position, stating:

5/ An officially sanctioned rate for most commercial transactions.

> Per the agreement, the GODR has one year from the date of the dollar disbursements to provide evidence that the dollars were used to import eligible commodities from the U.S. The GODR has informed us that they have used these dollars to offset Letters of Credit that had been opened at the one to one rate and, therefore, the local currency generated was at the one to one rate.

We found the USAID's most recently enunciated position in this matter to be inconsistent with the Mission's 14 September 1984 notification to the GODR/Secretariat in which it advised that the USAID expected the "difference" between what had been deposited up to that date (RD $14 million) and what should ultimately be generated as a result of the $14 million loan tranche disbursement to be deposited in the special account within 145 days from the date of that letter.

Furthermore, the bilateral agreement between the United States and the Dominican Republic, signed January 11, 1962, stated in Article VI that:

> Funds used for purposes of furnishing assistance hereunder shall be convertible into currency of the Dominican Republic at the rate providing the largest number of units of such currency per U.S. dollar which, at the time conversion is made, is not unlawful in the Dominican Republic.

The GODR had yet to officially advise the Mission as to how many pesos were generated in connection with the disbursement of the $14 million loan tranche. In our opinion, this matter should be resolved quickly in the best interest of the U.S. Government.

Mission Comments

The USAID stated in its August 2, 1985 response to the draft of this report:

> The intent of the letter dated September 14, 1984 signed by the Mission Director was to ensure that the conversion rate used would provide the largest number of pesos per U.S. dollar that was legally possible at that time. This procedure was established because at that time the GODR permitted the operation of a legal parallel exchange market for dollar-peso conversion and we wished to ensure that all pesos generated from the use of the AID loan would be deposited in the special account if the GODR exchanged dollars in the parallel market. Subsequently, the Technical Secretary to the Presidency and the Central Bank have confirmed to us that the Central Bank was not legally empowered to operate at any rate except for the official rate of exchange (1 US dollar 1 RD peso) until the January 23, 1985 decree of the monetary board. Under these circumstances, AID dollar funds were used to pay

obligations incurred at the official one to one rate of exchange, and that only 34 million Dominican pesos were generated by the use of the dollar funds.

Notwithstanding the above, we have sent operational letter No. 41 to the technical secretary on July 26, 1985 requesting confirmation of the rate of exchange used to convert the dollars to Dominican pesos under that loan. We anticipate receiving written confirmation soon that the dollars were exchanged at the official exchange rate as outlined above.

OIG Response

Our position that the parallel market exchange rate should have been used for the generation of local currency is based on Article VI of the bilateral agreement and prior written notification by the USAID to the Technical Secretariat in September 1984 requesting the GODR to increase the amount it had deposited from the US $14 million loan disbursement.

Although the exchange rate of one peso to one dollar was the "official" exchange rate in the Dominican Republic, the parallel market exchange rate, approximately RD $2.80 to US $1.00, was not unlawful and was an officially sanctioned exchange rate available in the Dominican Republic at the time. As a result, we find that the transfer of $14 million could and should have generated at least RD $39.2 million at the most favorable rate then legally available for this transaction.

Our original recommendation read:

> USAID/Dominican Republic reiterate to Technical Secretariat of the Presidency (GODR) its official position first communicated to the GODR in September 1984 with respect to the total amount of local currency that should have been generated from disbursement of the second tranche of loan 517-K-039B ($14 million) by using the officially sanctioned parallel exchange rate of not less than RD $2.80 to the U.S. dollar.

In view of the Mission's August 2, 1985 response to our draft report, we are revising the recommendation, as follows:

> Recommendation No. 1
>
> We recommend that USAID/Dominican Republic obtain a formal legal opinion from AID's General Counsel as to whether or not, within the context of Article VI of the Bilateral Agreement and prior correspondence with the GODR, the GODR may rightfully deposit local currency in connection with disbursement of the second tranche of loan 517-K-039B ($14 million) at the official exchange rate of RD $1.00 to US $1.00. USAID/Dominican Republic should take whatever action is necessary to implement General Counsel's determination.

PL 480 Title I Program

Deposit of PL 480 Title I Sales Proceeds in Special Account

During 1984 the GODR imported over $27.7 million in commodities from the United States as authorized under the PL 480 Title I Program. The GODR estimated the proceeds from the sale of these commodities to be RD $70.5 million, which amount should have been deposited in the Special Account at the Central Bank. In this connection, INESPRE has claimed RD $13.0 million (pesos) for costs related to importing the commodities. However, this amount has not been verified.

The procedures established in a Memorandum of Understanding between the GODR and USAID provided that all proceeds from the sale of commodities financed by the PL 480 Title I Program be paid directly by commercial banks to the Central Bank no later than 60 days after the arrival of the commodities. INESPRE was to require, prior to the sale of the commodities, that all private purchasers (including INESPRE itself) of the commodities open irrevocable interest-bearing letters of credit through commercial banks in the amount of the contracted sales price in favor of the GODR. Furthermore, the Memorandum of Understanding required INESPRE to inform USAID in writing of, inter alia, the arrival date and disposition of the commodities, and the date of deposit in the Central Bank, through the commercial banks, of commodity sales proceeds.

INESPRE had not informed USAID in writing of the amount of local currency generated from the importation of PL 480 Title I (1984) program commodities valued at $27.7 million. Also, INESPRE had not yet provided the required documentation to substantiate its claimed costs related to the importation of these commodities. As a result, the USAID was not certain that the RD $70.5 million in sales proceeds claimed by INESPRE was accurate or whether INESPRE's operational costs were reasonable.

Because of its record of making late deposits of local currency generations, USAID has removed INESPRE from participation in future PL 480 Sales Agreements. The National Planning Office has been named as the GODR agency responsible for the procurement of the PL 480 Title I commodities. We believe this action was justified under the circumstances and that the organizational change will prove beneficial to the success of the program.

The USAID advised us that a letter was being prepared requesting the Technical Secretariat to obtain documentation from INESPRE to support the expenses it claimed it had incurred in importing Title I commodities under the 1984 agreement.

The delay in the deposit of net local currency sale proceeds by INESPRE effectively inhibits the planned uses of these generations.

Recommendation No. 2

We recommend that USAID/Dominican Republic obtain from the Technical Secretariat of the Presidency and the National Price Stabilization Institute:

a) complete information on the amount of local currency generated from the Title I commodities imported during 1984 valued at $27.7 million, and

b) supporting documentation for the National Price Stabilization Institute's claimed costs for importing those commodities.

Mission Comments

In its August 2, 1985 reply to the draft of this report the USAID stated that:

On May 30, 1985 USAID sent a letter to the Technical Secretariat (TSP) requesting clarification of discrepancies between the amount to be deposited as reported by INESPRE to USAID, and the amount actually deposited in the Central Bank. The same letter also requested that the TSP obtain and retain detailed records in support of INESPRE's claim of RD pesos 12.3 million in operating costs. USAID has not yet received a response to this letter. In a meeting on July 30, 1985 USAID provided a copy of the letter to the Technical Secretary, along with a request for followup action. The Technical Secretary agreed to request that INESPRE provide detailed information supporting its claim and to deposit any difference in the special account that could not be documented.

OIG Response

While the USAID has taken positive steps to address the recommendation, we are retaining recommendation 2 until we are advised that the requested clarification and documentation have been received and found acceptable by the USAID.

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