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AUDIT OF
USAID/INDONESIA PRIVATE VOLUNTARY ORGANIZATION CO-FINANCING PROGRAM
PROJECT NO. 497-0336

AUDIT REPORT NO. 2-497-86-07
July 22, 1986

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UNITED STATES GOVERNMENT

Memorandum

TO : Mr. William P. Fuller
Director, USAID/Indonesia

DATE: July 22, 1986

RIG/EA-86-269

FROM : Leo L. LaMotte
RIG/A/Manila

SUBJECT: Audit of USAID/Indonesia Private Voluntary Organization Co-financing Program; Project No. 497-0336

This report presents the results of audit of the USAID/Indonesia private voluntary organization (PVO) co-financing program. It was primarily an economy and efficiency audit. Specific audit objectives were to determine whether: USAID/Indonesia's system for approving and overseeing block grants was adequate; the PVO co-financing program was evaluated as required by Agency guidelines; and the PVOs established and maintained accounting systems which complied with AID fund control regulations.

The co-financing program succeeded in bringing development assistance to remote areas at minimal overhead costs. USAID/Indonesia, however, did not (1) establish an adequate system to ensure that block grant proposals were effectively reviewed before grants were awarded; (2) evaluate the co-financing program as required by Agency guidelines; and (3) ensure that PVOs were using accounting systems which complied with AID fund control regulations.

The audit report recommends that USAID/Indonesia provide improved guidance for staff members reviewing block grant proposals, evaluate the co-financing program, and assist participating organizations in upgrading their accounting systems.

USAID/Indonesia agreed with and took substantive and rapid action to implement all of the report recommendations. Consequently, the recommendations will be considered closed as of the report issuance date. USAID/Indonesia comments are attached as Appendix 3 to the report.

Thank you for the assistance extended to the audit staff on this assignment.

Attachment: a/s

EXECUTIVE SUMMARY

USAID/Indonesia was the first Southeast Asian Mission to implement a private voluntary organization co-financing program. The program was designed to provide small-dollar-value grants to American and local private voluntary organizations to develop and implement innovative, small-scale, subprojects. The subprojects were "co-financed" by the private voluntary organizations, which means that the recipient organizations are required to provide at least 25 percent of necessary funding from non-AID sources.

Beginning in 1974, USAID/Indonesia's co-financing program provided 26 such organizations with over $12 million to implement 110 subprojects. The program has funded subprojects, such as installation of handpumps and publishing of local language textbooks on development topics.

This was primarily an economy and efficiency audit. Specific audit objectives were to determine whether: USAID/Indonesia's system for approving and overseeing block grants was adequate; the co-financing program was evaluated as required by Agency guidelines; and the private voluntary organizations had established and maintained accounting systems which complied with AID fund control regulations.

AID regulations state that grantees must demonstrate potential management capacity to efficiently plan and implement development activities in their field of expertise. However, the USAID awarded block grants to organizations not having sufficient management resources to efficiently manage the grant funds. This occurred because the USAID grant proposal review committees had neither the necessary information on the organizations' management capabilities nor adequate instructions for evaluating block grants. As a result, the two block grants awarded by USAID/Indonesia, totaling over $800,000 were inefficiently managed and some of the funds were used for questionable developmental purposes. We recommended that the USAID/Indonesia develop improved criteria for evaluating block grant proposals to ensure that recipient organizations have the resources and ability to effectively carry out development activities. USAID management concurred with this recommendation and developed guidelines to assist reviewers in evaluating grant proposals.

Agency guidelines require that AID programs and projects be evaluated periodically to ensure that they are being effectively and efficiently implemented. The USAID/Indonesia program was never formally evaluated although it was implemented in 1974 before the programs of USAIDs/Philippines and Thailand which have both already benefitted from evaluations. This occurred because the co-financing program planning documents did not adequately address the need for formal evalua-

tion. As a result, this opportunity for making improvements needed in the management of the co-financing program was not identified or implemented. We recommended that USAID/Indonesia provide for a comprehensive evaluation of the co-financing program in accordance with Agency regulations. USAID management agreed with this recommendation and assembled a review team and hired consultants to perform an evaluation.

Agency regulations require that private voluntary organizations have adequate financial management systems to control and account for expenditure of AID funds. None of the three organizations in our test had adequate systems because the organizations and USAIDs did not devote enough resources to establishing, maintaining, and monitoring PVO accounting systems. As a result, USAID/Indonesia can not be assured that grant funds were properly expended or controlled. We recommended that USAID/Indonesia devote additional resources to upgrade private voluntary organization accounting systems. USAID management agreed with this recommendation and initiated the necessary assistance.

Office of the Inspector General

AUDIT OF USAID/INDONESIA
PRIVATE VOLUNTARY ORGANIZATION
CO-FINANCING PROGRAM

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AUDIT OF USAID/INDONESIA
PRIVATE VOLUNTARY ORGANIZATION
CO-FINANCING PROGRAM

PART I - INTRODUCTION

A. Background

Responding to increasing Congressional interest in encouraging the overseas operations of private voluntary organizations (PVOs), several AID Missions in Southeast Asia have instituted "umbrella" projects designed to help PVOs develop and implement innovative, small-scale, subprojects. These umbrella projects involve numerous grants to both American and local PVOs. The subprojects are "co-financed" by the PVO, which means that the recipient organizations are required to provide at least 25 percent of necessary funding for project activities from non-AID sources.

USAID/Indonesia was the first Southeast Asian Mission to implement a PVO co-financing program. As stated in the project paper, the program was established to multiply and improve local level development efforts in Indonesia in the priority sectors of AID assistance. Beginning in 1974, the program has provided 26 American and Indonesian PVOs with over $12 million to implement 110 subprojects. This amount included block grants totalling over $800,000. The program has funded PVO subprojects, such as installation of handpumps and publication of local language textbooks on development topics.

The USAID/Indonesia Office of Voluntary and Humanitarian Programs manages the program, with assistance from Mission technical and staff offices which review grant proposals as requested.

B. Audit Objectives and Scope

This was primarily an economy and efficiency audit of the USAID/Indonesia PVO co-financing program. Specific audit objectives were to determine whether: USAID/Indonesia' system for approving and overseeing "block" grants was adequate; the PVO co-financing program was evaluated as required by Agency guidelines; and the PVOs had established and maintained accounting systems which complied with AID fund control regulations.

The review included site visits to six subprojects on the Indonesian islands of Java, Bali and Kalimantan (Borneo). Subprojects were chosen on the basis of geographical site location, type of activity, dollar value of the subproject, and length of time since or until subproject termination. AID contributed about $1.5 million to these subprojects, representing about 12 percent of total program funding.

Interviews were held with beneficiaries and PVO, Mission and Indonesian government officials, and analyses were made of progress and trip reports maintained in USAID files. Internal controls were tested by (1) reviewing and analyzing the USAID procedures for choosing and monitoring block grants and (2) evaluating whether PVO financial systems adequately accounted for AID-supplied funds. This involved interviews with project managers and other Mission officials, and a comprehensive review of Mission files documenting those procedures.

In December 1978, the AID Area Auditor General East Asia issued Audit Report No. 2-497-79-3, entitled "USAID/Indonesia Co-financing & Operational Program Grants". This report addressed the development activities of a small number of PVOs. The current audit was the first to review the management of the co-financing program.

The audit work was performed during the period March through June 1986 and carried out in accordance with generally accepted government auditing standards.

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PART II - RESULTS OF AUDIT

The audit showed that (a) multi-subproject block grants were awarded to private voluntary organizations (PVOs) which either did not possess adequate resources to effectively manage multiple subprojects, or had used grant money to fund subprojects outside priority development areas; (b) USAID/Indonesia's PVO co-financing program had never been formally evaluated, as required by Agency regulations; and (c) PVOs were not keeping adequate accounting records to ensure AID grant funds were properly spent.

The PVO co-financing program has succeeded in bringing development assistance to remote areas at minimal overhead costs. For example, two subprojects had succeeded in establishing potable water supplies in isolated rural areas. Another had provided basic medical services to people living in remote jungle villages.

We recommended that USAID/Indonesia incorporate Agency evaluative criteria into guidelines for reviewing and approving multi-project block grants, provide for a thorough evaluation of the PVO co-financing program, and assist in upgrading to Agency standards PVO procedures in accounting for grant expenditures.

A. Findings and Recommendations

1. Selection and Implementation Criteria for Multi-Project Support ("Block") Grants Needs Clarification

AID regulations state that grantees must demonstrate potential management capacity to efficiently plan and implement development activities in their field of expertise. However, the USAID awarded block grants to private voluntary organizations (PVOs) not having sufficient management resources to efficiently manage the grant funds. This occurred because the USAID grant proposal review committees had neither the necessary information on PVO management capabilities nor adequate instructions for evaluating block grants. As a result, the two block grants awarded by USAID/Indonesia, totaling over $800,000 were inefficiently managed and some of the funds were used for questionable developmental purposes.

Recommendation No. 1

We recommend that USAID/Indonesia

a. develop a system to ensure that reviewers evaluating block grant proposals are provided with written evaluations which include an analysis of the private voluntary organization's success in implementing development projects and its management capabilities, and

b. develop specific guidance for evaluating block grant proposals, including instructions to consider AID Handbook 3 criteria for assessing probable effectiveness of proposed development activities.

Discussion

USAID/Indonesia developed the "Multi-Project Support", or block grant to reduce the USAID's administrative burden by choosing PVOs to manage numerous small-dollar-value co-financing subprojects, and to encourage more organizations to request small amounts of grant money for development purposes. Such grants were to be used to support the on-going development activities of other well-established American and local PVOs in Indonesia.

According to USAID procedures, the block grant PVOs were to submit an overall multi-project support proposal to the USAID. This proposal would be less detailed than standard project proposals, and allow the PVO to decide which local organizations to fund through subgrants. The block grantee would then monitor the implementation of the resulting subprojects and submit annual reports to the USAID on block grant activities.

Through the period of our audit, USAID/Indonesia had awarded block grants totaling about $862,000 to two private voluntary organizations.

Block Grantees Lacked Adequate Management Capabilities - AID Handbook 13, Chapter 4 states that grantees must demonstrate potential management capabilities to efficiently plan and implement development activities in their field of expertise. A Mission PVO Project Review Committee is charged with evaluating each co-financing block grant proposal and recommending approval or disapproval to the USAID Director. The USAID/Indonesia PVO co-financing project paper states that the burden is on the PVO to demonstrate to AID sufficient management capability and experience. The project paper noted that the PVO could fulfill this requirement by having documented successful working experience in Indonesia in implementing at least two or three AID-funded development projects.

For the PVO, block grants are inherently labor-intensive. The PVO must determine which subgrants to fund, monitor implementation, assist the subgrantee in overcoming implementation problems, and report subgrant results to the USAID. Nevertheless, USAID/Indonesia awarded a $100,000 block grant to a PVO with a staff of one in-country representative. This single representative managed the block grant, providing assistance for six or more new community development projects in Indonesia. Under the grant agreement, the grantee representative was to submit to the USAID quarterly narrative reports and financial reports detailing grant progress.

While attempting to manage the block grant, the grantee also managed two additional grants under the co-financing program. These grants totaled over $200,000 and involved subprojects in two of the remotest areas of Indonesia.

In our opinion, the grantee did not have sufficient staff resources to effectively manage such a diverse portfolio. The grantee was unable to provide necessary services to its subgrantees, reliably manage AID resources, or keep the Mission adequately informed of subproject status. For example:

-- Because the subgrant project activities were not monitored, the grantee representative did not take remedial action to ensure the continued operation of a jungle hospital financed in part with the grant funds. For instance, the subgrantee was told by Indonesia government officials that the hospital probably would have to close because "foreign" medical personnel would be required to leave the country. Subgrantee officials told us the representative never visited the project site to evaluate implementation or provide assistance. Had this been done, the grantee representative could have assisted by helping the subgrantee find replacement "local" medical personnel. Subsequent to our field visit, the grantee representative stated that actions had and will be taken to ensure the continued operation of the jungle hospital. However, the auditors found no record in the grantee, subgrantee or USAID files

that the grantee was aware of the possible closure of the hospital before the audit was performed.

-- The block grantee did not have sufficient accounting expertise to properly control AID funds. As a result, the grantee approved subgrants totalling $120,000, or $20,000 more than the AID grant. This can be attributed to not keeping adequate accounting records to ensure that subgrants did not exceed the total amount authorized in the block grant. Upon completion of the audit, the grantee representative notified the USAID that the $20,000 shortfall in funding would be absorbed by his organization if a follow-on AID grant was delayed or disapproved.

-- The grantee did not devote enough personnel resources to keep the USAID adequately informed of the status of other subprojects. In this regard, the implementation information received by the USAID from the grantee on project activities was quite limited. As a result, USAID officials acknowledged that they did not know whether these subgrant projects were being successfully implemented.

USAID/Indonesia, did not require the Mission project review committee to record its decisions in writing. Therefore, it was impossible to specifically trace the process used by the USAID to determine that this PVO was qualified to manage effectively.

Committee members, however, had little substantive evidence upon which to evaluate the grantee's prior performance. Committee members stated that although the grantee had received five previous AID co-financing grants, totaling about $313,000, they did not have written evaluations of these projects when reviewing the grant proposal. Further, they received no instructions to give particular consideration to the grantee's management capabilities when evaluating a block grant proposal. One USAID official concluded that given the grantee's limited capabilities, the block grant should not have been approved by the USAID project review committee.

In summary, in the absence of information from the grantee, the USAID did not know whether subgrants had been successfully implemented. Moreover, the subgrantees were operating without the oversight necessary to ensure that AID funds were effectively and efficiently utilized.

Block Grant Lacked Clear Objectives - AID Handbook 3, section 3B states that precise definition of objectives is a basic project design task. Also, preference for AID support will be given to programs that show the greatest promise of meeting the most urgent needs of the people who constitute the poorest majority. Handbook 3 further notes that assessment of probable effectiveness of projects will be based on factors such as the

impact on poor people (employment income); clarity of definition of the participant group; proposal of the grantee, or tie-in with other programs which ensure complementary efforts necessary to provide a higher standard of living to the target group.

The second block grantee received $762,851 to build up the capacity of Indonesian private organizations and to mobilize underprivileged people to better their living conditions by participating in new self-help organizations. Specifics on how these goals were to be reached were not addressed in the grantee project paper. Consequently, most of the grant funds used (about $200,000) as of the close of our audit were either spent for questionable development activities or the grantee could not show how the funds used were directly related to the block grant or Agency development goals.

The grantee awarded 26 subgrants through March of 1985. The subgrants provided training for various individual participant groups, such as extension workers and pupils in "Islamic schools".

One example of a subgrant of questionable developmental value was where the grantee spent over $7,500 in AID funds to send a staff member of an Indonesian "management education" institution to a "Cooperative Management" training course in Torino, Italy. Even the grantee concluded that the course's usefulness in developing the management of cooperatives (the primary reason the participant wanted to take the course) was probably not realistic. In any event, the grantee noted that this training course grant appeared to have been quite successful in opening the horizons of a young promoter of small business.

In another example, a block grant was used to help finance ($1,600) a forum between Indonesia and Japanese environmentalists which was held in Japan. Particular emphasis in forum deliberation was the Jakarta Bay pollution problem. While there is little doubt that the forum would raise the awareness of this environmental problem, its relationship in meeting Agency development objectives appeared to be marginal.

Despite Mission requests, the grantee did not provide any explanation of how training provided under the 26 subgrants directly involved the "poor" in the target area. Moreover, he could not, in the opinion of Mission management, adequately explain the criteria it used to choose subgrantees.

Following completion of the audit, USAID/Indonesia analyzed the 26 subgrants. While the Mission concluded that its analysis showed that grant funds were basically used for institutional development of grassroots organizations, the analysis did not establish a connection between the training and direct benefit to the "poor majority" in Indonesia. See Appendix 1 for the Mission analysis of the 26 subgrants.

In summary, USAID/Indonesia developed the block grant to more efficiently utilize PVO co-financing program funds. Grantees were to be given increased responsibilities in choosing and monitoring subgrantee development projects. Grantees would assume an enhanced role in ensuring that subgrantees were able to meet and solve implementation problems. Thus, the USAID could use less resources by not participating directly in the management of a portion of the co-financing program. The saved resources could then be devoted to other USAID development activities. To realize these potential benefits, however, USAID/Indonesia should improve its procedures for reviewing block grant proposals. Grant proposal reviewers should have clear statements of a block grant's objectives, the criteria the grantee will use in awarding subgrants, and the grantee's management capabilities. With such information, reviewers would be better able to evaluate proposals and ensure that block grants are carried out effectively.

Management Comments

Mission management agreed with this recommendation and developed guidelines to assist reviewers evaluating block grant proposals. These guidelines state that evaluators should consider PVO management capacity when reviewing proposals. Further, the guidelines noted that grant awards should be made to PVOs which have demonstrated competence in implementing previous co-financed or USAID-supported, project activities, with a proven track record in achieving prior stated project objectives. In addition, reviewers would be provided with such information before beginning their evaluations. The instructions also stated that the proposal shall have a clearly-stated management plan/mechanism for implementing the block grant and the personnel resources to carry out that plan.

Office of The Inspector General Comments

Since USAID/Indonesia has adequately addressed our audit concerns, Recommendation No. 1 will be closed as of the report issuance date.

2. USAID/Indonesia Should Evaluate the Co-financing Program

Agency guidelines require that AID programs and projects be evaluated periodically to ensure that they are being effectively and efficiently implemented. The USAID/Indonesia program was never formally evaluated although it was implemented in 1974 before the programs of USAIDs/Philippines and Thailand, which have both already benefitted from evaluation. This occurred because the co-financing program planning documents did not adequately address the need for formal evaluation. As a result, this opportunity for making improvements needed in the management of the co-financing program was not identified or implemented.

Recommendation No. 2

We recommend that USAID/Indonesia

a. arrange within the near future an evaluation of the private voluntary organization co-financing program, as discussed in AID Handbook 3, and

b. include an evaluation plan in compliance with AID regulations in subsequent private voluntary organization co-financing programs.

Discussion

The Foreign Assistance Act of 1961 and AID regulations require that the Agency evaluate its development projects periodically. According to AID Handbook 3, evaluation refers to the general process, and specific activities undertaken to analyze and assess the performance and results of projects, programs, policies and procedures. Evaluations seek to determine whether a project, program, policy or procedure is achieving planned results and to measure their intended and unintended impact. Furthermore, Handbook 3 states that the essential elements for evaluation will be incorporated into all project designs from their earliest stages.

Since its inception in 1974, USAID/Indonesia had not formally evaluated the PVO co-financing program. At the time of our audit, the USAID had no firm plan to evaluate the program. The current USAID/Indonesia PVO co-financing program was scheduled to end in 1986. The Mission planned either to amend the project documents or to develop and implement a follow-on PVO co-financing program thereby extending funding through 1991.

While the program was never evaluated, one early program planning document supporting the project paper outlined a two-tiered evaluation system. At the subproject level, evaluations were to be performed by the private voluntary organization.

However, at a higher level, the program planning document merely stated that AID will evaluate whether AID has been able to engage the expertise of PVOs working in Indonesia and whether the AID contribution has resulted in a net increase in PVO sponsored development activity.

In our view, this instruction was insufficient to ensure productive and effective evaluation of the program. Such an evaluation, even if undertaken, would not have addressed the issue of the PVO co-financing program's success in reaching goals delineated in the planning document. [1] Moreover, it would not have addressed issues such as impact upon beneficiaries and continuing relevancy to Indonesia development.

USAID/Philippines and USAID/Thailand, both of which manage similar PVO co-financing programs, evaluated initial co-financing projects before embarking on follow-on co-financing programs. According to Mission managers of these USAIDs, both evaluations resulted in substantial alterations to program management procedures, which they felt greatly strengthened their programs. In the Philippines, for example, evaluators determined that:

-- Greater staff resources were needed to efficiently run the program. An additional contractor was subsequently hired to provide increased monitoring and managing capability.

-- The Mission should encourage the PVOs to submit smaller, less complex subprojects, with shorter implementation periods and a more immediate impact on development.

-- Explicitly stated quality criteria should be adopted for reviewing proposals. The criteria should indicate which specific factors should be used to evaluate each proposal.

-- The USAID should provide PVOs with more assistance during the subproject identification and proposal preparation stage.

-- The Mission should improve monitoring capabilities.

In Thailand, the evaluators determined, among other things, that:

-- The Mission should put more of its management time into working with the PVOs in the conceptualization and design phases of their proposal development.

-- The Mission should give greater consideration to analyzing PVO staff resources when approving grants.

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[1] A listing of project goals can be found at Appendix 2.

In summary, evaluations are important management tools. They can identify implementation problems, and help managers determine whether their projects are achieving desired objectives. AID missions managing PVO co-financing programs in other areas of Southeast Asia found that by implementing evaluation recommendations, they improved their co-financing programs. USAID/Indonesia should also evaluate its co-financing program to gauge its effect and shortcomings so that improvements can be made in program administration and implementation.

Management Comments

Mission management agreed with this recommendation and initiated action to evaluate its co-financing program. The Mission has begun Phase I of the evaluation. During this phase, it plans to review, organize and update data on co-financed subprojects; prepare summary data for a computerized co-financing database; and prepare and test an integrated computer software package for analysis of co-financing data. During the evaluation's second phase, the Mission will assess the co-financing program's success in meeting its objectives; assess the efficiency and effectiveness of the current subproject selection and monitoring procedures; and assess the strengths and weaknesses of the block grant strategy. The evaluation is scheduled to end by July 31, 1986. USAID/Indonesia's amended project paper, carrying the co-financing program into 1991, contains an expanded evaluation plan. This plan calls for the overall program evaluation now in progress, as well as an interim evaluation in 1989, and a final evaluation in 1991. These evaluations will stress issues such as cost-effectiveness, institutional development, and sustainability of subprojects.

Office of Inspector General Comments

USAID/Indonesia has taken the required measures to satisfy our audit concerns with respect to evaluation of the PVO co-financing program. Therefore, Recommendation No. 2 will be closed as of the report issuance date.

3. Private Voluntary Organizations Need Assistance in Developing Accounting Systems which Comply With Agency Fund Control Requirements

Agency regulations require that private voluntary organizations (PVOs) have adequate financial management systems to control and account for expenditure of AID funds. None of the three organizations in our test had adequate systems because the organizations and USAID did not devote enough resources in establishing, maintaining, and monitoring the systems. As a result, USAID/Indonesia can not be assured that grant funds were properly expended or controlled.

Recommendation No. 3

We recommend that USAID/Indonesia survey participating private voluntary organization accounting systems, and take steps to upgrade those systems, where necessary, to acceptable Agency standards.

Discussion

Office of Management and Budget Circular No. A-123 defines internal controls as the plan of organization and all of the methods and measures adopted within an agency to safeguard its resources, assure the accuracy and reliability of its information, assure adherence to applicable laws, regulations and policies, and promote operational economy and efficiency. It also states that, as a matter of policy agencies shall maintain effective systems of accounting and administrative controls.

According to AID Handbook 13, the grantee's financial management system shall provide for:

a. accurate, current, and complete disclosure for each AID-sponsored project or program;

b. effective control over and accountability for all funds, property, and other assets; and

c. accounting records that are supported by documentation that at a minimum will identify, segregate, accumulate, and record all costs incurred under a grant.

Of the six PVOs in our sample, accounting systems were reviewed for three PVOs. None of these PVOs met the accounting standards required by A-123 or AID regulations. For example

-- One local PVO was unable to produce documents to adequately support AID expense of $20,748, from a total grant of about $40,000. The PVO had also failed to segregate AID funds from other sources.

-- Another PVO, managing a $60,000 grant, failed to segregate AID funds.

-- A third PVO, managing a grant of about $300,000, did not segregate or keep separate books of account for AID funds. It also was not possible to trace grant expenditures from bookkeeping records kept at the subproject site.

Mission records showed that a fourth PVO's financial system was inadequate to account for expenditures of the $164,000 grant. The PVO was not maintaining transaction ledgers, purchases were not properly documented, and some costs were improperly charged to the grant.

Mission managers acknowledged that PVO accounting practices were often inadequate, but stated that, in view of Agency staffing constraints, AID could do little more than sample a small number of accounting systems on an ad hoc basis. Only one of the six PVOs in our sample had its local subproject accounting records audited by any source during the life of the grant. Indonesian accounting firms, we were told, charge about $4,000 to perform financial audits, a prohibitive sum for marginally financed local PVOs. The PVOs, often operating on very small budgets, did not, in the opinion of Mission managers', possess the capability of upgrading their financial systems without assistance.

USAID/Philippines, encountering a similar problem in managing its PVO co-financing program, hired a local management firm to systematically review PVO accounting systems and upgrade those systems to meet Agency standards. Funds were provided through the co-financing budget. Managers at that Mission stated that such action greatly improved the accounting practices of participating PVOs. We believe that USAID/Indonesia should consider similar action to improve program financial management.

In summary, USAID/Indonesia does not know whether the PVO co-financing program grant funds are properly controlled and expended. The Mission must assist participating PVOs to upgrade their record-keeping and accounting system. Only then will the co-financing program meet Agency fund control standards.

Management Comments

Mission management agreed with this recommendation and took action to strengthen and improve the accounting and financial management capabilities of PVOs participating in the co-financing program. By the close of our audit, the Mission was in the process of contracting with a consultant firm to produce a Financial Management Manual for PVOs. This manual would, among other things, cover "an entire double-entry accounting system including a basic chart of accounts, books of original entry such as cash journal and general journal, general ledger and its subsidiary ledgers, project and subproject ledgers." It

would also include a discussion of AID and A-123 requirements for grantee accounting systems. The consultants will be asked to conduct a brief workshop instructing PVOs on the use of the Manual. Further, the consultant will survey a number of PVO accounting systems to "upgrade those systems, where necessary, to acceptable USAID standards."

Office of Inspector General Comments

USAID/Indonesia has taken positive and substantive action to comply with our recommendation. Therefore, Recommendation No. 3 will be closed as of the report issuance date.

B. Compliance and Internal Controls

Compliance

As discussed in this report, we found that the USAID/Indonesia Private Voluntary Organization (PVO) co-financing program was not complying with Agency standards for

-- project development and

-- evaluation.

Our recommendations were directed toward correcting these problems. During the audit, we noted no other areas of non-compliance with applicable laws and regulations.

Internal Controls

We found that the USAID/Indonesia PVO co-financing program suffered from a material internal control weakness in the inability of participating PVOs to adequately account for AID grant funds in their possession. We have recommended Mission action to correct this deficiency.

AUDIT OF
USAID/INDONESIA PRIVATE VOLUNTARY
ORGANIZATION CO-FINANCING PROGRAM

PART III - APPENDICES

APPENDIX 1

USAID/Indonesia Analysis of PVO Subgrants Under "Training" Block Grant

Out of 26 subgrants:

-- Eighteen grants were for training, primarily for community extension workers, but a few for leadership and management positions;

-- There were 293 trainees in 14 provinces;

-- Of the leadership trainees, the PVO has maintained contact with 28 and can document effective development activity of 20;

-- Two grants were for pesantren (Islamic schools) development activities. This was an important innovation with institutions considered to have primary influence over some 20 million people in Indonesia. These grants laid the groundwork for dozens of pesantrens now involving their pupils in development activities;

-- Six grants were for improving management of grassroots PVOs; and

-- The PVO's findings are that six of the 26 grants ($35,000 out of $247,000) failed to achieve objectives.

APPENDIX 2

Project Goals [1]

1. Increased access to, and attainment of, training and education opportunities.

2. Reduced rates of unemployment and underemployment.

3. Increased levels of national income accompanied by more equitable distribution of national income.

4. Reduced infant motality and controlled population growth.

5. Increased number of U.S. and Indonesian PVOs collaborating with local counterparts in local development projects.

6. Increased capacity of PVOs to design and implement local development projects.

7. PVOs working in increasing number of GOI and AID policy areas.

8. Increased direct development impact on targeted beneficiaries from PVO/USAID development assistance programs.

9. Increased PVO/USAID emphasis on impact analysis and evaluation of their project.

10. Ten to 20 participating American PVOs.

11. Five to ten participating Indonesian PVOs.

12. Six to 80 projects undertaken.

13. Four hundred to 600,000 beneficiaries.

14. Six to ten training interventions.

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[1] From Project Paper.

UNITED STATES GOVERNMENT

memorandum

DATE: April 25, 1986

REPLY TO ATTN OF: William P. Fuller, USAID/Director, Indonesia

SUBJECT: Response to Draft Audit of PVO Co-Financing Project 497-0336

TO: Mr. Leo L. LaMotta, RIG/A/Manila

LaMotta to Fuller Memorandum of April 1, 1986

The Mission appreciates the inclusion in the Draft Audit of many comments from Mr. Coggins' memorandum of February 21, 1986, to Mr. Burns.

I believe the enclosed documentation will suffice to close the three recommendations of the Draft Audit:

Recommendation No. 1.

"We recommend that USAID/Indonesia

a. develop specific guidance for reviewers evaluating "block" grant proposals, including instructions to consider AID Handbook 3 criteria for assessing probable effectiveness, and

b. develop a system to ensure that reviewers evaluating "block" grant proposals are provided with written evaluations of the private voluntary organization's success in implementing previous AID development projects, including a comparison of achievements and goals as stated in prior grant agreements, and a statement of the organisation's management resources."

In response to this recommendation, please find (1) a copy of "Implementing Guidelines and Criteria for Review and Selection of Co-Financed Multi-Project Support (MPS) Grants," prepared by the VHP office and now being utilized in all MPS proposal reviews; and (2) a copy of the scope of work for the evaluation, now underway, of the PVO Co-Financing Project (MPS references marked). We request that this recommendation be closed.

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Recommendation No. 2

"We recommend that USAID/Indonesia

a. arrange in the near future an evaluation of the current Private Voluntary Organization Co-Financing Program, as discussed in AID Handbook 3, and

b. include an evaluation plan in compliance with AID regulations in the new Private Voluntary Organization Co-Financing Program."

As stated above, the evaluation is now underway. In addition to the copy of the Scope of Work, please find enclosed a copy of the PIO/T for the services of the archival specialist required in the initial phase of the evaluation. We request that this recommendation be closed.

Recommendation No. 3

"We recommend that USAID/Indonesia take action to survey participating private voluntary organization accounting systems, and upgrade those systems, where necessary, to acceptable Agency standards."

In response to this recommendation, please find enclosed (1) copy of memorandum dated 1/28/86 from the Mission Controller to VHP suggesting a method of responding to Recommendation No. 3; (2) a PIO/T for the services of financial management experts in producting in English and Bahasa Indonesia a financial management manual, conducting a workshop on its use, and surveying/upgrading as required six participating PVO accounting systems; and (3) copy of a letter dated April 3, 1986 from the Mission's Finance Office to USAID/Manila requesting a copy of a similar manual prepared by that Mission (copy of the manual now in hand). We request that this recommendation be closed.

As a general response to the draft audit, we are also enclosing:

-- a copy of the Project paper amendment for PVO Co-Financing II, dated October, 1985. Sections which address audit issues have been highlighted with a yellow marker.

-- a copy of a USAID Order, "Procedures for Approval of PVO Projects Within USAID Project, " dated February 10, 1986.

-- a copy of the PIO/T for the services of an expert consultant to assist in preparing a computerized database for PVO project evaluation and reporting.

-- a copy of a PIO/T for the services of a consultant to assist in the generation, selection, and review of MPS grants, as well as assistance in initial project implementation. The last includes the development of effective monitoring and reporting systems.

- copy of a letter to VHP from William Bergquist of Save the Children, West Java, dated 17 April. In the letter Mr. Bergquist states that the "earthen dam" in the referenced report was constructed by GOI funds and had no relation to the PVO Co-Financing grant from USAID.

Let me respond briefly to paragraph 3 of the cover memorandum in which you requested amplification of the actions of the "block" grantee. A field office has been set up in each of the three areas on which the subgrants focus. In J . n Jaya the agency's project consultant is an agriculturist (Masters' Degree, Ohio State University). In East Kalimantan a local m. experienced in community development has been hired. In West Kalimantan an experienced American has accepted the responsibility on a voluntary basis as a part of his missionary responsibility. These field officers will be responsible for proposal development with grassroots groups and monitoring of funded projects. A serious recruitment effort is underway to recruit an Indonesian national who will be trained for assumption of the Country Director position. Considering that the block grant is for $100,000, this may be tending to staff overkill. On accounting, Mr. Diedrich of the Mission's Finance Office examined the agency's records and found them in compliance with Aid financial management guidelines. The PVO will participate in the planned training course in the use of the financial management manual described in response to Recommendation No. 3.

In conclusion, let me state that the Draft Audit's conclusion that the Co-Financing program provides aid "to a wide variety of beneficiaries at relatively low cost" has a necessary corollary. We must keep the cost-benefit ratio low for these projects to be worthwhile. The Indonesian archipelago is large and travel costs quite expensive. To assist grassroots groups in isolated areas is an important part of the Mission's country development strategy. We expect that the current evaluation of the PVO Co-Financing Project will provide clear evidence of the impact of these efforts and will provide further impetus to strengthen them.

Drafted:
VHP:RCCoggins:as

Clearance:
FIN:TDiedrich in draft
A/DD:JSperling

#3799P

APPENDIX 4

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