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AUDIT  
OF USAID/HONDURAS'  
NATURAL RESOURCES MANAGEMENT  
PROJECT NO. 522-0168

Audit Report No. 1-522-86-25  
July 28, 1986

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

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**AGENCY FOR INTERNATIONAL DEVELOPMENT**

OFFICE OF THE REGIONAL INSPECTOR GENERAL  
AMERICAN EMBASSY  
TEGUCIGALPA — HONDURAS

TELEPHONES:  
32-0044 & 32-0092  
also 32-3120/9, EXT. 293 & 296

July 28, 1986

MEMORANDUM

TO : D/USAID/Honduras, Anthony Gauterucci  
FROM : RIG/A/T, *Linage Gothard* Coinage Gothard  
SUBJECT : Audit of USAID/Honduras' Natural Resources Management  
Project No. 522-0168

This report presents the results of our review of your Mission's Natural Resources Management Project. We made a program results audit of this activity in order to determine whether it was achieving its objectives and also to evaluate selective aspects of project operations relating to its efficiency and economy, and adherence to AID policies and regulations.

The Natural Resources Management Project's effectiveness was limited by nonadjustment of goals to completed land use studies, nonadherence to the project's special covenants, planning and execution weaknesses in implementing the project on the part of the main host country implementing agency, significant shortfalls in counterpart funding, and inadequate emphasis on protecting existing forests from fires. Measuring the project's effectiveness was impeded somewhat by a lack of financial and physical progress reports from the National Cadaster Agency and the Office of Hydrologic Resources. The efficiency of project operations was inhibited by late and incomplete submissions of annual detailed implementation plans, and sporadic resource flows to field offices each year. The Ministry of Natural Resources' disbursement procedures caused unnecessary delays in project implementation and also caused the project to lose three to four months' implementation time each year. Internal controls were deficient in several areas including the commingling of this project's funds with other AID funds; annual project plans were incomplete and late. The audit disclosed several instances of noncompliance with AID requirements such as incomplete counterpart reports, and nonadherence to special covenants.

During a two week field trip, we observed a number of project activities which were successful. We observed hundreds of meters of well-built stone walls constructed for soil retention and control of water runoff. A number of terraced plots showed no signs of erosion. Project beneficiaries reported that they supported the program of stone wall conservation works because it cleared their fields of rocks to make the walls and they received needed subsidies for this work. Many hectares of reforested land were observed along with some range management and

pasture improvement activities. We visited a number of community tree nurseries which were successfully producing thousands of seedlings for reforestation activities. Clearly, this activity has had certain beneficial impact in the project area.

While these activities were successful and, in some cases, even impressive, they were well below the goals and objectives set forth in the Project Agreement. We estimated that after more than five years, the project had achieved only a small portion of its policy and planning objectives, about one-third of its natural resources data collection and analysis goals and about one-fourth of the activities planned for the five Choluteca subwatersheds. About \$7.3 million in AID funds had been disbursed as of December 31, 1985 despite the fact that some special covenants of the project had not been met. The major host country implementing agency demonstrated serious administrative weaknesses and host country counterpart funding was well below agreed upon limits. The goals of the project paper appeared to be overly optimistic in some cases while, in our opinion, providing inadequate emphasis on the protection of existing watershed resources. We noted that only two percent of agroforestry and fuel production clean-up activities (removing underbrush, dead and damaged trees) were successfully completed. Since little progress in the agroforestry and fuel production activities had been made, we believe this contributed to weaknesses in the protection of existing resources because the danger of forest fires was not diminished by cutting out dead and damaged trees and removing underbrush which served to fuel brush fires. We noted several internal control weaknesses including the commingling of AID project funds; annual project plans were incomplete and late. Several compliance problems were also observed such as incomplete counterpart reports and noncompliance with special covenants.

Our recommendations seek to correct both systemic and project-specific deficiencies encountered during the course of our review. Please advise this office within 30 days of the actions taken or planned to implement the remaining open recommendation in this report.

## EXECUTIVE SUMMARY

Honduras faces serious problems in trying to conserve its watersheds from deforestation, erosion, fire and loss of soil fertility. To address these watershed problems, the Government of Honduras and USAID/Honduras signed a \$22.0 million agreement on July 31, 1980 for the Natural Resources Management Project (\$15.0 million USAID funds, \$7.0 million host country equivalent). There have been five amendments to the project; current AID life-of-project funding includes a \$2.7 million USAID grant and a \$12.3 million USAID loan. The project's completion date is July 30, 1987. The purposes of the project are to strengthen Honduran institutions that manage natural resources; increase the incomes for farmers in an important southern (Choluteca) watershed; and conserve soil and water resources there by modifying the agricultural and forestry practices.

The Office of the Inspector General conducted a program results audit of the Natural Resources Management Project covering activities from July 31, 1980 through April 9, 1986. The audit objectives were to determine the project's success in achieving planned results, the effectiveness of project operations, compliance with USAID requirements, and the adequacy of internal controls.

The project has three components: (1) Natural Resources Policy and Planning, (2) Natural Resources Data Collection and Analysis, and (3) the Choluteca Watershed Management Program. The Natural Resources Policy and Planning component completed two studies -- one on land titling and another on marketing.

The Natural Resources Data Collection and Analysis component successfully completed: five Choluteca subwatershed soil surveys; upgraded 17 hydrology stations; constructed 12 new hydrology stations; completed five ecology and forest classification studies; five forest delineation activities; and five actual and potential land-use studies. The Choluteca Watershed Management component protected 4,073 hectares of land with soil and water conservation works; improved 174 hectares of forest through agroforestry and fuel production clean-up activities; reforested 1,107 hectares of land; improved 1,140 hectares with better range management and pasture improvement activities; produced 1.9 million seedlings in project community nurseries for reforestation; established 209 community and women's groups to carry out project activities; and provided \$489,000 in credit for project related loans and subsidies.

Nevertheless, project accomplishments fell far short of those originally planned; furthermore, the goals and outputs as stated in the project agreement had not been revised. By our estimate, the project achieved only a small portion of component one's original policy and planning activities while having disbursed about 27 percent of USAID's originally authorized project budget. About one-third of component two's original data collection and analysis activities were completed while about 93 percent of USAID's originally authorized budget was spent. Only about one-fourth of component three's original Watershed Management activities were successfully accomplished, although about 36 percent of the originally authorized USAID funds were spent.

About \$7.3 million in USAID funds had been disbursed as of December 31, 1985 despite the fact that, in our opinion, some special covenants of the project were not met. The major host country implementing agency experienced serious administrative shortcomings and host country counterpart contributions to the project had been well below agreed upon limits. The goals and outputs of the Project Agreement appeared to be overly optimistic in some cases while, at the same time, not providing adequate emphasis on the protection of existing watershed resources. We concluded that the lack of success in agroforestry and fuel production clean-up activities had contributed to weaknesses in the protection of existing resources because the danger of forest fires had not diminished in those areas where cutting out dead and damaged trees and removing underbrush had not taken place.

We noted six internal control weaknesses including commingling of USAID project funds. Annual project plans were incomplete and late. Six compliance problems were observed including inadequate and incomplete host country counterpart reports, and noncompliance with special covenants.

We have recommended revising the project's original goals and objectives to reflect completed land use studies and actual economic and governmental activities in the region; suspending further disbursements until special covenants are revised or met; requiring the Government of Honduras to improve its project administration; programming \$3.4 million in GOH funds; reevaluating the project's design to consider initiating activities to protect existing forest resources; reconciling and opening a separate account for funds advanced under this project; assisting the Government of Honduras to undertake required annual financial audits; and obtaining required counterpart reports from certain nonreporting host country agencies.

The recommendations included in this report are designed to address both project-specific and systemic deficiencies disclosed as a result of the audit.

*Office of the Inspector General*

AUDIT  
OF USAID/HONDURAS'  
NATURAL RESOURCES MANAGEMENT PROJECT  
PROJECT NO. 522-0168

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PART I - INTRODUCTION

A. Background

With an area of more than 43,000 square miles (about the size of Tennessee), Honduras is the second largest Central American country. In 1985 it had a population of about 4.4 million of which (1981 data indicated) about 60 to 65 percent were rural inhabitants and 35 to 40 percent urban. According to USAID/Honduras' Country Development Strategy Statement, estimated per capita income was \$675 (1981 estimate), making Honduras the poorest country in Central America. The Project Paper stated that rapid population growth in the past several decades had put great pressure on Honduran watersheds, resulting in increased deforestation, erosion, and soil depletion.

To reverse natural resource degradation, the Government of Honduras (GOH) and USAID/Honduras entered into the Natural Resources Management Project. The project's purposes were to: strengthen institutional mechanisms by which Honduras manages its natural resources; increase incomes of farmers in a southern (Choluteca) watershed; and conserve the natural resources of the soil and water in that watershed through modified agricultural and forestry practices. Primarily through this project, the GOH planned to improve the ineffective management of the country's water and land resources, diminish the rate of destruction of the country's forested areas, and eliminate destructive cultivation practices.

On July 31, 1980 USAID/Honduras and the GOH signed loan and grant agreements for the Natural Resources Management Project totaling \$15 million in USAID funds and \$7 million in equivalent GOH funds. There were five amendments to the project and current life of project contributions are \$2.7 million in USAID grant funds and \$12.3 million USAID loan funds. The project completion date has been extended to July 30, 1987. A GOH Agricultural Policy Commission was to provide overall direction and guidance to the project and a Project Office at the GOH Ministry of Natural Resources was to be the principal implementing unit. Two other GOH agencies, the National Cadaster Agency and the Hydrologic Resources Office, were to assist in natural resources data collection and analysis activities.

To meet the goals of the project, the Project Agreement included funding for the following components:

1. Natural Resources Policy and Planning, which was to provide for the establishment of a system of land use classification, land zoning, and reviews of proposed new development projects from the point of view of appropriate land and natural resources uses;

2. Natural Resources Data Collection and Analysis, which was to gather and analyze natural resources data, undertake soil surveys and laboratory work, improve hydrology and climatology services, complete ecology and forest classification studies, and forest delineation efforts, formulate actual and potential land-use classifications, and furnish cadaster surveys and general project support; and
3. The Choluteca Watershed Management Program, which was to oversee activities in soil conservation and intensive agricultural practices, agroforestry and fuelwood production activities, reforestation activities, range management and pasture improvement, community nurseries and tool grants, watershed management credit funds and grant activities.

B. Audit Objectives and Scope

The Office of the Regional Inspector General for Audit/Tegucigalpa reviewed USAID/Honduras' Natural Resources Management Project from its inception on July 31, 1980 to April 9, 1986. The audit covered \$7.3 million in AID accrued and disbursed expenditures and \$1.6 million equivalent GOH contributions as of December 31, 1985. Audit field work was conducted from January 20 to April 9, 1986.

Audit objectives included determining:

- success in achieving planned results,
- effectiveness of project operations,
- compliance with AID requirements, and
- adequacy of internal controls.

To accomplish these objectives, we reviewed project files and interviewed project officials at USAID/Honduras, the Ministry of Natural Resources, the National Cadaster Agency, Hydrologic Resources Office, Central Office of the National Agricultural Development Bank, Choluteca Regional Project Office, Forest Development Corporation (COHDEFOR), Choluteca branch of the National Agricultural Development Bank (BANADESA), and GOH Ministry of Finance. We visited eleven watershed management units in four subwatersheds and observed a wide range of project activities. We interviewed 55 project field and administrative personnel and 128 project beneficiaries, and examined documentation supporting expenditures of \$6.0 million in AID expenses and \$1,344,000 in advances of AID funds.

The audit was performed in accordance with generally accepted government auditing standards.

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PART II RESULTS OF AUDIT

The Natural Resources Management Project's effectiveness was limited by nonadjustment of goals to completed land use studies, nonadherence to the project's special covenants, planning and execution weaknesses in implementing the project on the part of the main host country implementing agency, significant shortfalls in counterpart funding, and inadequate emphasis on protecting existing forests from fires. Measuring the project's effectiveness was impeded somewhat by a lack of financial and physical progress reports from the National Cadaster Agency and the Office of Hydrologic Resources. The efficiency of project operations was inhibited by late and incomplete submissions of annual detailed implementation plans, and sporadic resource flows to field offices each year. The Ministry of Natural Resources' disbursement procedures caused unnecessary delays in project implementation and also caused the project to lose three to four months' implementation time each year. Internal controls were deficient in several areas including the commingling of this project's funds with other AID funds; annual project plans were incomplete and late. The audit disclosed several instances of noncompliance with AID requirements such as incomplete counterpart reports, and nonadherence to special covenants.

During a two week field trip, we observed a number of project activities which were successful. We observed hundreds of meters of well-built stone walls constructed for soil retention and control of water runoff. A number of terraced plots showed no signs of erosion. Project beneficiaries reported that they supported the program of stone wall conservation works because it cleared their fields of rocks to make the walls and they received needed subsidies for this work. Many hectares of reforested land were observed along with some range management and pasture improvement activities. We visited a number of community tree nurseries which were successfully producing thousands of seedlings for reforestation activities. Progress reports indicated the following accomplishments as of December 31, 1985:

- 1 completed study in land tenure;
- 1 completed study in marketing;
- 17 upgraded hydrology stations;
- 12 newly constructed hydrology stations;
- 5 completed Choluteca subwatershed ecology and forest classification studies;
- 4,073 hectares of land protected with soil and water conservation works;
- 174 hectares of existing forests improved by agroforestry and fuel production activities;
- 1,107 hectares of land reforested;

- 1,140 hectares of land improved by range management and pasture improvement planting activities;
- 1.9 million seedlings produced by project-created community nurseries for reforestation efforts;
- 209 community and women's groups established to carry out project activities; and
- \$489,000 in credit provided for project related loans and subsidies.

In their June 23, 1986 response, the Mission suggested we add the following project accomplishments which had not been provided to us during the audit:

- 3412 hectares of land protected through fire control vigilance and fire break construction;
- 341.6 kilometers in shrub fences;
- 15 kilometers of firebreaks; and
- 209.4 kilometers of windbreaks.

While these activities were successful and, in some cases, even impressive, they were well below the goals and objectives set forth in the Project Agreement. <sup>1/</sup> We estimated that after more than five years, the project had achieved a small portion of component one's policy and planning activities, about one-third of component two's natural resources data collection and analysis activities, and about one-fourth of component three's activities in the five Choluteca subwatersheds. About \$7.3 million in AID funds had been disbursed as of December 31, 1985 despite the fact that some special covenants of the project had not been met. The major host country implementing agency demonstrated serious administrative weaknesses and host country counterpart funding was well below agreed upon limits. The goals of the project paper appeared to be overly optimistic in some cases while, in our opinion, providing inadequate emphasis on the protection of existing watershed resources. We noted that only two percent of agroforestry and fuel production clean-up activities (removing underbrush, dead and damaged trees) were successfully completed. Since little progress in the agroforestry and fuel production activities had been made, we believe this contributed to weaknesses in the protection of existing resources because the danger of forest fires was not diminished by cutting out dead and damaged trees and removing underbrush which served to fuel brush fires. We noted several internal control weaknesses including the commingling of AID project funds; annual project plans were incomplete and late. Several compliance problems were also observed such as incomplete counterpart reports and noncompliance with special covenants.

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<sup>1/</sup> PIL 104, dated June 11, 1985, modified the project but did not formally revise or change the original outputs in the Project Agreement.

Our recommendations seek to correct both systemic and project-specific deficiencies encountered during the course of our review. We have recommended that USAID/Honduras:

- formally revise original project goals and objectives to reflect both the results of land-use studies and other economic and governmental activities in the region;
- suspend further project disbursements until special covenants are either revised or met;
- seek from the GOH improvements in its project administration and strengthen its own project monitoring;
- obtain from the GOH formal programming of the \$3.4 million in unprogrammed local funds;
- review the project's design to determine if forest fire protection activities to protect existing forest resources should be initiated to augment short and medium-term project strategy;
- reconcile and open a separate account for project funds advanced;
- assist the GOH to undertake required annual audits for the remaining life of the project; and
- obtain required counterpart reports from those project implementing agencies not submitting such reports and more closely monitor counterpart contributions.

## A. Findings and Recommendations

### 1. Overly Optimistic Goals

The original goals and outputs of the project agreement were overly optimistic and were not formally revised to reflect the results of completed land-use studies which included recommendations to improve the effectiveness of this project and other economic and governmental activities in the region. At the time of our audit, we estimated that less than one-third of the overall Project Agreement's goals had been met even though the original PACD had already expired and about 48 percent of authorized AID funds had been expended. In the policy and planning component, 27 percent of the original authorized project budget had been disbursed, but we estimated only a small portion of the planned goals had been accomplished. In the natural resources data collection and analysis component, 93 percent of the authorized budget had been disbursed while we estimated only about one-third of the goals had been accomplished. In the Choluteca watershed management component, 36 percent of the authorized budget had been disbursed, while we estimated about one-fourth of the goals had been met. The specific goals and outputs laid out in the 1980 Project Agreement were not subsequently amended in Project Implementation Letter Number 104, dated June 11, 1985, to reflect the results of the completed land-use studies in the Choluteca watershed and other competing economic and governmental activities. We were not able to determine why these specific goals and objectives had not been revised. Project personnel, including the project officer and contractors working on the project, expressed the view that similar projects in other countries had lower goals and that the project paper had probably been done with insufficient analysis. One contractor believed that the goals were built up in order to obtain a more favorable cost-benefit analysis and to get more rapid approval from AID/Washington.

#### Recommendation No. 1

We recommend that USAID/Honduras, in consultation with the Government of Honduras, formally revise the Project Agreement's goals and objectives to reflect both the results of completed land-use studies and other ongoing economic and governmental activities in the region and adequately quantify project goals and objectives so that progress can be measured.

#### Discussion

Little Progress in the Policy and Planning Component Achieved - At the time of the audit, \$219,360 of the planned \$815,700 originally authorized had been disbursed. One study in land tenure and one study in marketing had been completed which included recommendations to improve the effectiveness of the project. In contrast, the Project Agreement's goals contemplated that new natural resources management laws and regulations would be promulgated after analyzing existing laws and regulations. It was originally planned that studies of alternative land uses would lead to alternative solutions and their economic and social consequences would be calculated. Comprehensive and rational policies were to be developed for other priority areas such as the deteriorated Ulua and Chamelecon

watersheds. Also, land-use planning and actual land-use studies would be utilized to help develop and organize the capability of the GOH in natural resources management.

We believe that the principal reason many of these planning activities never materialized was that the Agricultural Policy Commission, the agency through which these planning activities would be accomplished, was abolished early in the project by Council for Economic Planning (CONSUPLANE) and no other organization was formally assigned this role by PIL or revised Project Agreement. We believe that not having completed these planning activities severely limits the impact of this project and prevents comprehensive natural resources management from being implemented in a systematic fashion (rather than the current piece-meal approach) as was set forth in the project design.

Limited Progress in the Natural Resources Data Collection and Analysis Component - At the time of the audit, \$3,101,520 of the \$3.3 million originally authorized USAID funds had been disbursed, and the following originally planned activities had been completed by the National Cadaster Agency and the Hydrologic Resources Office; 25 percent of the watershed soil surveys; about 10 percent of the upgrading of existing meteorological and hydrological stations; about 10 percent of the new construction efforts for meteorological and hydrological stations; about 25 percent of the ecology and forest classification activities; about 25 percent of the forest delineation activities; and 100 percent of the actual and potential land-use studies of five Choluteca river basin subwatersheds.

We believe that the Mission overestimated the capabilities of the National Cadaster Agency and the Hydrologic Resources Office to accomplish planned goals. These agencies had an inadequate understanding of the goals and objectives to be accomplished, an insufficient budget and staff to carry out these activities.

Limited Progress in the Choluteca Watershed Management Component - At the time of the audit, \$3,942,980 of the originally authorized \$10,859,900 USAID funds had been disbursed, and the following planned activities had been completed: 23 percent of the soil and water conservation works; two percent of agroforestry and fuel production activities; 26 percent of the planned reforestation efforts (about 40 percent of the reforested areas had not survived, leaving about 15 percent successfully reforested); 23 percent of the range management and pasture improvement activities; 61 percent of planned nurseries; seven percent of the planned 25 million seedlings had been produced and 27 percent of the revised \$1.79 million in credit for project-related loans and subsidies.

The Mission's project paper assessment of what could be accomplished by the Ministry of Natural Resources was overly optimistic. The lack of progress in this component was due to many factors. First, the project did not really get underway for about two years. Second, valuable time (three to four months each year) was lost due to the lengthy disbursement process and the process of annually renewing the majority of the project's administrative personnel contracts. Project personnel often

did not learn whether their contracts had been renewed until three or four months had passed. Third, other competing governmental and private sector activities which offered subsidies lured potential project participants away from various project activities. The poverty of project participants, in our opinion, prevented them from voluntarily cleaning up existing forests and maintaining already completed conservation works because of their need to work long hours to provide their daily necessities. We believe that these activity objectives likely could not be met in the Choluteca watershed without subsidies.

We concluded that the outputs for this component needed to be formally revised to more realistically reflect: the time lost in the first two years of the project, weak administrative processes in the Ministry of Natural Resources, recently completed potential and actual land-use studies in the Choluteca watershed; and the competing governmental, international, and private sector activities which lured away project participants because of the low level of project incentives.

#### Management Comments

While the Mission did not agree with all aspects of this finding, the Mission has, with the current project amendment number six, revised targets in the Project Description annex to the Project Agreement, as suggested by the auditors.

#### Inspector General Comments

As a result, recommendation number one is closed upon issuance of this report.

## 2. Special Covenants Not Complied With

Four of the six special covenants of the Natural Resources Management Project, in our opinion, were not adequately complied with and another was less than fully effective. The Project Agreement has six special covenants which include giving institutional permanence to the natural resources management policy, planning and execution function; establishing permanent institutional arrangements for current and future watershed management improvements; preparing annual detailed implementation plans and budgets; ensuring continuation of the watershed management credit fund; providing adequate budgetary support for activities as required and specified in the Project Agreement; and establishing an evaluation program. It is our opinion that USAID/Honduras officials did not effectively monitor compliance with the Project Agreement to ensure these special covenants were met. Further, no written Mission policy existed detailing what actions needed to be taken when noncompliance occurred. We concluded that ultimate success of the project was in doubt because: there were no formally designated, permanent institutional arrangements for current and future watershed management improvements; annual implementation plans were submitted incomplete and late; and host country counterpart contributions had lagged behind planned levels.

### Recommendation No.2

We recommend that USAID/Honduras:

- a. suspend further disbursements on this project until the GOH and USAID/Honduras determine how to obtain compliance with these special covenants;
- b. amend the project agreement, as necessary, if it is determined that certain covenants need to be revised or waived; and
- c. reimburse the Ministry of Natural Resources only that percentage of costs for which USAID/Honduras is responsible.

### Discussion

Four of the six special covenants had not been met by the GOH and one had been less than fully effective in its implementation.

Natural Resources Management Policy, Planning, and Execution Functions Lack National Institutional Permanence - Special Covenant number four in the Project Agreement required that, by the beginning of the fourth project year (July 30, 1983), natural resources management policy, planning and execution be accorded permanent national institutional status. Four months after the project started, the Agricultural Planning Commission, the entity that was intended to embody the institutional permanence for natural resources policy, planning and execution, was abolished. No other organization at the national level was subsequently designated to carry out this function. We believe that the permanent institutional presence sought by this project may not become a reality as

a result. Also, without overall planning of the natural resources base, Honduras may not achieve optimal economic advantages from its resources in the future. We concluded that USAID/Honduras, in consultation with the GOH, should formally review and revise this covenant in order to find alternative ways to devise a permanent national institutional mechanism through which the GOH could manage its natural resources (as opposed to the present temporary regional mechanism).

No Formally Designated Permanent Arrangements to Continue Watershed Improvements - Permanent arrangements between the Ministry of Natural Resources, the Forest Development Corporation (COHDEFOR), the National Cadaster Agency, and the Hydrologic Resources Office had not been made to continue and extend the work in the Choluteca watershed or extend it to other watersheds. Instead, the Ministry of Natural Resources only has a regional office in the Choluteca watershed which is primarily staffed with temporary employees. Project Covenant number five required that by July 30, 1984 these permanent working arrangements would be in place in order to continue work in the Choluteca watershed and to extend the work to other watersheds such as the Chamelecon and Ulua, after project completion. We believe a contributing factor to current noncompliance with covenant number five was a lack of knowledge of the AID Handbook and that USAID/Honduras had no formalized procedures (ie. Mission Orders) to be implemented when compliance with the terms of special covenants was not achieved. We believe the lack of written procedures is important because project officers cannot realistically be expected to know when and how to report and act on various problems in the absence of written instructions from Mission management. It seems unlikely to us that conservation work will be extended into other badly deteriorating watersheds after project completion unless permanent national arrangements (as envisioned in Special Covenant Number Five) to continue watershed improvements are made. The Project Paper implies that the productive potential of such watersheds as the Ulua and Chamelecon will be irretrievably lost in 22 years, and that Honduras will lose hundreds of millions of dollars of future economic activity as a result. We do not believe that the present temporary regional arrangement complies with the covenant. Consequently, we concluded that USAID/Honduras should review this covenant in conjunction with the GOH to find ways of accomplishing it or formally revise it.

Late and Incomplete Annual Implementation Plans - Annual implementation plans generally were not submitted to AID until well after the start of the calendar year and the plans we reviewed did not provide schedules for procuring such project inputs as technical assistance, training and commodities. Special Covenant number two requires that a detailed implementation plan including a schedule for such project inputs as technical assistance, training and commodities be submitted annually to USAID/Honduras by August 1. We found that late and incomplete plans had been accepted throughout the life of this project because the project officer had not insisted on their timely submission, and because the three GOH implementing agencies were on a calendar year cycle of operations. These implementation plans were prepared and submitted to AID roughly in accordance with the Honduran budget cycle. The result of this administrative practice was that each year three to four months of

valuable project implementation time was lost. We noted that these incomplete and late project implementation plans had often led to delays in implementing project activities, planning oversights, loss of project momentum, missed agricultural cycles, and the potential loss of the full value of technical assistance and training due to the untimely interplay and coordination between various project components. We concluded that USAID/Honduras, in consultation with the GOH, should strive to improve the GOH's administrative performance in this area by complying with this project covenant or by formally revising it.

Host Country Contributions Well Below Planned Amounts - At the time of our audit the GOH had made about 23 percent of its authorized contributions while USAID/Honduras had disbursed about 48 percent of AID's. Special covenant number six requires the Borrower/Grantee to provide adequate budgetary support for expanded activities as required and specified in the Project Agreement. Since project inception, through the issuance of Project Implementation Letter No. 104, dated June 11, 1985, USAID/Honduras' funding for this activity had increased substantially from \$5.7 million to \$9.7 million, while we noted that \$3.4 million of GOH's \$7.0 million authorized contribution remained unprogrammed (no detailed line-item budget existed). Additionally, as of March 31, 1986 (according to the USAID Controller's Local Currency Accounting Report), only \$2.9 million of the required \$7.0 million equivalent had been made available. This occurred despite the fact that host country contributions had been facilitated in recent years through ESF and PL 480 local currency generations, and the original PACD had expired. We concluded the shortfall in host country expenditures had occurred for three reasons: USAID/Honduras had no Mission Orders that specified what actions project officers and other responsible Mission personnel were to take when host country expenditure shortfalls occurred; the Project Agreement did not have a disbursement mechanism for ensuring adequate host country contributions (for example, the USAID/Honduras Controller's Office reimbursed host country project vouchers 100 percent instead of reimbursing only the percentage that USAID/Honduras was responsible for); and USAID/Honduras did not effectively address GOH noncompliance with the special covenant that required host country funding levels to be specified at quarterly or semi-annual project review meetings. We concluded that failure of the GOH to timely contribute its share of project financing had clearly affected project progress and implementation efforts. As a result of untimely GOH contributions, field offices were not able to purchase sufficient quantities of diesel fuel to visit project participants; to receive materials and supplies needed to accomplish project construction works, and to make timely salary payments to project employees. We concluded that USAID/Honduras should develop Mission procedures specifying what actions should be taken when expenditures by the host country fall short of agreed upon levels. We also concluded that the Controller should develop procedures to ensure timely disbursements by the GOH and sufficient local currency generations to completely fund GOH agreements. Current procedures in monitoring counterpart contributions had been less than fully effective.

Potential Shortfalls in Capitalizing the Watershed Management Credit Fund - At the time of the review, less than 18 months before the project's already extended completion date, the Watershed Management Credit Fund had received less than 42 percent of the revised funding level (\$1.79 million) calculated to be sufficient to finance activities at an appropriate level in the future. As of December 31, 1985, this fund had received \$750,000; it would have needed over \$1.79 million to meet this special covenant as revised by Implementation Letter No. 104. This financing obligation was in addition to the \$7.0 million counterpart requirement, of which the GOH had reported providing only 23 percent, after more than five and one-half years of project activity.

The fund was to have had sufficient capital to maintain conservation activities in this watershed for five years after the PACD. Technically, in light of the extended PACD, it would not be necessary to fully fund the Watershed Management Credit Fund at this time, but we have serious reservations that the fund will be fully capitalized in the future, based on past GOH compliance with its funding commitments.

#### Management Comments

While the Mission has some disagreement with aspects of this finding, they have made four changes to the project's special covenants. They noted that special covenant number four had been revised as part of current project amendment number six and that the GOH was in full compliance with the amended covenant.

They stated that special covenant number five had been deleted from the current project amendment because the wording and approach were too narrow, and because the Ministry of Natural Resources had taken effective leadership in this area and continued to make arrangements with other institutions as required.

They stated special covenant number two had been revised as part of the current project amendment by substituting the wording "January" for "August"; that PIL number 123 had been issued to clarify the reporting issue; and that technical assistance and training were now the subject of separate correspondence and their inclusion was not needed in annual workplans.

Regarding compliance with special covenant six, host country contributions, the Mission stated that by reducing GOH counterpart from \$6.9 million to \$5.6 million equivalent in amendment number six and by the inclusion of previously unreported counterpart contributions in 1983 and 1984, the host country was now in compliance.

The Mission stated that the credit fund had received all the financing it now needed and that \$1.79 million was not required of the GOH to capitalize this fiduciary agreement. AID loan funds of \$750,000 had been reserved through PIL's for the purpose of capitalizing this activity.

Inspector General Comments

We believe that the actions taken by the Mission satisfy the intent of the revised special covenants. This recommendation is also closed upon issuance of this report.

### 3. Administrative Weaknesses of Implementing Agency

Project personnel faced serious administrative obstacles and morale problems in carrying out their duties even though the project agreement required the GOH to provide adequate administrative support. In our opinion the project did not receive adequate administrative support in the areas of salaries, transportation, materials and supplies for field operations. In addition, no USAID site visit reports had been written identifying these administrative problems. The nonreporting of these administrative problems resulted in a less than optimal level of performance by the field offices because no corrective actions were undertaken.

#### Recommendation No. 3

We recommend USAID/Honduras:

- a. identify and resolve the various administrative and implementation problems affecting this project in consultation with the Government of Honduras in order to improve the project's performance;
- b. improve its project monitoring by issuing a Mission Order which specifically addresses actions to be taken by the Project Officer in monitoring Mission projects; and
- c. ensure that project officers prepare site visit reports upon completion of field trips as required by the AID Handbook and Mission Orders.

#### Discussion

The project agreement required the GOH to provide adequate administrative support. The following conditions indicate an adequate level of support was not being provided.

The majority of project personnel were hired on one-year contracts and experienced delays of up to five months in receiving their initial salary payments. In succeeding years, delays of up to three months occurred before initial salary checks were received. In addition, recently hired personnel received higher salaries than more experienced personnel who had been working with the project for more than two years because there was no uniform salary policy that would have established appropriate rates of pay for new and experienced employees. Also, the salaries awarded in the older contracts had been frozen at the original rates.

Field units with four to seven employees were assigned only one vehicle and in the southern region there were no maintenance programs for vehicles. Also, small expenditures for vehicle repairs and other office expenses were often not adequately reimbursed. This had limited the number of site visits which had, in turn, hindered project progress.

Employee performance in the field was also hampered by the lack and timely receipt of tools and supplies for undertaking conservation works such as crowbars, shovels and hoes which we were told were often received late. Usually, these items were requested from the Central Office in December of each year, in order to initiate the coming year's activities with project participants. However, we were told that the field offices often received these materials up to four months after the date needed. This condition slowed the implementation of activities programmed for that period and lowered performance of field office personnel.

In addition to these shortcomings, USAID project monitoring needed improvement. No site visit reports had been prepared or filed by the current USAID project officer or his predecessors during the six years of the project. The current project officer stated he was unaware of this requirement and his mission superiors had never requested such reports. Site visit reports are required by AID Handbook 3, Supplement A, Appendix E, Page 1.

#### Management Comments

Regarding recommendation 3.a, the Mission stated meetings were held in May 1986, with representatives of the Ministries of Natural Resources and Finance and Public Credit, with the purposes of resolving contracting and payment delays which they considered important problems. The Mission believed these meetings were useful and productive, and that they had already seen positive and concrete results in terms of approved salary raises for "veteran" employees of the project, contract renewals, salary payments and an end to the political appointment problem within the project, and a joint request by the Ministry of Natural Resources and AID to convene the Executive Committee for this project on a regular basis to deal with administrative issues as they arise. The Mission stated that the delivery of a new fleet of vehicles was completed in May, and the lack of field vehicles was no longer a problem.

Regarding recommendation 3.b, the Mission promised review at the management level.

Regarding recommendation 3.c, the project officer stated that site visit reports were now being prepared.

#### Inspector General Comments

Recommendation 3.a is closed upon the issuance of this report.

After receiving a satisfactory Mission Order or other Mission written directive, recommendation 3.b will be considered for closure.

Recommendation 3.c is also closed because of a recent USAID policy directive requiring site visit reports.

#### 4. Counterpart Funding Shortfalls

Five years into the project, the Government of Honduras reported spending only \$1.6 million (23 percent) of \$7.0 million committed to in the Project Agreement while USAID/Honduras spent \$7.3 million of \$15.0 million (48 percent) authorized for the project. Of the \$5.3 million not expended by GOH, \$3.4 was not programmed by line item. Also, from September 29, 1982 through March 31, 1986 only \$2.9 million equivalent had been programmed and made available from ESF and PL 480 generations for this project (\$7.0 million are needed). USAID/Honduras had not accounted for the difference in funds provided by the local currency generations for the project and funds expended by the GOH for the project. USAID/Honduras had no Mission Orders to instruct project officers on what actions needed to be taken when host country counterpart expenditures fell below AID's level of expenditures. We concluded that the lack of counterpart expenditures had contributed to delayed project implementation, as mentioned in finding number three, and that total counterpart funds expected to be made available through PL 480 and ESF local currency generations had fallen 59 percent short of requirements.

#### Recommendation No. 4

We recommend USAID/Honduras:

- a. obtain from the Government of Honduras formal programming of the \$3.4 million in unprogrammed local funds which represent nearly 50 percent of their project commitments;
- b. designate sufficient local currency generations for this project to ensure that the GOH will meet its agreed upon requirements; and
- c. reconcile the difference between the \$1.6 million equivalent expended by the GOH and the \$3.0 million equivalent in local currency generations for the project, and determine if expenditures were project related.

#### Discussion

Reported GOH counterpart expenditures amounted to \$1.6 million equivalent as of December 31, 1985, which was 23 percent of the amount agreed to in the Project Agreement. However, USAID/Honduras local currency generations from PL 480 and ESF programs for this project were \$3.0 million equivalent from September 29, 1982 to March 31, 1986. As of that date, AID had disbursed \$7.3 million, or 48 percent of its \$15.0 million authorized contribution. According to the GOH Implementing Unit Administrator, GOH disbursements had been slower than USAID disbursements: "emphasis was placed on expending AID loan funds rather than GOH resources because the nonuse of loan funds was considered to be an indicator of project failure." At the time of the audit, with a remaining project life of less than 18 months, and less than fully effective USAID/Honduras monitoring of counterpart expenditures, we believe it is questionable whether the GOH will be able to meet

expenditure levels as agreed to in the Project Agreement, notwithstanding the availability of PL 480 and ESF Mission generated local currency programs.

On June 11, 1985 the Project Agreement was revised and the GOH counterpart contribution reallocated; however, this revision showed an unprogrammed amount which totaled \$3.4 million equivalent for 1985, 1986, and 1987. This document was reviewed and approved by USAID/Honduras. Quarterly project progress reports made no reference to shortfalls in required counterpart expenditures which, at the time of these reports, were well below agreed upon levels and AID's proportional level of contributions to the project. In addition, there were no Mission Orders addressing monitoring of host counterpart expenditures.

We noted that even with the local currency generations designated for this project, the expenditure shortfall was about \$4.0 million equivalent as of March 31, 1986. We therefore concluded that USAID/Honduras needed to pay more attention to the monitoring of counterpart expenditures to ensure that they were at levels proportionate to AID disbursements. Also, we believe more local currency generations needed to be allocated to this project's counterpart funds in order to ensure that the GOH'S funding requirements would be met.

#### Management Comments

The Mission indicated in its response to this finding that on June 6, 1986, amendment number six to the Project Loan and Grant Agreement had been issued. A revised Project Description, Annex I, was also included.

GOH counterpart was formally reduced from \$6.967 million equivalent to \$5.6 million equivalent. Also, \$3.4 million in unprogrammed local funds were programmed through 1989 in Annex I, Attachment B.

The Mission also provided an analysis of GOH counterpart funds spent to date by the Ministry of Natural Resources and the National Cadaster Agency which accounted for the \$1.3 million difference between funds provided versus funds reported on. Finally, they indicated that additional local currency resources were being programmed for this project.

#### Inspector General Comments

We believe that the actions taken by the Mission adequately address the three-part recommendation and, therefore, recommendation four is closed upon issuance of this report.

## 5. Inadequate Protection of Existing Resources

In our opinion, the impact of the natural resources management project is minimized by inadequate protection of existing forest resources. Reported forest fires in the Choluteca Watershed had not decreased during the life of the project. As a result, fires continued to destroy vast amounts of forests in the Choluteca watershed. The Project Paper anticipated that the number of forest fires and hectares destroyed through carelessness and poor agricultural practices would gradually decrease through the introduction of such forestry management programs as agroforestry, fuel production, reforestation, education of the campesinos and the resultant changes in attitudes toward the forest, etc. We believe that the reported forest fires had not decreased because there had been insufficient training and organization of the campesinos to fight fires, a lack of firefighting equipment and tools, and the limited impact of the project's forestry management component (only a small fraction of the project goals to cut out dead and damaged trees and to remove underbrush which served as fuel for brush fires had been accomplished). As a result, and using conservative estimates of loss, at least twice as many trees were being lost to fires each year in the project area as the project had been able to regenerate.

### Recommendation No. 5

We recommend that, if it is decided to continue or expand this project, USAID/Honduras, in consultation with the Government of Honduras, review the project's design to ascertain if the project's short and medium-term strategies could be improved by a fire fighting component to include:

- a. campesino training programs in fire fighting;
- b. increasing training programs and subsidized demonstration activities for proper care of existing forests; and
- c. determining the appropriate amount and type of forest fighting tools to be distributed throughout the Choluteca watershed (ie. rakes, portable sprayers etc.).

### Discussion

Reported forest fires in the Choluteca Watershed had not decreased during the life of this project as shown by the number of forest fires reported by COMDEFOR from 1975 through 1985:

<u>Year</u>	<u>Reported Fires</u>	<u>Hectares of Forest Destroyed</u>
<u>Fires Before the Project</u>		
1975	246	6,562
1976	168	1,783
1977	348	7,646
1978	430	5,566
1979	443	4,108
<u>Fires After the Project</u>		
1980	527	18,846
1981	485	4,795
1982	656	13,423
1983	590	13,090
1984	528	14,817
1985	516	8,743

As can be seen from the chart, the number of reported fires and hectares of forest destroyed was lower before the project's inception in 1980. However, COHDEFOR officials responsible for collecting forest fire data stated that current data was more complete and that in the earlier years many fires may have gone and probably did go unreported. Nevertheless, these figures indicate that forest fires in the Choluteca watershed were a continuing problem which needed to be adequately dealt with if the project's goals of improved watershed management were going to take place.

The Forest Protection Department of COHDEFOR told us that the forests in the Choluteca watershed were classified as follows: adult forest, as few as 80 trees per hectare; young forest, up to 2,500 trees per hectare; and regeneration, 2,500 to 3,000 trees per hectare. They stated that fire damage was much more intensive in the latter category because small trees do not have any resistance to forest fires. He stated that a young forest receives significantly more damage than adult forests which usually survive brush fires (with the exception of adult pine trees tapped for turpentine).

Since project inception in 1980, an average of 12,285 hectares of forest had been lost each year. If one assumes 80 trees are lost per hectare in a fire (the lowest and most conservative estimate), about one million trees a year would be lost to fire in the Choluteca watershed. This means that at least twice as many trees are lost as the number of trees planted each year by the project during its five-year life. Additionally, about 40 percent of the project's newly planted trees had not survived after three years.

The Project Paper predicted a gradual decrease in forests lost to fire because of the widespread adoption of forestry management programs, a change in the attitudes of campesinos in the forested areas of the watershed, etc. We believe this prediction was unrealistic. Reported forest fires had not decreased, in our opinion, because the forestry management program had not progressed at all, accomplishing only a small fraction of its intended goals. We believe this program had not been well received by project participants because of the limited economic benefits received from participation, the time and effort needed to undertake a clean-up of forests, and the general poverty of the potential participants who must seek out other forms of work which offer more income. The project had envisioned that the economic benefits of selling firewood from diseased, dying, and damaged trees would be enough for the participants to undertake a clean-up of the forests in the watershed. However, numerous project participants told us they could not afford to participate in this activity because the price of firewood was too low in relation to the time required to gather and sell it. The project officer and GOH were not inclined to offer incentives for these activities because they believed the participants would become dependent on such subsidies. We were also told by project participants that they lacked forest fire training, organization, and equipment to adequately fight forest fires. They noted that COHDEFOR employees rarely arrived in time to prevent damage from forest fires in their areas.

Since project inception, statistics indicate approximately 74,000 hectares of forest have been lost to fire in the Choluteca watershed. This we consider to be unacceptably high.

#### Management Comments

USAID project officials held that the project had accomplished a great deal more in the area of forest protection than our field visits indicated and that the efforts to bring COHDEFOR resources to bear on the forest protection issue continue and were bearing fruit. AID and COHDEFOR are currently developing a major bilateral forestry project to help COHDEFOR fulfill its legal mandate in fire protection.

Project officials have now renewed contacts with COHDEFOR, encouraging that institution to live up to its responsibilities in fire protection and control, and COHDEFOR has responded with short courses and food-for-work for farmer groups participating in the project.

#### Inspector General Comments

The auditors recognize that there is more than one solution to any problem. Accordingly, when the Mission furnishes the IG Office with a copy of an executed agreement between AID and COHDEFOR, we will consider closing the recommendation.

## 6. Commingling of USAID Project Funds

GOH officials did not maintain a separate bank account for the project's advances of funds as required by USAID regulations. There had not been formal communications to GOH officials indicating that a separate account should be maintained for advances under this project. As a result, funds advanced for project implementation were commingled with other AID funds and project officials did not readily know which funds were available for the different project activities.

### Recommendation No.6

We recommend that USAID/Honduras, in consultation with the Government of Honduras, reconcile and subsequently establish a separate account for funds advanced under this project and close out outstanding advances for other projects no longer active.

### Discussion

As of January 31, 1986 the local currency equivalent of \$1,255,207 was on deposit in project account #2500086 at the Central Bank of Honduras. Outstanding project advances amounted to \$288,292. According to GOH officials, the large difference in these amounts was due to advances from three other USAID projects which were deposited into this same account. The Ministry of Finance and USAID/Honduras had not reconciled the advance account to the various projects. This came about because USAID/Honduras had not required bank statements when project advances were issued. Furthermore, some of these advances had been outstanding for sometime, as two of these projects had been inactive for several years.

Of the \$288,292 in project advances outstanding on January 24, 1986, only \$36,374 had been liquidated as of April 3, 1986, the remainder had been outstanding more than 90 days.

<u>Length of Time Outstanding</u>	<u>Amount Outstanding</u> <u>As of April 3, 1986</u>
More than two years	\$ 3,296.10
One year to two years	40,462.70
Six months to one year	10.50
60 days to six months	<u>208,148.28</u>
Total	\$251,917.58 =====

Other AID project funds commingled in this account were from: Loan 522-T-029, Food and Nutrition Plan, whose activities were completed in 1981; Grant 522-0139, Agricultural Research, which was completed in 1984; and Grant 522-0153, Health Sector I, whose project completion date is 1987. Even though two of these projects had been inactive for more than six months, we were told that no efforts had been made to reconcile advance balances for these closed projects and to return unused amounts to USAID/Honduras. Without an account reconciliation and a subsequent close-out of these completed projects, a determination cannot be made as to available project funds and the amount of outstanding advances. We therefore concluded that an account reconciliation needed to be done and that those advances remaining from aforementioned completed projects be returned to USAID.

#### Management Comments

On June 6, 1986, USAID/Honduras formally requested the Directorate of Public Credit to make a complete analysis of the bank account referred to in the draft report. The Mission's letter was accompanied by a copy of our report finding, "commingling of USAID project funds." The analysis should be completed before the close of June 1986.

#### Inspector General Comments

Upon receipt of the analysis of this account, closure of the old project accounts, and establishment of separate accounts for the active projects, we will consider closing this recommendation.

## 7. Required Financial Audits Not Performed

Required annual financial audits were not being performed. After nearly six years of project activities and with less than 1-1/2 years of project life remaining, only one financial audit of project expenditures had been conducted. Project Implementation Letter Number 27, dated February 19, 1982 required the borrower/grantee to conduct annual financial audits. USAID/Honduras officials stated that they did not remember this requirement and consequently did not monitor this audit provision for compliance. Since the USAID project officer did not recall this requirement, he was unaware that GOH project officials had decided to waive this requirement because of the expense involved and the lengthy process required to contract out those services to an external firm. As of December 31, 1985, about 48 percent of authorized USAID grant and loan monies had been disbursed, in our opinion, without adequate assurance that project funds had been properly expended and accounted for.

### Recommendation No. 7

We recommend that USAID/Honduras, in consultation with the GOH ensure that required annual audits are performed and that the ensuing reports are forwarded to AID.

### Discussion

Only one financial audit, by the Controller General of Honduras in 1982, had been conducted on project expenditures. Part C, Annex II to the Project Agreement, d. Section B.5, Reports, Records, Inspections, and Audit, page 29, states

"The Borrower/Grantee should also conduct annual financial audits. The financial audits should examine books and records pertaining to the financial support received under this Project. The audits are to ensure that proper accounting practices are being employed, that proper bookkeeping procedures are being observed, and that expenditures of project monies are properly made. AID funds will be available for financial and end-use audits to be conducted at the end of each Government of Honduras Accounting Year and upon completion of project activities. Such audits will be conducted of each participating entity by an independent auditing agency. AID reserves the right, however, to accept the financial audit findings of, or presented by the Government of Honduras in satisfaction of AID's audit requirements or to request additional financial audits at any time. As required, project funds may be utilized for contracting such additional audits".

The project officer stated that he did not recall the provisions of PIL number 27 requiring annual GOH audits and thus they were not carried out. According to GOH project officials, they were aware of this requirement but had decided to unilaterally waive it because they believed the contracting process involved would require substantial time

and effort. One audit by the Controller General of Honduras had been performed in 1983 but the majority of project funds were disbursed afterwards. External audits were needed to establish that project funds were being properly expended. In addition, USAID/Honduras was not sufficiently monitoring project implementation nor complying with established USAID procedures. We therefore believe that USAID/Honduras should request the GOH to obtain these audit services as specified in PIL 27: "Controller's Office will consult with the participating entities to further discuss AID requirements for accounting and audits".

#### Mission Comments

On June 12, 1986 Ministry officials informally advised USAID/Honduras that an internal audit was initiated on June 10, 1986 by the Ministry's Internal Audit Section because the GOH Controller General did not have the staff to do the work. The examination should be completed in the near future.

#### Inspector General Comments

Upon receipt of the completed audit report, we will consider closing this recommendation.

## 8. Counterpart Funding Reports Incomplete

There were no counterpart expenditure reports for program activities under Component No. I (Policy and Planning) and Component II (Data and Analysis). These components were to be implemented by the Agricultural Policy Commission, Hydrologic Resources Office and the National Cadaster Agency respectively. Even though this information was required by the Project Agreement, the lack of adequate communication with implementing units resulted in no counterpart funding reports being submitted by these agencies (as distinguished from AID funds reports submitted by GOH). Additionally, the Agricultural Policy Commission was abolished at the beginning of the project. As a result, project activities under Component No. I had been de-emphasized and no laws or regulations regarding natural resources protection had been issued. Under Component No. II, we believe the lack of GOH contributions had contributed to the reduction of the area of the country to be classified by the National Cadaster agency. (Instead of being national in scope, as specified in the Project Agreement, the project area was reduced to the Choluteca watershed. The project officer told us there were plans to extend the project into two more areas outside this watershed.)

### Recommendation No.8

We recommend that USAID/Honduras ensure that the Government of Honduras prepare counterpart funding reports for nonreporting project implementing agencies; these reports should be prepared from the time the activities were started until their completion; the instructions should indicate what, when, and how often these reports are to be prepared and forwarded to AID.

### Discussion

USAID/Honduras' expenditures as of December 31, 1985 amounted to \$219,360 for Component No. I and \$2,817,896 for Component No. II. For Components I and II there were no counterpart funding reports from GOH implementing units. According to National Cadaster Officials, counterpart funding reports had never been required of them and USAID had not informed them officially (by PIL) that a separate accounting of their expenditures was required for their counterpart contributions.

Although the implementing unit for component No. I, the Agricultural Policy Commission, was abolished in 1980 and the Natural Resources Management Unit did not take over this activity until July 1985, USAID/Honduras had incurred expenditures under this component totaling \$219,360 as of December 31, 1985. During the same period, there were no counterpart funds expenditure reports. Although more than \$200,000 was spent, no natural resources management laws or regulations had been issued.

Under Component No. II, (Data Analysis) which was implemented by the National Cadaster Unit, USAID/Honduras had expenditures as of December 31, 1985 totaling \$2,817,896. However, there were no reports from GOH

implementing units showing any matching host country counterpart fund expenditures for that period. According to National Cadaster officials, counterpart reports had never been required and USAID had not informed them officially (by PIL) that a separate accounting for such funds was required. Consequently, ESF and PL 480 local currency generations that had been provided to the National Cadaster agency under the Natural Resources Management Program for 1982, 1983 and 1984 were not reported. We were told that the local currency generations were used to cover National Cadaster's general budget and support expenses and had not been used for this project only. We believe the use of these funds should have been restricted since they were earmarked for the Natural Resources Management project. Records kept by the National Cadaster agency did not reflect counterpart expenditures for its various programs; this probably resulted in the lack of reporting on counterpart expenditures for the project.

Due to the lack of reports on GOH counterpart expenditures in components I and II, USAID/Honduras had not been able to determine the extent of GOH funding levels for ongoing activities or the total amount of GOH counterpart fund contributions to date for the project.

Counterpart expenditure reports were prepared by the Natural Resources Management Unit. However, these reports dealt only with Component No. III, and therefore did not present a complete picture of GOH counterpart expenditures.

We therefore concluded that USAID/Honduras, in cooperation with the Government of Honduras, needed to determine past expenditures for project Components I and II.

#### Mission Comments

The Mission is issuing a PIL classifying reporting requirements, as suggested by the audit report.

#### Inspector General Comments

Draft project implementation letter number 123 appears to adequately address the thrust of recommendation number eight. Upon receipt of a copy of the final PIL, we will close this recommendation.

## B. Compliance and Internal Controls

### Compliance

The audit disclosed six compliance exceptions:

- USAID funds were disbursed despite the fact that four of the six special covenants had not been met (Finding 2).
- Project officers were not filing site visit reports (Finding 3).
- The GOH was not furnishing the agreed upon level of support to the project (Finding 4).
- Project funds were commingled with other USAID project funds (Finding 6).
- Annual project financial audits were not performed by the GOH (Finding 7).
- Host country financial and activity progress reports were inadequate (Finding 8).

Other than the conditions cited, tested items were in compliance with applicable laws and regulations and nothing else came to our attention that would indicate that untested items were not in compliance with applicable laws and regulations.

### Internal controls

We noted six internal control exceptions:

- Annual project plans for subcomponent implementation were incomplete and late (Finding 2).
- There was no Mission Order on actions to be taken by Project Officers and others when special covenants were not being met (Finding 2).
- There was no Mission Order differentiating the use of Project Implementation Letters versus loan or grant amendments to project agreements (Finding 2).
- Controls over project funds disbursed were inadequate because the Mission did not have a system to ensure that the host country was contributing proportionately to the project as required (Finding 4).
- Project Implementation Letter Number 104 did not include programming of almost 50 percent of GOH project budget resources; as a result, \$3.4 million equivalent in counterpart funds remained unprogrammed at a time when the project was almost six years old (Finding 4).

-- Controls over Mission project advances needed improvement because the project account contained advances still outstanding which pertained to two projects that had been inactive since 1981 and 1984 (Finding 6).

AUDIT  
OF USAID/HONDURAS'  
NATURAL RESOURCES MANAGEMENT  
PROJECT NO. 522-0168

PART III - EXHIBITS AND APPENDICES

Natural Resources Management  
 Status of USAID Funding  
 As of December 31, 1995  
 in US\$ (000)

Project Component	AID GRANT			AID LOAN			Counterpart Funds	
	Authorized	Obligated	Disbursed	Authorized	Obligated	Disbursed	Authorized	Disbursed
I. Policy and Planning	\$689.0	\$175.1	\$175.0	\$126.7	\$69.6	\$44.4	\$262.5	N/A *
II. Data Collection and Analysis	\$627.0	\$303.8	\$303.8	\$2,692.1	\$3,450.0	\$2,797.8	\$2,324.1	N/A *
Natural Resources Data Processing	55.1	N/A *	N/A *	354.1	N/A	N/A	229.1	N/A
Soil Surveys and Laboratory	139.8	N/A	N/A	217.7	N/A	N/A	562.7	N/A
Hydrology and Climatology	204.0	N/A	N/A	355.9	N/A	N/A	423.1	N/A
Ecology and Forest Classification	32.0	N/A	N/A	46.4	N/A	N/A	198.1	N/A
Forest Delineation	0.0	N/A	N/A	41.1	N/A	N/A	297.9	N/A
Actual/Potential Land Use	36.0	N/A	N/A	54.9	N/A	N/A	423.6	N/A
General Project Support	160.0	N/A	N/A	1620.0	N/A	N/A	189.6	N/A
III. Choluteca Watershed Management	\$1,420.0	\$2,221.1	\$1,795.7	\$9,439.9	\$3,480.4	\$2,147.3	\$4,380.1	\$1,607.5
Soil/Water Conservation	315.4	N/A	N/A	1703.8	N/A	N/A	814.4	N/A
Agroforestry and Fuel Production	500.4	N/A	N/A	3206.6	N/A	N/A	1495.3	N/A
Reforestation Activities	253.3	N/A	N/A	1623.8	N/A	N/A	757.1	N/A
Range Mgmt and Pasture Improvement	216.4	N/A	N/A	1703.0	N/A	N/A	774.1	N/A
Community Nurseries	134.6	N/A	N/A	1202.6	N/A	N/A	539.2	N/A
Credit Fund 1/								
<b>Total</b>	<b>\$2,736.0</b>	<b>\$2,700.0</b>	<b>\$2,274.5</b>	<b>\$12,258.7</b>	<b>\$7,000.0</b>	<b>\$4,999.5</b>	<b>\$6,966.7</b>	<b>\$1,607.5</b>

\* Accounting data not Available

1/ Loans/Subsidies to be granted are included in each sub-component.

EXHIBIT 1

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Natural Resources Management  
Analysis of Project Accomplishments  
As of December 31, 1985  
(in US\$'000)

Project Component	Amount Authorized	Amount Disbursed	Percent of Authorization Disbursed	Accomplishments	Project Goals	% Estimate of Percent of Goals Achieved
<b>I Policy and Planning</b> (5% of planned resources)	\$ 815.7 (AID) 1/ 262.5 (GDM) 2/ 1,078.2 (Total)	\$ 219.4 (AID)	27%			
- Analysis of Laws and Regulations					New Laws and Regulations	
- Alternative Solutions and their Economic/Social Consequences				1 Study - Land Tenure	Studies of Alternatives	
- Comprehensive and Rational Policies				1 Study - Marketing	New Policies in Priority Areas	20%
- Land Use Planning					Develop and Organize Capability	
- Actual Land Use					Land Use for Major Valleys	
Revised in 1984 to Focus on Project Geographical Area Only.						
<b>II Natural Resources Data Collection and Analysis</b> (25% of planned resources)	\$ 3,319.0 (AID) 3/ 2,324.1 (GDM) 4/ 5,643.1 (Total)	\$ 1,101.6 (AID)	33%			
- Soil Surveys				5 Subwatersheds in the Cholulaca River Basin	Coxayaqua, Olancha and Yoro by 1982. Remainder of the Country by 1985.	25%
- Hydrology				Study for New Installations 17 Old Upgraded 12 New Constructed	Improving 102 Meteorological Stations and 49 Hydrological Stations. Constructing 65 Meteorological and 38 Hydrological Stations	10%
- Ecology and Forest Classification				5 Subwatersheds in the Cholulaca River Basin	Olancha, Colon and Gracias a Dios by 1982. Country Wide by 1985.	25%
- Forest Delineation				5 Subwatersheds in the Cholulaca River Basin	Priority Coxayaqua, Olancha and Yoro by 1982. Country Wide.	25%
- Actual/Potential Land Use				5 Subwatersheds in the Cholulaca River Basin	Priority Area	100%
<b>III Cholulaca Watershed Management</b> (70% of planned resources)	\$10,859.9 (AID) 4,380.1 (GDM) 15,240.0 (Total)	\$7,943.0 (AID) 1,607.5 (GDM) 9,550.5 (Total)	36%			
- Soil/Water Conservation						
Farmers				not available 5/ 4,073.18	5,500 18,000	23%
Hectares						
- Agroforestry & Fuel Production						
Farmers				not available 5/ 174.11	2,700 8,260	2%
Hectares						
- Reforestation				1,107.10	4,233	26%
Hectares						
- Range Management & Pasture Improvement						
Farmers				not available 5/ 1,139.62	300 5,000	23%
Hectares						
- Community Nurseries						
Community Groups				209	264	79%
Hectares Treated				6/	12,593	6/
Seedlings by 1985				1.9 M	25.5 M	7%
- Credit Fund						
Loans/Subsidies by 1985				6489.3	61,700	27%
	\$14,994.6 (AID) 6,966.7 (GDM) 21,961.3 (Total)	\$7,264.0 (AID) 1,607.5 (GDM) 8,871.5 (Total)	48%		100%	27% 1/

1/ The overall percentage of completion was calculated by weight averaging the percentage of completion for each component based on the planned percentages of dollar authorization for that component.

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NATURAL RESOURCES MANAGEMENT  
PROJECT STATUS SUMMARY  
FOOTNOTES

- 1/ On June 11, 1985, this component was de-emphasized; funds were reprogrammed. New budget for policy and planning is \$244,700 of which 90 percent had been disbursed.
- 2/ There are no GOH reports on counterpart expenditures for this component.
- 3/ Amount authorized for this component was increased to \$3,753,800, an increase of \$434,800.
- 4/ There are no GOH reports on counterpart expenditures for this component, even though \$1,260,700 in ESF local currency generations had been allocated to the National Cadaster office (implementing unit).
- 5/ Reports prepared by the GOH showed a total of 1,304 individuals that had benefited from the project, but there was no breakdown by activity. Also, data was available for numbers of beneficiaries only through June 30, 1985.
- 6/ Activities under this subcomponent were included in the reforestation subcomponent.

LIST OF REPORT RECOMMENDATIONS

Recommendation No. 1

We recommend that USAID/Honduras, in consultation with the Government of Honduras, formally revise the Project Agreement's goals and objectives to reflect both the results of completed land-use studies and other ongoing economic and governmental activities in the region and adequately quantify project goals and objectives so that progress can be measured.

Recommendation No.2

We recommend that USAID/Honduras:

- a. suspend further disbursements on this project until the GOH and USAID/Honduras determine how to obtain compliance with these special covenants;
- b. amend the project agreement, as necessary, if it is determined that certain covenants need to be revised or waived; and
- c. reimburse the Ministry of Natural Resources only that percentage of costs for which USAID/Honduras is responsible.

Recommendation No.3

We recommend USAID/Honduras:

- a. identify and resolve the various administrative and implementation problems affecting this project in consultation with the Government of Honduras in order to improve the project's performance;
- b. improve its project monitoring by issuing a Mission Order which specifically addresses actions to be taken by the Project Officer in monitoring Mission projects; and
- c. ensure that project officers prepare site visit reports upon completion of field trips as required by the AID Handbook and Mission Orders.

Recommendation No.4

We recommend USAID/Honduras:

- a. obtain from the Government of Honduras formal programming of the \$3.4 million in unprogrammed local funds which represent nearly 50 percent of their project commitments;

1,1

- b. designate sufficient local currency generations for this project to ensure that the GOH will meet its agreed upon requirements; and
- c. reconcile the difference between the \$1.6 million equivalent expended by the GOH and the \$3.0 million equivalent in local currency generations for the project, and determine if expenditures were project related.

Recommendation No. 5

We recommend that, if it is decided to continue or expand this project, USAID/Honduras, in consultation with the Government of Honduras, review the project's design to ascertain if the project's short and medium-term strategies could be improved by a fire fighting component to include:

- a. campesino training programs in fire fighting;
- b. increasing training programs and subsidized demonstration activities for proper care of existing forests; and
- c. determining the appropriate amount and type of forest fighting tools to be distributed throughout the Choluteca watershed (ie. rakes, portable sprayers etc.).

Recommendation No.6

We recommend that USAID/Honduras, in consultation with the Government of Honduras, reconcile and subsequently establish a separate account for funds advanced under this project and close out outstanding advances for other projects no longer active.

Recommendation No. 7

We recommend that USAID/Honduras, in consultation with the GOH ensure that required annual audits are performed and that the ensuing reports are forwarded to AID.

Recommendation No.8

We recommend that USAID/Honduras ensure that the Government of Honduras prepare counterpart funding reports for nonreporting project implementing agencies; these reports should be prepared from the time the activities were started until their completion; the instructions should indicate what, when, and how often these reports are to be prepared and forwarded to AID.

REPORT DISTRIBUTION

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