

PD-AMU-851

IAN = 4831 2

AUDIT OF USAID/PERU'S
DISASTER RELIEF, REHABILITATION
AND RECONSTRUCTION PROJECT (NO. 527-0277)

Audit Report No. 1-527-87-11
January 29, 1987

AGENCY FOR INTERNATIONAL DEVELOPMENT

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

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA — HONDURAS

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

January 29, 1987

MEMORANDUM

FOR: USAID/Peru Director, Donor Lion
FROM: RIG/A/T, *Coinage N. Gothard*
SUBJECT: Audit of USAID/Peru's Disaster Relief, Rehabilitation, and Reconstruction Project

This report presents the results of audit of USAID/Peru's Disaster Relief, Rehabilitation, and Reconstruction Project. The objectives of this program results audit were to evaluate the project's effectiveness in achieving planned results, and to assess compliance with AID requirements.

The project had achieved its purpose of making a disaster assistance coordinating unit and a reconstruction fund operational. USAID/Peru's system for measuring project effectiveness was generally satisfactory, although its reports on the progress of AID-funded subprojects contained some inaccuracies. For example, the reports were supposed to show the subprojects' overall progress for all three years of the project. According to the project monitoring coordinator, however, as late as August 22, 1986 the percentage completion shown for each subproject could actually represent progress against 1986 goals only, or the status of the project at the end of 1984. Other inaccuracies were also noted. Compliance with AID requirements was generally adequate.

The findings in this report describe the need to complete flood protection work in Tembladera, and delays in receiving emergency medicines. Four other pertinent matters are also discussed. The recommendations are that flood protection work in Tembladera be completed, and that lessons learned from a delayed medical procurement be documented.

USAID/Peru agreed with the report findings and recommendations, but disagreed with our presentation of some of the matters discussed in the "other pertinent matters" section of the report.

Please advise this office within thirty days of the actions planned or taken to implement the two report recommendations.

EXECUTIVE SUMMARY

According to USAID/Peru, the El Nino disaster caused \$1 billion in damage in 1982 and 1983. AID responded to the disaster with emergency relief, immediate rehabilitation, and long-term rehabilitation and reconstruction assistance. The Disaster Relief, Rehabilitation, and Reconstruction project was the largest component of AID's longer-term response. The project began on July 20, 1983 and was scheduled to end on March 31, 1987. The project budget was \$87 million, including \$65 million in AID funds and \$22 million in counterpart contributions. Most of these funds were set aside for subprojects proposed by the Government of Peru at the beginning of each year. At the time of our audit, USAID/Peru had approved 113 subprojects which were further divided into well over 1,000 individual works or locations.

The Office of the Regional Inspector General for Audit/Tegucigalpa conducted a program results audit to calculate the project's effectiveness in achieving its planned results, and to assess compliance with AID requirements. The audit showed that the project was highly effective in responding to the effects of the El Nino disaster, although the Mission was still trying to eliminate inaccuracies in the reporting system it used to monitor the project's effectiveness. Compliance with AID requirements was generally adequate.

USAID/Peru had done a good job of managing an \$87 million project implemented in fifteen departments of Peru. The project had provided thousands of employment opportunities, and had provided massive assistance for rebuilding infrastructure and reactivating agricultural production.

The findings in this report describe the need to complete flood protection work in Tembladera, and delays in receiving emergency medicines. Four other pertinent matters, concerning the appropriateness of some project activities, subproject approvals, separation of duties, and updating the Mission disaster plan are also discussed.

The Departmental Development Corporation in Cajamarca spent about \$277,000 in Tembladera to protect the town from destructive flash floods and to rebuild two bridges which were destroyed in 1983. Additional works were planned to direct flow of water above the town. However, these works had not been completed because Corporation officials believed that building these flood defenses was the responsibility of a private company which controlled the land above the town. In February 1985, the Corporation sent one letter to secure the company's cooperation, but had not received a response and had not followed up on the matter. As a result, the town was still vulnerable to flash floods which caused a great deal of destruction during the El Nino disaster. We recommend that the flood protection work in Tembladera be completed. USAID/Peru agreed with this finding and recommendation.

AID should be able to respond to urgent medicine requirements in a timely fashion. It took more than a year, however, for medicines purchased under the Disaster Rehabilitation project to arrive at the two Ministry

of Health regions selected for assistance. It took the medicines more than a year to arrive because of the time required to refine the Ministry of Health's requirements and order the medicines, and more importantly because of bureaucratic delays in clearing the medicines from the customs warehouse in Peru and sending them to the regions where they were needed. These delays reduced the medicine component's effectiveness in responding to the health crisis created by the El Nino disaster. We recommend that lessons learned from this procurement be documented to help the designers of future projects avoid similar problems. USAID/Peru officials agreed with this finding and recommendation.

Office of the Inspector General

AUDIT OF USAID/PERU'S
DISASTER RELIEF, REHABILITATION
AND RECONSTRUCTION PROJECT (NO. 527-0277)

TABLE OF CONTENTS

	<u>Page</u>
PART I - INTRODUCTION	1
A. Background	1
B. Audit Objectives and Scope	2
PART II - RESULTS OF AUDIT	3
A. Findings and Recommendations	4
1. Flood Defenses for Tembladera Needed To Be Completed	4
2. Medical Procurement Was Substantially Delayed	6
B. Compliance and Internal Controls	8
1. Compliance	8
2. Internal Controls	8
C. Other Pertinent Matters	9
PART III - EXHIBITS AND APPENDICES	
A. Exhibits	
1. Status of AID Funding as of September 30, 1986	
B. Appendices	
1. Management Comments	
2. Report Distribution	

AUDIT OF USAID/PERU'S
DISASTER RELIEF, REHABILITATION
AND RECONSTRUCTION PROJECT (NO. 527-0277)

PART I - INTRODUCTION

A. Background

El Nino is a warm ocean current which normally appears off the coast of Peru and Ecuador near Christmastime. Abnormal variations in the current in 1982 caused severe flooding in the North and severe drought in the South of Peru. USAID/Peru estimated that the economic losses attributable to the disaster accounted to no less than \$1.8 billion. According to Mission officials, Peru's gross national product fell 11 percent in 1983. They estimated that one-half of this decline was directly attributable to the El Nino disaster.

AID's response to the disaster in Peru consisted of three phases: emergency relief, immediate rehabilitation, and long-term rehabilitation and reconstruction. Emergency relief was provided by the Office of Foreign Disaster Assistance, and by USAID/Peru in the form of reprogrammed food and medicines from its ongoing programs. Immediate rehabilitation assistance included reprogrammed housing investment guarantee funds, reprogrammed Section 416 milk, Public Law 480 Title I and II foodstuffs, and operational support to private voluntary organizations responsible for food distribution. AID's longer-term response principally consisted of additional housing investment guarantee funds, balance of payments support, and the Disaster Relief, Rehabilitation, and Reconstruction project (No. 527-0277).

The Disaster Relief, Rehabilitation, and Reconstruction project was the largest component of AID's longer-term response. The project agreement was signed on July 20, 1983, and the project assistance completion date (extended nine months from the original date) was March 31, 1987. The project budget included \$65 million in AID funds and \$22 million in counterpart funds, for a total of \$87 million. Exhibit 1 of this report summarizes the status of AID funding as of September 30, 1986.

The purpose of the project was to establish a coordinating unit for disaster assistance in the National Development Institute (INADE), and to establish a reconstruction fund for financing disaster recovery subprojects. The project design was unique in that most of the AID funds were not programmed for specific purposes at the outset of the project. Rather, they were made available to fund subprojects proposed by the Government at the beginning of each year of the project. In general, the subprojects in the North of Peru approved by AID were directed toward reconstructing irrigation works, roads, bridges, housing, and service infrastructure destroyed by floods. The approved subprojects in the South generally aimed to reactivate the agricultural sector, generate employment, and diminish the effects of future droughts. At the time of our audit, USAID/Peru had approved 113 subprojects. While the Mission

was concerned primarily with approving and monitoring the status of subprojects, these subprojects could be further divided into about 770 components and well over 1,000 individual works or locations.

USAID/Peru hired 34 contractors to carry out AID's implementation and monitoring responsibilities. In the Government of Peru, INADE was responsible for overall project coordination. Almost all of the project activities were implemented by fifteen Departmental Development Corporations, although the Ministry of Health and the Materials Bank implemented two small components for importing medicines and rebuilding houses and services destroyed by floods.

B. Audit Objectives and Scope

The Office of the Regional Inspector General for Audit/Tegucigalpa conducted a program results audit of USAID/Peru's Disaster Relief, Rehabilitation, and Reconstruction project. The audit objectives were to evaluate the project's effectiveness in achieving planned results, and to assess compliance with AID requirements. Where project deficiencies were disclosed, applicable internal controls were examined.

The audit work was performed from August 11 through November 21, 1986, in the Departments of Lima, Cajamarca, Moquegua, Piura, and Tacna, Peru. Activities from the project's inception on July 20, 1983 through November 21, 1986 were reviewed. The audit covered AID disbursements and advances of \$60.5 million as of September 30, 1986.

The audit included interviews with officials in USAID/Peru, the Government of Peru, and one private voluntary organization implementing the project. It also included reviews of documentation such as plans, agreements, reports, correspondence, and financial records. Documentation supporting AID expenditures of \$87,125 was reviewed. No supporting documentation for the expenditure of counterpart funds was reviewed.

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

AUDIT OF USAID/PERU'S
DISASTER RELIEF, REHABILITATION
AND RECONSTRUCTION PROJECT (NO. 527-0277)

PART II - RESULTS OF AUDIT

The Disaster Relief, Rehabilitation, and Reconstruction project had achieved its purpose of making a disaster assistance coordinating unit and a reconstruction fund operational. USAID/Peru's system for measuring project effectiveness was generally satisfactory, although its reports on the progress of AID-funded subprojects contained some inaccuracies. For example, the reports were supposed to show the subprojects' overall progress for all three years of the project. According to the project monitoring coordinator, however, as late as August 22, 1986 the percentage completion shown for each subproject could actually represent progress against 1986 goals only, or the status of the project at the end of 1984. Other inaccuracies were also noted. Compliance with AID requirements was generally adequate.

The project's effectiveness reflected the hard work performed by a large number of well-qualified professionals in the AID Mission and in the Government of Peru. In a little over three years, over \$50 million had been disbursed in fifteen Departments throughout Peru. According to the National Development Institute, the project had:

- rehabilitated or expanded irrigation systems serving 312,534 hectares (over 1,200 square miles) of farm or pasture land;
- rehabilitated 3,425 kilometers of road, and reconstructed or repaired bridges extending a total of two kilometers in length;
- distributed 5,790 metric tons of seeds and fertilizers, and provided 13,955 recapitalization loans to small farmers affected by the drought;
- installed potable water systems delivering a total of 1,380 liters per second, built 656 wells, and rehabilitated 24 others;
- repaired or built 1,869 homes;
- built or repaired 196 small reservoirs, controlling over 130,000 cubic meters of water;
- built over 29 kilometers of river defense walls and breakwaters, protecting urban populations and farm land.

The findings in this report describe the need to complete flood protection work in Tembladera, and delays in receiving emergency medicines. Four other pertinent matters are also discussed. The recommendations are that flood protection work in Tembladera be completed, and that lessons learned from a delayed medical procurement be documented.

A. Findings and Recommendations

1. Flood Defenses for Tembladera Needed To Be Completed

The Departmental Development Corporation (CORDE) in Cajamarca spent about \$277,000 in Tembladera to protect the town from destructive flash floods and to rebuild two bridges which were destroyed in 1983. Additional works were planned to direct flow of water above the town. However, these works had not been completed because CORDE officials believed that building these Flood defenses was the responsibility of a private company which controlled the land above the town. In February 1985, the CORDE sent one letter to secure the company's cooperation, but had not received a response and had not followed up on the matter. As a result, the town was still vulnerable to flash floods which caused a great deal of destruction during the El Nino disaster.

Recommendation No. 1

We recommend that USAID/Peru obtain evidence that appropriate flood defenses have been built above the town of Tembladera.

Discussion

In 1983, a flash flood swept through the town of Tembladera and destroyed two vehicular bridges. CORDE Cajamarca spent about \$277,000 to widen and line a natural ravine with cement, and to rebuild the bridges. The purpose of widening and lining the ravine within the town itself was to protect against future flash floods. Above the town, eight rock and cement walls were planned to be constructed to direct flood waters into the ravine in order to ensure that they did not pass through another part of the town, destroying houses and possibly causing loss of life.

While the work within Tembladera was complete at the time of our audit, no work was done on the flood defenses above the town. While the path of flood waters had never been predictable, the work of a cement company on this land made their future course even more uncertain. The CORDE President, who had personally inspected the site, believed that flood waters would most likely not flow into the ravine which was widened and strengthened to channel them harmlessly through the town.

CORDE officials believed that the private cement company which controlled the land was responsible for constructing the planned flood control works above Tembladera. They maintained that public funds could not be invested on private land. In February 1985, the CORDE sent a letter to the district civil defense committee urging the committee to secure the company's cooperation. It received no reply, however, and had not since followed up on the matter. If the planned works above Tembladera are not completed, the flood protection works within the town will probably not serve their intended purpose.

USAID/Peru should ensure that the planned flood control works above Tembladera are completed. These works are needed to make the existing investment in the town effective, and to prevent future destruction which could possibly include loss of life.

Management Comments

USAID/Peru officials agreed with this finding and recommendation, but wondered if a commitment to take corrective action would suffice to close the recommendation.

Office of Inspector General Comments

The Inspector General's policy is that for actions which can be accomplished within one year of report issuance, the appropriate basis for closing audit recommendations is completed corrective action.

2. Medical Procurement Was Substantially Delayed

AID should be able to respond to urgent medicine requirements in a timely fashion. It took more than a year, however, for medicines purchased under the Disaster Rehabilitation project to arrive at the two Ministry of Health regions selected for assistance. It took the medicines more than a year to arrive because of the time required to refine the Ministry of Health's requirements and order the medicines, and more importantly because of bureaucratic delays in clearing the medicines from the customs warehouse in Peru and sending them to the regions where they needed. These delays reduced the medicine component's effectiveness in responding to the health crisis created by the El Nino disaster.

Recommendation No. 2

We recommend that USAID/Peru document, through a Mission Order or another appropriate means, lessons learned from the Disaster Rehabilitation project medicine procurement to help designers of future projects avoid similar delays.

Discussion

The El Nino disaster created a health crisis which included increased incidence of malaria, tuberculosis, skin diseases, and respiratory and gastro-intestinal infections. The Disaster Rehabilitation Project included \$410,109 in funding for medicines, to address the disaster-related requirements that were not met through other ongoing AID projects. Given the fact that many medicines were either depleted or in very short supply, USAID/Peru should have ensured that the medicines arrived in the regions where they were needed in a timely manner.

In fact, it took the medicines an average of more than a year to reach the health regions. None of the medicines arrived earlier than one year after the Ministry of Health requested them, and one shipment took twenty months to arrive. These delays reduced the medicine component's effectiveness in responding to the health crisis created by the El Nino disaster.

The following table shows the average time it took to complete the major steps in the procurement and distribution process:

Review Ministry of Health request and issue project implementation order	3 months
Issue purchase orders	2 months
Ship medicines	2 months
Receive medicines (in customs)	7 days
Clear medicines from customs	4 months
Receive medicines in the regions	3 months

It took three months to review the Ministry's request, refine the list of medicines, and issue the project implementation order. This was because non-disaster-related medicines had to be removed from the list, and because it was difficult to identify suppliers for some medicines. It was particularly difficult to locate a supplier for Primaquine, a drug used to treat malaria in epidemic situations.

Lengthier delays were caused by the Ministry's inability or unwillingness to carry out its responsibilities expeditiously. While USAID/Peru had worked with other parts of the Ministry, it had never worked with the Epidemiology Division before. Both the Mission and the Epidemiology Division were interested in responding to the increasing incidence of tuberculosis, and the Disaster Rehabilitation medicine procurement was seen as a pilot project for a possible larger effort. Experience showed, however, that many of the Division's personnel were less than competent, and did not assign any sense of urgency to implementing the medicine component. The Division's limited capabilities were reduced by frequent reorganizations and turnover of key personnel. In retrospect, Mission officials believed that technical assistance should have been provided to speed implementation of this component.

It took the Ministry an average of four months to clear medicines through Peruvian customs, and it took eleven months to clear one shipment. The Mission's Health Development Officer agreed it would have been wise to consign the medicines to the AID Mission to avoid these delays, even though the Mission's customs clearance personnel were burdened with other responsibilities.

Once cleared from customs, the medicines remained in the Ministry's central warehouse for an average of three months before they were sent to the health regions where they were needed. Two drugs were not sent to the regions for almost six months. According to the Mission Health Officer, this could have been due to a lack of money for transportation or to a lack of understanding of the urgent need for these medicines.

The most important delays discussed above could have been avoided if urgently needed medicines had been consigned to USAID/Peru to facilitate customs clearance, and if the Mission had provided for technical assistance (or at least considered providing technical assistance, given that it had no previous experience with the Epidemiology Division). These lessons learned should be documented through a Mission Order or another appropriate means, to help designers of future projects avoid similar delays.

Management Comments

Mission officials agreed with this finding and recommendation. They emphasized their willingness to apply lessons learned through experience to future projects.

B. Compliance and Internal Controls

1. Compliance

The audit disclosed three compliance exceptions:

- Some AID-funded subprojects did not comply with the selection criteria developed by INADE and approved by USAID/Peru (following report section).
- In at least 30 cases, subproject proposals were not approved by INADE or AID's Departmental Advisors, as required by Project Implementation Letter No. 77 (following report section).
- USAID/Peru's Disaster Relief Plan had not been updated annually, as required by AID Handbook 8 (following report section).

Other than the conditions cited, tested compliance items were in compliance, and nothing led us to believe that untested items were not in compliance with applicable laws and regulations.

2. Internal Controls

The audit revealed three internal control exceptions:

- No AID/Washington guidance was available to prevent use of funds from the Disaster Relief, Rehabilitation, and Reconstruction project to support long-term development activities which did not respond to the effects of the El Nino disaster (following report section).
- USAID/Peru's system for ensuring that subproject proposals were reviewed by INADE and AID's Departmental Advisors did not always operate effectively (following report section).
- Mission personnel responsible for payment verification reported to the project coordinator. The principle of separation of duties requires that the Controller supervise these personnel (following report section).

C. Other Pertinent Matters

Appropriateness of Subprojects - To satisfy a condition precedent to disbursement, INADE developed six criteria for selecting disaster relief subprojects. A small portion of the subprojects approved and funded by USAID/Peru did not comply with these criteria and, in our opinion, should not have been funded under this project. The subprojects which did not comply with INADE's criteria aimed to introduce innovative farming and watershed management practices which could not reasonably be expected to have a significant impact until many years after the effects of the El Nino disaster had passed. These types of activities might be acceptable in a disaster assistance project if at the same time they helped respond to the effects of the disaster: for example, by providing employment opportunities. Activities which do not respond to the effects of a disaster, however, should not by definition be funded through disaster assistance projects.

For example, one component of the "Assistance to Agricultural Production" subproject in Tacna was intended to develop and disseminate water-saving irrigation methods. Before these innovative irrigation systems are accepted by a significant number of farmers, however, the Government of Peru must adopt water pricing policies that encourage farmers to save water, and a way must be found to make the systems more affordable. This component may have been worthy of AID's support through a development assistance project. However, it should not have been funded through the Disaster Rehabilitation project because it did not comply with INADE's criteria for subproject selection, because it had not helped mitigate the effects of the El Nino disaster, and because it will be many years before the systems promoted through this component are accepted by a large number of farmers. For the same reasons, we question USAID/Peru's funding of another pilot irrigation activity in Moquegua, an experimental forestation and reforestation subproject in Tacna, and an agricultural demonstration subproject in Huancavelica. These activities were approved for AID funding of about \$200,000. We plan to recommend in a separate report that the Bureau for Program and Policy Coordination develop guidance on what activities should and should not be funded under disaster assistance projects.

Subproject Approvals - Project Implementation Letter No. 77 required that subproject proposals be signed by an INADE representative and by an AID Departmental Advisor. Over 30 subproject proposals funded by AID lacked one or both of these approvals. On the other hand, while these formal approvals were frequently missing, the Mission's files contained ample evidence that subproject proposals were closely scrutinized before they were funded by USAID/Peru.

Separation of Duties - The principle of separation of duties requires that the Controller's Office manage payment verification activities while line offices manage project implementation activities. The purpose of this separation of duties is to ensure the independence of personnel who enforce AID requirements for accountability of funds. However, USAID/Peru had assigned four newly-hired project-funded financial analysts to the Disaster Relief and Rehabilitation Office because the

Controller's Office was burdened with other responsibilities. These financial analysts reviewed the supporting documentation for expenditures of AID funds, although they did not have authority for voucher processing or for recording transactions in the Mission's accounting records. In the future, USAID/Peru should provide for an appropriate separation of duties between the Controller's Office and its line offices.

Disaster Relief Plan - Section 3E of AID Handbook 8 requires that Mission Disaster Relief Plans be updated annually or as often as needed. USAID/Peru's Disaster Relief Plan, however, had not been revised since November 1980. Mission officials recognized that the plan needed to be revised, but had not done so due to other competing priorities. As a result, the Mission did not have a disaster relief plan with current information on AID, host country, and other donor resources available to deal with disasters, although it did have a list of current host country contacts and phone numbers. It is particularly important that the Disaster Relief Plan be revised since Peru is one of the most disaster-prone countries in the world.

AUDIT OF USAID/PERU'S
DISASTER RELIEF, REHABILITATION
AND RECONSTRUCTION PROJECT (NO. 527-0277)

PART III - EXHIBITS AND APPENDICES

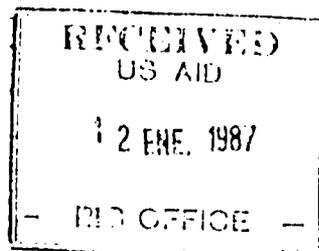
EXHIBIT 1

Status of AID Funding
As of September 30, 1986

<u>Element</u>	<u>Obligations</u> <u>(\$000)</u>	<u>Accrued</u> <u>Expenditures</u> <u>(\$000)</u>
Technical Assistance	5,448	5,001
Operational Support	2,792	2,370
CORDE Subprojects	50,360	46,466
Ministry of Health	600	468
Materials Bank	1,000	861
PVO Operational Support	<u>4,800</u>	<u>4,434</u>
Totals	65,000 =====	59,600 =====

UNITED STATES GOVERNMENT

Memorandum



APPENDIX 1
Page 1 of 7

TO : Mr. Coinage N. Gothard, RIG/A/T

DATE: December 30, 1986

FROM : *George A. Hill*
George A. Hill, Deputy Director, USAID/Peru

SUBJECT: Mission Comments on Draft Report on Audit of USAID/Peru's Disaster Relief, Rehabilitation and Reconstruction Project (No. 527-0277)

1. Even though the issue of eligibility of payroll taxes in project costs has been resolved, as reported in cable Lima 05252, we believe that the audit report's allusions to inconsistency in application of concepts needs clarification. The Mission believes that allocations of project and counterpart financing for local costs should be part of the project design and negotiation process. As a policy we believe that whichever entity (AID or the GOP) finances a salary input, that same entity should finance the employer's benefit contribution payroll costs. This will facilitate internal accounting control over different financing sources. We assume that "Management Comments", page 24, will be adjusted to reflect the above comments as well as the payroll tax eligibility clarification.
2. On pages 26 and 27, there are comments related to Financial Analysis which are inaccurate. With respect to payment verification, the audit should make clear that project financial analysts did not have authority for voucher processing or for recording transactions in the Mission's accounting records. These functions were performed independently by the Mission Controller's Office. In no way did all Mission personnel responsible for payment verification report to the project coordinator. Secondly, project financial analysts were frequently expected to play a technical role in providing on-site advice in the CORDES regarding financial administration issues and, in this capacity, formed part of the Mission's and the CORDES' implementation team. The independent USAID Controller function of assuring that adequate payment review and accounting procedures were in place at the implementing organization level was performed by Controller staff not by project-financed financial analysts.
3. The following comments and clarifications may affect some of the conclusions drawn from your field review. They, at least, modify the presentation of "Management Comments", page 13.



- a) Executive Summary, page i: There is some divergence in estimates of damage from the 1982-83 El Niño disaster; some studies do not support a figure as high as \$1.8 billion. It would be safer to state that the damage was over \$1 billion.
- b) Page ii: We disagree with the following conclusions: (1) that some of the subprojects did not respond to the effects of the El Niño disaster, (2) that subproject criteria were not always adhered to, (3) that subproject proposals were not always formally approved by INADE and the departmental advisors, and (4) that funds which could have been used to directly address the effects of the disaster went instead to support activities which had only a tangential relationship with the disaster. See more detailed discussion below in (i), (j), and (k).
- c) Page iii: After further review, we believe that all subprojects funded through the Project were appropriate for Project financing. See (i) below.
- d) Audit Report, page 1: While a mild form of the El Niño current comes every year, every several years it is accompanied by a reversal of equatorial winds and by other meteorological anomalies, which bring substantial rains to the normally arid northern coastal plain of Peru. More often than not, this is accompanied by drought during what is normally the rainy season in the southern highlands. The 1982-83 El Niño did not come especially early, and it lasted only one season but what characterized it was its severity. It rained more in six months in Piura Department than it had in the previous 57 years combined. Some scientists estimate it was the most severe El Niño in at least a century.
- e) Page 1: See comment in (a) above on estimate of economic losses.
- f) Page 5: We do not agree that there were serious inaccuracies in the subproject monitoring and reporting system. The system was initially established to follow the progress of subprojects and components on a year-by-year basis, in conformance with the GOP's own project monitoring procedures. We then began to transform the system to be able to follow the progress of each component over all the years of its implementation, while continuing to track progress of yearly subproject objectives.

By mid 1986, this transition was still being made, and it was almost complete. We were aware of those cases where the information was still not fully in the multi-year format, generally footnoted those cases in the consolidated reports, and were actively working on obtaining reliable, updated information to input into the system. It should be pointed out that information for the system comes not only from periodic reports from the CORDES but also from the inspection observations of a large number of AID and INADE technical advisors. Great pains are made to resolve and verify conflicting information. In all, the Mission believes that while not perfect, the subproject monitoring system is highly accurate, especially considering the large number of components being tracked and their geographic dispersion and remoteness. The Mission therefore accepts that while there may still have been deficiencies in the system on August 22, 1986, and perhaps some minor inaccuracies, "serious inaccuracies" did not exist.

- g) Pages 5-6: Updated estimates from INADE on achievements are:
- rehabilitated or expanded irrigation systems serving 312,534 hectares (over 1,200 square miles) of farm or pasture land;
 - rehabilitated 3,425 kilometers of road;
 - distributed 5,790 metric tons of seeds and fertilizers;
 - installed potable water systems delivering a total of 1,380 liters per second;
 - repaired or built 1,869 homes;
 - reconstructed or repaired bridges extending a total of two kilometers in length;
 - built or repaired 196 small reservoirs, controlling over 130,000 cubic meters of water;
 - built over 29 kilometers of river defense walls and breakwaters, protecting urban populations and farm land;
 - provided 13,955 recapitalization loans, through revolving funds, to small farmers affected by the drought; and

- built 656 new wells in the south and rehabilitated 24 others, providing over 75,000 cubic meters of water for irrigation and potable water use.
- h) Page 7: Same comments as in (b) above. See the detailed discussion in (i), (j), and (k) below.
- i) Pages 8-11: The PP indeed stated that project funds would be used to finance only activities which are directly related to the natural disasters, and yet it did include in its illustrative list of possible subprojects such development oriented activities as trial seed plots and hydraulic studies. This apparent discrepancy was discussed in the PP, which stated that the unusual weather brought certain opportunities for natural resources development which should be capitalized on. Indeed, USAID believes that in a drought recovery, in an area of recurrent droughts, it is short-sighted to concentrate solely on getting agricultural and animal production back to pre-drought levels and not to train people in how to properly utilize their land and scarce water resources. Otherwise, the GOP and the AID will be back with another major assistance program the next time the rains fail. During and immediately after a drought is the ideal moment to undertake such irrigation, reforestation, soil conservation, animal husbandry, and water and land use training activities which make the investments being made much more effective by helping to alleviate future droughts, since people's memories are fresh about the drought's affects.

The examples given in the draft audit report are cases in point. The dissemination of water-saving irrigation methods in arid Tacna and Moquegua, forestation geared to holding soils and protecting watersheds in drought-affected areas, and the demonstration of drought-resistant seed varieties are long-term development activities which are also directly related to drought recuperation. USAID would agree that a major forestry program, or the establishment of a host country research capability, would not be appropriate as part of a reconstruction project. But small efforts, targetted directly to affected populations, utilizing or adapting known technologies, and geared to making the agricultural recovery more effective in the long-run, are appropriate reconstruction activities. In short, we believe that certain long-term development activities may qualify as

being disaster related and that such activities are consistent with INADE's criteria of reactivating the agricultural sector in the South of Peru. Thus we do not agree with the argument (page 11) that preparing for future disasters is an either/or proposition vis-a-vis disaster reconstruction. The two can be intimately related.

The Cajamarca watershed study (p. 10) has a completely different history. A number of streams and small rivers flow through the City of Cajamarca and its environs, prior to forming a single river which flows out of the valley. These streams and rivers flooded in 1983, causing considerable damage. Early in the reconstruction program, a number of immediately needed river defenses were constructed or reconstructed, with several larger investments proposed for later. There was concern on the part of both the Cajamarca Development Corporation and USAID that such investments not be made without a thorough study of the watershed and its flows. Thus the study did not have a long-term development orientation, as stated in the draft audit report, but a technical orientation directly related to proposed reconstruction activities. As the draft audit report correctly states, as funds became tight in 1986, INADE asked that the study be withdrawn from Project financing. The study and the additional river channeling investments are expected to be financed in the future by the GOP with its own funds.

Since the departure of the audit team, INADE and USAID have held a series of meetings at which every component financed under the Project was reviewed. USAID believes that every activity financed under the Project appropriately responded to the effects of the El Niño disaster and fell within the criteria set forth in the P.P.

- j) Page 11: We believe that AID-funded subprojects did comply with the established criteria. As discussed above, it is our position (and the GOP's) that the AID-financed activities geared toward preventing future disasters were an integral part of the reactivation of the agricultural sector in the South of Peru, which was one of INADE's criteria. Another INADE criterion was that priority for Project-funded activities be given to those activities which were included in the National Rehabilitation and Reconstruction Plan. That Plan establishes on page one of Volume II that one of

the objectives of the Reconstruction Program will be to prevent future disasters, and the majority of the activities questioned by the auditors are specifically listed in the Plan. Admittedly the criteria developed by INADE, in the heat of early implementation, were not as specifically extensive as they might have been. But it seems unrealistic to expect USAID to have rejected proposals for activities listed in both the GOP's Reconstruction Plan and our own PP, which were sent to us by INADE under cover letter stating that in INADE's opinion they complied with INADE's own selection criteria. We believe that the selection criteria were fully understood by all involved parties and were consistently applied. The Project files are filled with examples of proposals which were rejected because they did not comply with these criteria.

- k) Pages 11-12: It is incorrect to state that subproject proposals were not always formally approved by INADE. Every proposal came under a cover letter indicating INADE's approval, even when on occasion the actual proposal form itself might not have been signed.

It is true that occasionally a subproject proposal form was submitted without the Departmental Advisor's signature. The audit report should reflect, however, that this was typically due to advisors covering more than one department and being unavailable when a proposal form was being prepared. This, of course, could have been rectified by post factum signature, but for one reason or another such was not always done. However, the record (e.g., advisor's reports, notes from advisors' meetings, field trip reports) is clear that subprojects were only approved which had Departmental Advisors' support. USAID does not consider the occasional lack of signature as a "problem".

- l) Page 12: As discussed in (i) above, we disagree with the statement that inappropriate activities were funded, and that therefore some appropriate activities lacked funding.
- m) Page 13: At the auditors' exit conference, USAID officials did concede the possibility that a few Project-funded activities may not have been entirely appropriate for inclusion in the Project. A subsequent review, however, component by component, has not identified a single activity which the Mission considers inappropriate for Project financing.

- n) Page 25: For reasons discussed in (i) above, we do not agree that some AID-funded subprojects did not comply with the Project's selection criteria. We also (see (k) above) do not agree that subproject proposal were not approved by INADE. While some subproject proposals forms were not signed by Departmental Advisors, we believe the record is sufficiently clear as to the Advisors' concurrence with the activities undertaken, and thus we do not believe the lack of signature constitutes a compliance exception from a procedure we ourselves established.
- o) Pages 25-26: We reiterate that certain long-term development activities can also be considered appropriate in a post-drought agricultural recuperation context. We also fail to see the connection between INADE's sending their approval via cover letter rather than signing the actual subproject proposal form and the statement that our system for ensuring review of subproject proposals "did not always operate effectively." Likewise, when an advisor who indicates approval of a subproject by other means fails to sign the subproject approval form, it does not mean that the system for ensuring subproject proposal review was ineffective.
4. In summary, we believe that only the last of the compliance exceptions, page 25, is accurately presented. We are in the process of updating the "Plan". We do not agree with the internal control exceptions. We have met with all parties concerned trying to develop a solution to the problem presented in Recommendation No. 2. However, time may be the greatest restraint. We agree with the content of Recommendation No. 3 and will take action to document Mission experience.

APPENDIX 2

REPORT DISTRIBUTION

	<u>No. of Copies</u>
Director, USAID/Peru	5
AA/LAC	2
AA/M	2
AA/PPC	2
LAC/SAM/BP	1
LAC/CONT	1
LAC/DP	1
LAC/DR	1
LAC/GC	1
OFDA	1
GC	1
AA/XA	2
XA/PR	1
LEG	1
M/FM/ASD	3
LAC RIAs	1
PPC/CDIE	3
IG	1
D/IG	1
IG/PPO	2
IG/LC	1
IG/PSA	1
IG/FMS/C&R	12
IG/II	1
RIG/II/T	1
Other RIG/As	1