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AUDIT OF THE CREDIT PROGRAM FOR RURAL COOPERATIVES WITH THE COSTA RICAN COOPERATIVE BANK IN COSTA RICA

PUBLIC LAW 480, TITLE I

Audit Report No. 1-515-87-25-N
May 22, 1987

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

AGENCY FOR INTERNATIONAL DEVELOPMENT

OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

TELEPHONES:
32-9987
also 32-3120 EXT. 2701-2703

May 22, 1987

MEMORANDUM

TO : D/USAID/Costa Rica, Daniel A. Chaij

Coinage N. Gothard

FROM : RIG/A/T, Coinage N. Gothard, Jr.

SUBJECT: Audit Report No. 1-515-87-25-N, "Audit of the Credit Program for Rural Cooperatives with the Costa Rican Cooperative Bank in Costa Rica - Public Law 480, Title I"

This report presents the results of a non-Federal financial and compliance audit requested by your Mission of the Credit Program for Rural Cooperatives with the Costa Rican Cooperative Bank (BANCOOP) - Public Law 480, Title I. The certified public accounting firm of Touche Ross & Co. prepared the report, which is dated May 18, 1987.

The purpose of this financial and compliance audit was to determine if the financial information of the project fairly presented its financial position and results of operations as of September 30, 1985; to study and evaluate BANCOOP's internal controls for controlling project assets; and to determine if BANCOOP complied with applicable laws, regulations and agreements.

In the opinion of Touche Ross, the financial information presented fairly the financial position and results of operations of the project as of September 30, 1985 except for certain non-compliance with agreement terms. Their study and evaluation of internal controls disclosed weaknesses in BANCOOP's accounting records and loan information system. Also, BANCOOP did not use a separate bank account for PL480, Title I funds. These conditions result in more than a relatively low risk that errors or irregularities in amounts that would be material in relation to the project's financial information may occur and not be detected within a timely period. They also determined that BANCOOP had not complied with certain agreement terms applicable to the project. For items not tested, nothing came to their attention that caused them to believe that untested items were not in compliance.

The Touche Ross report contains 15 recommendations to improve BANCOOP's internal controls and 6 recommendations to achieve compliance with applicable laws, regulations, and agreements. We believe that these recommendations will significantly improve BANCOOP's administrative and compliance weaknesses. As a result, the following recommendation will be included in the Office of the Inspector General's audit recommendation follow-up system.

Recommendation No. 1

We recommend that USAID/Costa Rica obtain evidence from the Costa Rican Cooperative Bank (BANCOOP) in Costa Rica to demonstrate that, to improve the Credit Program for Rural Cooperatives, it has implemented the 15 recommendations for internal controls and the 6 recommendations for compliance contained in the Touche Ross report dated May 18, 1987.

Please advise this office within 30 days of the actions planned or taken to implement this recommendation.

Lara & González, CPA
Member Firm
Touche Ross International

COSTA RICAN COOPERATIVE BANK (BANCOOP)
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CREDIT PROGRAM FOR RURAL COOPERATIVES

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COSTA RICAN COOPERATIVE BANK (BANCOOP)

PL 480 TITLE I IN COSTA RICA

CREDIT PROGRAM FOR RURAL COOPERATIVES

AUDIT REPORT

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Lara & González, CPA
Member Firm
Touche Ross International

May 18, 1987

Mr. Coinage N. Gothard
Regional Inspector General for Audit
U. S. Agency for International Development
Tegucigalpa, Honduras, C. A.

Dear Mr. Gothard:

This report presents the results of our examination of the agreement among the Costa Rican Cooperative Bank (Banco Cooperativo Costarricense, R. L., BANCOOP) the National Institute for Cooperative Promotion (Instituto Nacional de Fomento Cooperativo, INFOCOOP), the Ministry of National Planning and Economic Policy (Ministerio de Planificación Nacional y Política Económica, MIDEPLAN), and the U. S. Agency for International Development in Costa Rica (USAID/Costa Rica), signed on December 21, 1983, as part of the assistance program of the United States of America to developing countries under Public Law 480 Title I (PL 480 Title I).

BACKGROUND

On March 25, 1982, the Governments of the United States of America and Costa Rica (GOCR) signed an agreement for the sale of agricultural products under PL480 Title I, which was confirmed on April 22, 1982, by the GOCR Law Decree No. 6751. Under this agreement the Government of the United States was to provide $18 million worth of U. S. agricultural products during fiscal year 1982. These products were to be sold to authorized Costa Rican buyers and the proceeds (approximately 485 million Costa Rican Colones), would be used by the GOCR to stimulate agricultural production and provide economic development assistance, thereby combating hunger and malnutrition.

The part of the agreement subject to this audit was signed on December 21, 1983, with MIDEPLAN as coordinator, BANCOOP and INFOCOOP as recipients and USAID/Costa Rica representing the U. S. Government. This agreement provided 191,250,000 Costa Rican Colones (equivalent to $5,000,000 at that date) to be invested in BANCOOP as Special Contribution Certificates at a minimum annual interest rate of 6% during a period of ten years. These special

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certificates could be repaid by BANCOOP in 20 annual instalments starting in the eleventh year. The agreement entitled INFOCOOP to use the earned interest to finance its activities regarding supervision, training, promotion and technical advisory services for cooperatives. However by Law Decree No. 6957 of February 23, 1984, and 7015 of November 29, 1985; the earned interest should be used for the same purposes through: Cooperative Training and Study Center (CENECOOP) (62.5%) Cooperative Youth Programs (25%), and National Council of Cooperatives (CONACOOP) (12.5%).

BANCOOP, for its part, shall use the provided funds to finance exclusively rural cooperatives in activities that: a) produce savings or foreign currencies; b) improve the commercialization channels and the utilization of natural resources; and, c) promote a better democratization of the economy. Among other requirements, BANCOOP should: a) present to MIDEPLAN quarterly reports on financial information and progress of the project; and b) keep independent accounting records for project's operations.

The Bank was set up as a corporation in January 1982, in accordance with the laws of Costa Rica and the dispositions of the Organic Law of the National Banking System. As a result of Law 6894 of September 22, 1983, that allowed the creation of private cooperative banks, in November 1983 the stockholders of the Banco Costarricense de la Cooperación, S. A. represented by the associated cooperatives, approved the constitution and the transfer of all the assets and liabilities to the Banco Cooperativo Costarricense, R. L. (BANCOOP). This action was approved in January 1984 by the General Banking Auditor of Costa Rica.

BANCOOP is administered by a Board of Directors integrated by five members elected annually by the General Assembly of Associates. The members of the Board cannot be managers, officers or employees of the same or other banks.

AUDIT OBJETIVES AND SCOPE

The general objective was to conduct a financial and compliance review of the specific project carried out by the BANCOOP during the fiscal years ended on September 30, 1984 and 1985.

The audit was performed in accordance with generally accepted auditing standards and the U. S. General Accounting Office "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision), and therefore included such tests of the accounting records considered necessary in the circumstances. Our examination was made to determine whether:

1. The financial information of the BANCOOP's audited program fairly presented the financial position of the project and

the results of its financial operations in accordance with generally accepted accounting principles;

2. The internal accounting control of BANCOOP reasonably contributed to controlling the project assets, disclosing any material weaknesses with recommendations for corrective action; and

3. BANCOOP had complied with applicable terms and conditions of the approved National Budget, local currency activity agreements and letters of understanding; with a positive assurance on tested items and a negative assurance on those items not tested.

The scope of our work consisted of:

1. examining the specific project from February 22, 1984, the date of the initial transfer of PL480 Title I funds in local currency to BANCOOP, up to September 30, 1985;

2. reviewing all the applicable agreements on local currency;

3. reviewing the letters of understanding and the decrees under which programmed funds were incorporated to the National Budget of Costa Rica;

4. performing a study and evaluation of BANCOOP's system of internal accounting control, limited to controls on the PL480 Title I funds;

5. evaluating the reasonability of the information reported by each involved institution to USAID/Costa Rica and the Costa Rican Government;

6. reviewing the reconciliations of the bank accounts used to control PL480 Title I funds' reception and disbursement, and determining the validity of the transactions recorded;

7. comparing the agreement funds recorded by BANCOOP against the amounts reported by the transfering institution;

8. determining if BANCOOP had complied with all the terms and conditions approved in the National Budget, the agreement, the letters of understanding and the applicable laws and regulations;

9. determining if BANCOOP: a) had paid fair and reasonable prices for the acquisition of goods and services with PL480 Title I funds; and b) followed sound commercial practices for the use of PL480, Title I funds; and

10. determining if the funds were disbursed only for the purposes of the agreement.

RESULTS OF THE AUDIT

Financial Information of the Project

The financial information of the project as of September 30, 1985, except for non-compliance with agreement terms as explained below, presented fairly the financial position at that date and the accumulated results of operations for the period of nineteen months then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Our review included written confirmation of the loan receivable balances as of September 30, 1985, for approximately 43%, and alternative procedures for approximately 34% of the loan portfolio, in order to: a) trace the loan balances to subsidiary records; b) trace the balances from subsidiary records to the general ledger and to audited financial statements; c) trace individual loan balances to written confirmations made by external auditors "Young & Young Touche Ross" as of December 31, 1985, as applicable; d) review of the subsequent events, including collection of loans, during the period elapsed between the date of the financial information and our opinion (from September 30, 1985 to October 21, 1986).

We reviewed the cash accounts and long-term deposits to determine the reasonableness of balances as of September 30, 1985, and reviewed the operations related to income and expenses connected with PL480 Title I funds from February 29, 1984, the date of the disbursement of funds to BANCOOP, to September 30, 1985. Our review revealed that income taxes paid when BANCOOP was a private bank amounting to 304,053 Colones (approximately $8,000) were deducted by error from income generated by PL480 Title I funds. This amount was not adjusted for in the presented financial statements and we did not qualify our opinion because this amount only represented 1.3% of the accrued earnings as of September 30, 1985. However, we recommend that it be adjusted in findings regarding internal accounting control.

Internal Accounting Control

As part of our examination, we made a study and evaluation of BANCOOP's internal accounting control related to the control and use of project funds, to the extent considered necessary to determine the nature, timing and extent of the auditing procedures necessary for expressing an opinion on BANCOOP's project financial information. Our study and evaluation was more limited that would be necessary to express an opinion on the system of internal accounting control taken as a whole.

Our study and evaluation included the following major areas with the following results:

1. Accounting Records for the Project. Except for some subsidiary records and general ledger accounts, no specific and independent accounting records had been used to record the project operations. However, the BANCOOP's accounting records are appropriate in the circumstances.

2. Income and Disbursements and Cash Controls. BANCOOP did not utilize a specific bank account to control the funds. Consecuently, we could not review the bank activities and reconciliations. However, we reviewed the income and disbursement controls and procedures in use and, except for minor weaknesses included in this report, we concluded that these controls are reasonable and provided an acceptable control of PL480 Title I funds.

3. Presentation of Financial Information. The reports to MIDEPLAN and USAID/Costa Rica presented fairly the financial information and progress of the project, however, the reports were submitted after the dates required by the agreement and, since May 1985, no reports have been submitted because BANCOOP considers that the project was almost completed.

4. Loans Receivable. The evaluated areas were principally related to authorization, disbursements, accountability and recovery of loans receivable. Our study and evaluation revealed some weaknesses that in our opinion, result in more than a relatively low risk that errors or irregularities in amounts that would be material in relation to the project may occur and not be detected.

Compliance with Applicable Laws, Regulations and Agreement Terms

As result of our review, we determined that BANCOOP did not comply with the agreement in what is referred to financing of the rural cooperative sector, independence of accounting records and presentation of reports. Additionally, some changes were made to the agreement terms without the concurrence of all parts involved.

The non-compliance included: a) Loans to the non-cooperative sector, for approximately 70,000,000 Colones, which diverted the PL480 Title I funds which were provided to finance the rural cooperative sector (clause 4.b). The balance of these loans as of September 30, 1985 amounted to approximately 20,000,000 Colones and BANCOOP had apparent good reasons to make the loans. However, a waiver was not obtained. b) No specific and independent accounting records were implemented to control the project operations as required by clause 4.i. However subsidiary records and some isolated general ledger accounts had been used for these purposes and we found that the project financial information could be prepared, but with additional effort. c) Reports were presented to MIDEPLAN and USAID/Costa Rica on an irregular basis; as of September 30, 1985, only four reports were presented and the last report was presented on May 9, 1985, including information as of February 28, 1985. Clause 4.g of the agreement required the presentation of quarterly reports starting on April 24, 1984 (three months after the agreement approval by the General Comptroller of Costa Rica which was issued on January 24, 1984). d) The agreement terms related to the use of proceeds by INFOCOOP were changed by Law Decrees No. 6957 and 7015 without evidence of concurrence of MIDEPLAN and USAID/Costa Rica, as required by Clause 7 of the agreement.

Nothing came to our attention that caused us to believe that untested items were not in compliance with applicable laws, regulations and agreement terms. Finally, although the purpose of our job was not to audit MIDEPLAN, we consider that this institution did not perform the functions of supervising and accomplish self-assistance steps and the agreement did not establish penalties in case of default.

MANAGEMENT COMMENTS

USAID/Costa Rica reviewed this report and BANCOOP's principal officials participated in a discussion of all findings here mentioned, and were in general agreement that the report reflects BANCOOP's condition at the time of the audit work, regarding project operations and control.

Touche Ross & Co.
TOUCHE ROSS & CO.
Certified Public Accountants

Lara & González, CPA
Member Firm
Touche Ross International

COSTA RICAN COOPERATIVE BANK (BANCOOP)

PL480 TITLE I IN COSTA RICA

CREDIT PROGRAM FOR RURAL COOPERATIVES

REPORT ON PROJECT'S FINANCIAL INFORMATION

AUDITOR'S OPINION

We have examined the financial information of the Credit Program for Rural Cooperatives managed by the Costa Rican Cooperative Bank (Banco Cooperativo Costarricense, R. L., BANCOOP), related to PL480 Title I in Costa Rica for the period of nineteen months ended on September 30, 1985. The agreement, signed on December 21, 1983, by BANCOOP, the National Institute for Cooperative Promotion (Instituto Nacional de Fomento Cooperativo, INFOCOOP), the Ministry of National Planning and Economic Policy (Ministerio de Planificación Nacional y Política Económica, MIDEPLAN) and the U. S. Agency for International Development in Costa Rica (USAID/Costa Rica), provided 191,250,000 Costa Rican Colones to finance development activities of Costa Rica's Rural cooperative movement. Our examination was performed in accordance with generally accepted auditing standards and the U. S. General Accounting Office "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision), and accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the project's financial information referred to above, present fairly the financial information therein included related to the project's operations during the period of nineteen months ended on September 30, 1985 in conformity with generally accepted accounting principles applied on a consistent basis, and except for non-compliance with agreement terms without a waiver, as explained in our opinion on this matter issued on October 21, 1986, the funds were used as agreed.

This report is intended solely for the use of BANCOOP, MIDEPLAN, and the U. S. Agency for International Development. This

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restriction is not intended to limit the distribution of this report which, upon acceptance by the AID Regional Inspector General, is a matter of public record.

Touche Ross & Co.

October 21, 1986
San José, Costa Rica

COSTA RICAN COOPERATIVE BANK

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CREDIT PROGRAM FOR RURAL COOPERATIVES

PROJECT'S FINANCIAL INFORMATION

SEPTEMBER 30, 1985

		Colones (Note D)
Funds provided to BANCOOP as special contribution certificates		₡ 191,250,000
Use of funds provided:	Sums Approved	Balance
Loans receivable:		
Cooperative sector	₡ 180,109,000	₡ 162,056,883
Non-cooperative sector	27,332,000	19,660,210
	₡ 207,441,000	181,717,093
Long-term deposits 26% of interest		2,000,000
Cash on hand		7,532,907
		₡ 191,250,000
Non-distributable accrued income included in BANCOOP's financial statements as of September 30, 1985		₡ 26,324,000

The accompanied notes are part integral of this financial information.

COSTA RICAN COOPERATIVE BANK

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PROJECT'S FINANCIAL INFORMATION

BALANCE OF LOANS AS OF SEPTEMBER 30, 1985

	Number of Loans	Colones (Note D)
Cooperative Sector		
Fedecrédito, R. L.	4	¢ 38,250,000
Cooprole, R. L.	1	20,000,000
Fedecoop, R. L.	3	18,600,000
Coopeagri El General, R. L.	2	17,000,000
Coopemontecillos, R. L.	4	16,553,301
Cooprosanvito, R. L.	6	16,285,993
Coopevictoria, R. L.	1	9,500,000
Coopeleca, R. L.	2	8,589,364
Coopejorco, R. L.	2	5,485,714
Coopetierrablanca, R. L.	3	3,750,000
Coopesancarlos, R. L.	3	3,000,000
Coopellanobonito, R. L.	1	2,000,000
Coopesa, R. L.	2	1,666,666
Coopecartago, R. L.	1	882,323
Coonaprosal, R. L.	1	493,522
	36	162,056,883
Non-Cooperative Sector:		
Rohm & Haas, S. A.	2	11,148,204
Atlas Electrónica, S. A.	1	5,000,000
Panaja, S. A.	1	2,000,000
Gte. Sylvania, S. A.	1	1,512,006
	5	19,660,210
	41	¢ 181,717,093

The accompanied notes are part integral of this financial information.

COSTA RICAN COOPERATIVE BANK (BANCOOP)

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CREDIT PROGRAM FOR RURAL COOPERATIVES

NOTES TO PROJECT'S FINANCIAL INFORMATION

FEBRUARY 22, 1984 TO SEPTEMBER 30, 1985

A. Basis of Presentation

BANCOOP's policy is to prepare the project financial information on an accrued basis in accordance with generally accepted accounting principles consistently applied. The accrued net income generated by the project is recorded as "non-distributable accrued income" in the BANCOOP's financial statements.

B. Terms of the Agreement

The agreement was signed on December 21, 1983 by BANCOOP, INFOCOOP, MIDEPLAN and USAID/Costa Rica to provide 191,250,000 Colones from proceeds of PL480 Title I. The funds were disbursed by the Government of Costa Rica and invested in BANCOOP by INFOCOOP on February 22, 1984, as Special Contribution Certificates during a ten year period earning an annual interest rate of 6%.

Commitments of INFOCOOP:

a) Use the interest from the Special Contribution Certificates to finance activities of supervision, training, promotion and technical assistance to the cooperative system, excluding the credit lines.

b) Submit, to the satisfaction of MIDEPLAN, a plan of the activities to be financed within thirty days from the date of the agreement.

c) Present semester progress reports to MIDEPLAN within 15 days after the end of each semester.

d) Maintain independent accounting records related to the handling of the funds received.

Commitments of BANCOOP:

a) Issue the Special contribution Certificates.

b) Allot the funds received for the Special Contribution Certificates to a credit program to finance operations and projects of rural cooperatives with the following conditions:

- that the cooperatives be exclusively rural,
- that activities promote an increase in short-term production,
- that activities produce a saving or generate foreign exchange, and
- that activities promote an increase in productivity, an improvement in the commercialization channels, a better utilization of natural resources, and a better democratization of the economy.

c) Finance projects of the federated subsector saving and credit cooperative using up to 20% of the provided funds under the same conditions and to be applied as a counterpart for the project COLAC/FEDECREDITO.

d) Charge interest rates equal to the highest rates established by the Central Bank of Costa Rica for similar activities.

e) Recognize a 6% interest rate as a minimum on the Special Contribution Certificates.

f) Allot the loan recoveries to finance activities and projects related to the agreement.

g) Submit quarterly reports to MIDEPLAN on the implementation of the agreement.

h) Include within its bylaws, INFOCOOP's right to hold one representative on the BANCOOP's Administrative Council and to be represented in the Surveillance Committee, during the validity of the Special Contribution Certificates.

i) Maintain independent accounting records related to the implementation of the program.

j) Capitalize all the accrued earnings generated by the agreement until its redemption and in no case let them be distributed.

BANCOOP has the right to repay the Special Contribution Certificates from the tenth year on, counted from the beginning of the disbursements. When this right is applied, the BANCOOP will recognize 3% of annual interest on the balance of the certificates, from the period in which the payments begin.

The resources from the redemption of these certificates will be delivered to INFOCOOP as equity to strenghten its promotion programs.

The terms of the agreement cannot be modified without prior written authorization of MIDEPLAN, USAID/Costa Rica and the General Comptroller of Costa Rica, whatever divergency in the interpretation or implementation of the agrement will be resolved by the General Comptroller of the Republic.

C. Organization

The Bank was set up as a corporatión in January 1982, in accordance with the laws of Costa Rica and the dispositions of the Organic Law of the National Banking System. As a result of Law 6894 of September 22, 1983 that allowed the creation of private cooperative banks, in November 1983 the stockholders of the Banco Costarricense de la Cooperacion, S. A. represented by the associated cooperatives, approved the constitution and the transfer of all the assets and liabilities to the Banco Cooperativo Costarricense, R. L. (BANCOOP). This action was approved in January 1984, by the General Banking Auditor of Costa Rica.

D. Monetary Unit

The project's financial information is reported in Colones, the monetary unit of the Republic of Costa Rica, represented by the symbol C in the financial information. Transactions in foreign currencies are restricted and controlled by the Central Bank of Costa Rica. As of September 30, 1985 the Central Bank maintained the following exchange rates: a) C20.00:US$1.00 for some Government transactions, and b) C52.45:US$1.00 to liquidate active foreign transactions and liabilities authorized by the Central Bank.

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CREDIT PROGRAM FOR RURAL COOPERATIVES

REPORT ON INTERNAL ACCOUNTING CONTROL

AUDITOR'S OPINION

We have examined the financial information of the Credit Program for Rural Cooperatives among the Costa Rican Cooperative Bank (Banco Cooperativo Costarricense, R. L., BANCOOP), National Institute of Cooperative Promotion (Instituto Nacional de Fomento Cooperativo, INFOCOOP), the Ministry of National Planning and Economic Policy (Ministerio de Planificación Nacional y Política Económica, MIDEPLAN), and the U. S. Agency for International Development in Costa Rica (USAID/Costa Rica). Our examination covered the period from February 22, 1984 to September 30, 1985, and we have issued our report thereon dated October 21, 1986. As part of our examination, we made a study and evaluation of the BANCOOP's system of internal accounting control to the extent we considered necessary solely to determine the nature, timing and extent of our auditing procedures. Our study and evaluation was made in accordance with generally accepted auditing standards and the U. S. General Accounting Office "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision) and included the review of the following significant internal accounting controls: accounting records, income and disbursement and cash controls, investment in securities, loan receivable and financial information system. BANCOOP did not use a specific bank account for PL480 Title I funds, consecuently we could not perform an appropriate study and evaluation of this particular area, including bank account reconciliations.

The management of the Costa Rican Cooperative Bank (BANCOOP) is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable but, not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected. Also projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with the procedures may deteriorate.

Our study and evaluation made for the limited purposes as described in the first paragraph would not necessarily disclose all material weaknesses in the system. Accordingly we do not express an opinion on the system of internal accounting control of BANCOOP taken as a whole. However our study and evaluation disclosed the conditions described as findings 1 to 15 that we believe result in more than a relatively low risk that errors or irregularities in amounts that would be material in relation to the project's financial information may occur and not be detected within a timely period. These conditions were considered in determining the nature, timing and extent of the audit tests to be applied in our examination of the project's financial information which was not affected.

This report is intended solely for the use of BANCOOP, MIDEPLAN and the U. S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the AID Regional Inspector General, is a matter of public record.

Touche Ross & Co

October 21, 1986
San José, Costa Rica

COSTA RICAN COOPERATIVE BANK (BANCOOP)

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CREDIT PROGRAM FOR RURAL COOPERATIVES

REPORT ON THE INTERNAL ACCOUNTING CONTROL

FINDINGS

1. Lack of Controls on Loan Collateral Guaranties

Condition:

The accounting system did not include a real control of collateral guaranties on loans granted; the only control is maintained through subsidiary records not integrated with the accounting records and not reconciled with collateral guaranties on hand nor with the credit controls. Some collateral guaranties on paid loans were still in BANCOOP's vault and, in one case, the collateral guaranties on an oustanding loan were not found either physically or in the control book.

Criterion:

The legal documents regarding guaranties should be controlled through the accounting records and periodically reconciled with physical counts of the guaranties on hand.

Cause:

There was a lack of attention to this specific control.

Effect:

The possibility exists that the documents for guaranties could be lost or misplaced without being detected in a timely manner.

Recommendation:

BANCOOP should design a control system for the collaterals as part of the accounting system through memoranda accounts, classifying them by credit lines and by type of collateral, and organize the physical file in the same way. Additionaly, BANCOOP's internal auditing annual plan should include the physical verification of the collaterals against records and outstanding loans.

2. Interest on Late Payments was not Charged

Condition:

In distinct cases we found that, at the time of charging mature capital amortizations, interest on late payments was not charged. For example:

Payment order	Date of amortization	Days over-due	Moratory interest	Total to be charged	Total charged
0068	27-10-85	105	C 5,400	C 85,275.50	C 79,872.50
0078	27-10-85	105	6,506	102,744.45	96,238.45
0085	27-10-85	105	2,535	40,035.00	37,500.00

Criterion:

According to commercial practices, the Costa Rican Business Code and the Laws for Banks, in the case of overdue amortizations the bank can charge moratory interests.

Cause:

The handling and control of the loans on those dates were manual and due to the workload, in some cases, the interest on late payments were not included in the collections. At present this control is done by computer.

Effect:

The omission of collecting interest on late payments represents a loss of resources, and lack of control of the loans receivable.

Recommendation:

BANCOOP should review the actual procedure to determine if the interest on late payments has been collected without exception.

3. Documentation of the Rescheduled Loans was not Renewed

Condition:

During our review we observed that for the following rescheduled loans the bills of exchange were not renewed.

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REPORT ON THE INTERNAL ACCOUNTING CONTROL

FINDINGS

Loan No.	Cooperative	Amount	Due dates Original	Due dates Rescheduled	Original document
PL0274	Coopemonte-cillos, R.L.	C6,000,000	25-11-85	23-11-86	L.C. 274
PL0351	Coopetierra-blanca, R.L.	1,000,000	21-10-85	21-08-86	L.C. 351
PL0319	Coopesancar-los, .L.	1,000,000	15-09-85	15-09-86	L.C. 319

Criterion:

Any rescheduled loan should be guarantied by new bills of exchange appropriately signed which legally guarantee individual payments.

Cause:

These documents are issued only on new loans due to costs involved and because the bills of exhange terminate in four years.

Effect:

The lack of new documents for rescheduled loans reduces the legal recourse to recover the loans from the borrowers.

Recommendation:

BANCOOP should set up a formal policy to document new and rescheduled loans.

4. Lack of Information on Loan Control

Condition:

The loans were codified indicating their source, but they were not classified into control accounts by project. There was no utility program in the computer system to determine the balance of the loans by project and source.

Criterion:

The balance and analysis of the loans by project and source should be provided as part of the accounting system, with no additional effort, so that the information can be used as an administrative tool in a systematic way.

Cause:

The portfolio is controlled and analyzed as a whole and it is only separated by project, destiny and other classifications due to requirements of the Central Bank.

Effect:

The disposition of the portfolio by source and project needs to be known at any given moment; consecuéntly, additional efforts are usually incurred to prepare it.

Recommendation:

BANCOOP should implement a system which enables the classification of the portfolio by project and source.

5. Lack of References on the Loan Formalization Orders

Condition:

The credit formalization orders did not include a reference to: a) the Credit Committee minutes in which the loan was authorized; and b) the sequential number of the loan formalization.

Criterion:

The loan formalization orders should be referenced with the Credit Committee minutes and the sequential number of the correspondent loan formalization.

Cause:

This procedure was not in practice during 1985. BANCOOP started to implement it in 1986.

Effect:

The lack of reference to the Credit Committee minutes and the number of formalization could cause delays or legal problems in a given moment.

Recommendation:

BANCOOP should review and reference all loan formalization orders which are not already referenced and maintain the system on a current basis.

6. No loan Formalization Orders Attached to the Copy of the Check.

Condition:

Before 1986, the loan formalization orders were not attached to the voucher checks for loan disbursements and some checks were not found at all.

Criterion:

Loan formalization orders shall be attached to the corresponding check as evidence of the authorization of the loan as well as the name of the recipient, amount and other pertinent data for any later clarification or review.

Cause:

The weaknesses were detected and corrected by 1986.

Effect:

The lack of the loan formalization orders attached to copies of the checks lessens the internal control over loan disbursement and unathorized disbursements or incorrect amounts could be registered without detection.

Recommendation:

BANCOOP should find the credit formalization orders previous to 1986 and file them as appropriate, and mantain the procedure updated in the future.

7. Lack of Evidence of Authorization for Rescheduling of Loans.

Condition:

For some loans, there were no authorizations of rescheduling, for example:

Loan No.	Borrower	Original due date	Rescheduled due date	Balance
PL0053	PANASA, S. A.	12-05-84	12-09-86	C4,000,000.00
PL0319	Coopesancarlos, R. L.	15-09-85	15-09-86	1,000,000.00
PL0348	Gte Silvania, S. A.	16-10-85	28-10-86	1,609,890.80
PL0351	Coopetierrablanca, R.L.	21-10-85	21-08-86	1,000,000.00

Criterion:

Good internal controls require the rescheduled loans should clearly show the renewal authorization through a formal memorandum referenced to the correspondent minutes. These minutes should be signed by the appropriate officer of BANCOOP.

Cause:

The lack of evidence may be caused by unauthorized rescheduling of loans, lack of the appropriate annotation in the minutes, or deficiencies in the file procedures.

Effect:

The lack of evidence of authorization in some rescheduled loans, increases the possibility that risky loans can be included in the financial statements without a clear explanation and/or without the appropriate allowance for bad debts.

Recommendation:

BANCOOP should establish the necessary procedures to include the evidence of authorization in all rescheduled loans and include, within the general internal auditing plan, compliance procedures to verify these attributes for the authorized deferments in the year.

8. Lack of Preparer and Reviewer Signatures on Delinquency and other Reports.

Condition:

The delinquency reports were not signed by the preparer and reviewer, and the service statement of loans report was not signed by the accountant and the deputy manager.

Criterion:

All reports used by the management should be signed by preparers and reviewers to improve confidence in them and to assign responsibilities, if needed.

Cause:

Signing these reports is a normal procedure in BANCOOP; however it is not always followed.

Effect:

The lack of evidence of review and authorization could result in possible errors in the reports, which could lead to bad management decisions.

Recommendation:

BANCOOP should draw up formal instructions so that every document is signed at the time of its preparation, review and/or approval.

9. Copies of Checks without Recipient Signatures.

Condition:

We observed that checks related to loan disbursements Nos. 9251 of February, 1986; 946 of March 1986 and 10946 of July, 1986 were not signed by the recipients.

Criterion:

All checks should be signed by the recipient as evidence that funds were received. This procedure reduces the possibility of errors in loan recording.

Cause:

In some cases, the checks are deposited directly in the bank accounts of the recipients, giving them the deposit slip without leaving evidence for BANCOOP.

Effect:

The lack of signature of the recipient on these checks increases the possibility of errors in accounting recording procedures, could cause recording of loans not disbursed and could allow the possible diversion of funds.

Recommendation:

BANCOOP should obtain the recipient's signature on the issued check, and/or a letter of authorization and copy of the deposit slip when deposited in bank accounts.

10. Lack of Evidence of the Reviewer's Signature on the Checks

Condition:

Checks No. 10946 of July, 1986 and No. 303695 of August, 1986 for 8,000,000 and 6,000,000 Colones respectively, were not signed when reviewed by the Accounting Department.

Criterion:

The signing of a check review by the accountant is a procedure necessary to define the responsibility of the reviewer and to prevent possible mistakes in check issuance.

Cause:

In accordance with BANCOOP's policies, the review of checks was the responsibility of each department, and the Accounting Department reviewed only those checks sent to them for review.

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Effect:

The omission of check review by the Accounting Department reduces the possibility of early detection of errors in the check issuance procedure.

Recommendation:

BANCOOP should establish a formal procedure of review prior to signing and delivering the check.

11. Lack of Real Control on the Sequential Numbers of Checks

Condition:

The files to control the sequential number of the issued checks were incomplete. We could not find the following checks:

Account No.	Bank	Missing checks	Month
56635-6	Anglo Costarricense	290856/ 0857/0863	September 85
93817-3	De Costa Rica	900262/ 0266	September 85
84072-8	Nacional	4899	December 84

Also, the copies of the voided checks were not filed in the sequential number control.

Criterion:

A strict control of the checks' sequential number should be carried out to improve check recording and to detect possible omissions in check issuance procedures.

Cause:

There was not a strict control on checks' sequential numbers nor were the control copies of voided checks filed in this file.

Effect:

The missing checks could represent the possibility of unauthorized issuance of checks or checks unrecorded in the accounting records.

Recommendation:

BANCOOP should determine where the missing checks are and file all the checks in the sequential number control, including the correspondent copies of all voided checks.

12. Inconsistency in the Sequential Control of the Cash Receipts

Condition:

The receipts of credit amortization as well as interest collections had not been filed sequentially because those corresponding to 1984 and January to March of 1985 were not found. In addition, since May 1986 the receipts were prepared by the computer with only one copy, which is filed in the loan file, as a sequential did not exist.

Criterion:

As a measure of internal control, it is important to maintain consecutive files of the collection receipts to prevent or to detect potential errors from a lack of entering income or from unreceived income as well as to facilitate later consultations.

Cause:

The new system did not include triplicate receipt forms to avoid excessive document volume. The sequential number file was replaced by a computer list, however a new sequential file was recently introduced.

Effect:

The total or partial lack of these control procedures increased the possibility of income recording error and diversion of cash.

Recommendation:

BANCOOP should permanently maintain an appropriate control of receipts in sequential order and assure that for the period there was no control the transactions are completed.

13. Issue of Expiration Notices

Condition:

Since June, 1986, the loan expiration notices are prepared by the computer only in original, which is given to the client without a copy for the loan file.

Criterion:

In accordance with the loan filing system and the follow up of the loan, evidence should exist of client notification for future clarification.

Cause:

The new computer stationery for loan expiration notices did not include copies.

Effect:

Not having copies of the loan expiration notices reduces the evidence of collection efforts and the possibility of prevention or detection of errors, principally in late collections.

Recommendation:

BANCOOP should make a copy of the loan expiration notices to include in the loan file and assign somebody independent of the credit department to verify that all the notices were issued and sent, and to investigate those returned, if any.

14. Deficiency in Loan Files

Condition:

We observed that the loan files did not always have the basic information required by the BANCOOP's filing system. We observed that in many cases the following documents were not found: Administrative Council autorization in the minutes, summary of credit analysis, formalization orders, letters confirming the cooperative's Administrative Council authorization to take out the loan, and the borrower's financial statements.

Criterion:

The filing system is a means of accessibility to the loan information, therefore it should be handled in accordance with a system, and its compliance should be verified.

Cause:

The principal deficiencies began at the opening of BANCOOP, which correspond to the period audited. Currently, it is being controlled adequately.

Effect:

There is no sufficient evidence of authorization and formalization of loans, and additional investigation and efforts are needed in case of legal claims or simple consultation.

Recommendation:

BANCOOP should review and complete all the files and include, within the internal auditing general plan, procedures for ensuring compliance with the requirements of the filing system.

15. Unauthorized Deductions from Project Income

Condition:

During 1984 BANCOOP deducted approximately 304,000 Colones from income generated by PL 480 Title I funds. This deducted amount was part of income taxes paid in past periods, when BANCOOP was a corporation.

Criterion:

This kind of deduction was not authorized by the agreement, which required that net income generated by PL 480 Title I funds

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operations was to be capitalized as a non-distributable account. Any deduction not authorized contravenes this point.

Cause:

This deduction was made in error by the Accounting Department.

Effect:

The amount of the non-distributable accrued earnings as of September 30, 1985 was reduced by approximately 304,000 Colones.

Recommendation:

We recommend that BANCOOP increase the non-distributable accrued earnings account by C304,053, transfering it from current year income. This adjustment represents a "Prior period adjustment" as descried by accounting principles, however, due to its low value, it is acceptable to charge it to current income. However, a clear explanation and proper authorization are required.

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CREDIT PROGRAM FOR RURAL COOPERATIVES

REPORT ON COMPLIANCE WITH LAWS, REGULATIONS AND AGREEMENT TERMS

AUDITOR'S OPINION

We have made a study and evaluation to determine whether the Costa Rican Cooperative Bank (Banco Cooperativo Costarricense, R. L., BANCOOP) had complied with applicable laws, regulations and terms of its agreement signed on December 21, 1983 with the National Institute of Cooperative Promotion (Instituto Nacional de Fomento Cooperativo, INFOCOOP), the Ministry of National Planning and Economic Policy (Ministerio de Planificación Nacional y Política Económica, MIDEPLAN), and the U. S. Agency for International Development in Costa Rica (USAID/Costa Rica). The agreement provided 191,250.000 Costa Rican Colones to capitalize BANCOOP and finance rural cooperative activities. Our examination covered the period from February 22, 1984 through September 30, 1985 and was carried out to establish if BANCOOP had complied with the applicable laws, regulations and the agreement terms with respect to the control and utilization of the funds and other conditions described in the agreement. Our examination was made in accordance with generally accepted auditing standards and the U. S. General Accounting Office, "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" (1981 Revision).

The agreement among BANCOOP, INFOCOOP, MIDEPLAN and USAID/Costa Rica was not followed as explained in findings No. 1 through 4 as follows: a) Some loans were granted with PL 480 Title I funds to the non-cooperative sector for approximately 70,000,000 Colones (the balance as of September 30, 1985 was approximately C20,000,000), in contravention of Clause 4b; b) no specific and independent accounting records had been implemented by BANCOOP to record the project's operations, as required by Clause 4i; c) financial reports were not presented to MIDEPLAN and USAID/Costa Rica on a timely basis as required by Clause 4g; and d) changes were made to the agreement terms without evidence of the concurrence of all involved parties as required by Clause 7.

In our opinion, and according to the nature and extent of our evaluation as explained in the first paragraph; except for some loans granted to non-cooperative sector; the lack of independent accounting records for the project's operations; delays in the presentation of project's financial information; and changes made to the agreement terms as mentioned in the precedent paragraph; tested items were in compliance with agreement terms and BANCOOP had complied with applicable laws and regulations. Additionally, nothing came to our attention that caused us to believe that untested items were not in compliance with applicable laws, regulations and agreement terms.

Additionally, our examination revealed some weaknesses in the agreement commented on in the following pages as finding No. 5 that in our opinion, did not allow full achievement of the project's goals in compliance with the objectives of PL480 Title I.

This report is intended solely for the use of BANCOOP, MIDEPLAN and the U. S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the AID Regional Inspector General, is a matter of public record.

Touche Ross & Coy.

October 21, 1986
San José, Costa Rica

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1. Financing Non-Cooperative Sector

Condition:

BANCOOP had used PL480 Title I funds to finance operations of enterprises which are not cooperatives. The loans granted during the period amounted to approximately 70,000,000 Costa Rican Colones with a balance of approximately 20,000,000 Colones at September 30, 1985.

Criterion:

In accordance with Clause 4b of the agreement among BANCOOP, INFOCOOP, MIDEPLAN and USAID/Costa Rica, the PL480 Title I funds should be destined only to finance rural cooperatives.

Cause:

BANCOOP loaned part of PL480 Title I funds to the non-cooperative sector in the absence of sufficient cooperatives with good credit status and because it was more convenient to loan the money to private sector on a short-term basis than to have it idle in cash or low profit investments.

Effect:

Because its principal objective was to support the cooperative system to promote the democratization of the economy, through soft credit lines, the agreement is very specific about the destiny of PL480 Title I funds. To divert these funds for other purposes limits the attainment of the project goals.

Recommendation:

BANCOOP should comply strictly with the underwritten agreement by not loaning to the non-cooperative sector and/or obtaining waivers if needed.

2. Lack of Independent Accounting Records

Condition:

An independent and specific accounting system had not been implemented for the project's operations as required by Clause 4i.

Some subsidiary records and some isolated general ledger accounts had been used for these purposes.

Criterion:

The accounting system must guarantee the clarity and adequacy of transactions and the reliability and fairness of the information system especially in this project, because the amounts and specific goals are so important for BANCOOP and the Government of Costa Rica.

Cause:

The agreement did not establish the specific accounting records required, and BANCOOP staff considered that the actual system was adequate and easy to carry out.

Effect:

PL480 Title I funds and income and expenses related to the project were mixed with those other funds and transactions connected with the BANCOOP's normal operations. As result, considerable efforts were required to compile the project's financial information, when needed.

Recommendation:

BANCOOP should design and implement independent accounting records to control project operations.

3. Non-Compliance with the Presentation of Reports

Condition:

The presentation of quarterly reports to MIDEPLAN had been irregular and as of September 30, 1985, date of our review, the last report had been presented on May 9, 1985.

The reports were presented as follows:

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Report No.	As of date	Submission date
1	May. 31, 1984	Jul. 20, 1984
2	Aug. 31, 1984	Sep. 21, 1984
3	Nov. 30, 1984	Dec. 13, 1984
4	Feb. 28, 1985	May. 9, 1985

The next report was presented on February 11, 1986 and included project information up to December 31, 1985.

Criterion:

Quarterly reports shall be submitted as agreed because MIDEPLAN is also obligated to report in the same manner to the Costa Rican Government and USAID/Costa Rica. The project will conclude at the completion of the agreed 10 years, consequently loans repaid by cooperatives consitute part of PL 480 Title I funds, and should be managed in the same way.

Cause:

BANCOOP officers explained that the report presented on May 9, 1985, included almost the complete project (approximately 90% of funds), so they deemed it more convenient to present the next reports each semester.

Effect:

The omission of quartely reports did not allow MIDEPLAN, as the supervising institution, to observe whether the project is being carried out adequately, and it constitutes a violation of the agreement.

Recommendation:

BANCOOP should present the quarterly reports as required by the agreement, any modification deemed necessary should have written authorization prior to implementing it.

4. Change of Agreement Terms

Condition:

The agreement terms related to the use of the proceeds by the

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National Institute for Cooperative Promotion (INFOCOOP) to finance its activities pertaining to supervision, training, promotion and advisory services to cooperatives, were changed by the Costa Rican Law Decree No. 6957 of February 23, 1984, and No. 7015 of November 29, 1985, The proceeds were transferred to Cooperative Training and Study Center (Centro de Estudio y Capacitación Cooperativa, CENECOOP) (62.5%), Cooperative Youth Program (Programa de Cooperativas Juveniles) (25%), and National Council of Cooperatives (Consejo Nacional de Cooperativas, CONACOOP) (12.5%), to be used for the same purposes. This change was made without evidence of concurrence by the other parties involved in the agreement.

Criterion:

Clause 7 of the agreement, established that any change cannot be made without the previous written authorization of MIDEPLAN, USAID/Costa Rica and the General Comptroller of Costa Rica, consequently, the agreement terms only should be changed with the concurrence of these parties.

Cause:

The Costa Rica Government decided to channel the proceeds to the specific institutions managing training and youth programs of cooperatives.

Effect:

INFOCOOP is now almost out of the project and considers itself without responsibility for the management of proceeds, consequently, no reports about the use of these funds were sent by either INFOCOOP or the other recipients to MIDEPLAN and USAID/Costa Rica.

Recommendation:

We recommend that INFOCOOP and BANCOOP discuss the changes to agreement terms with MIDEPLAN, USAID/Costa Rica and the General Comptroller of Costa Rica to find an acceptable solution to informal changes already made.

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5. Weaknesses in the Agreement Terms

Condition:

The agreement did not include all necessary conditions and did not establish the specific characteristics of the procedures to supervise and evaluate its execution. Among other, we observed the following conditions:

A. The way in which the capitalization of the earned interest will be calculated was not specified. During 1984 BANCOOP calculated separately the interest generated by PL480 Title I funds and by the other funds using the same criteria. However during 1985, it was estimated that the cost of processing loans to the cooperative sector was twice that of loans to the private sector, and the operation expenses were charged in proportion to the income previously calculated.

   Additionally there were no established procedures to recognize losses on uncollectible loans. The related allowances were calculated by BANCOOP on its whole portfolio, in compliance with the regulations of the Central Bank of Costa Rica and the project was charged in proportion to the income generated in the year. As of September 30, 1985 no loan had been cancelled as uncollectible.

B. It was established that independent accounting records should be maintained, but the requirements of the independent system were not defined, additionally a specific bank account was not required.

C. The agreement did not establish penalties in case of non-compliance.

Criterion:

The agreement should be drafted in a clear and well-defined manner, including all those clauses necessary for its adequate interpretation and execution as well as the penalty clauses in the case of non-compliance. The following matters should be considered:

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A. Provision for capitalization of the generated surplus should include the calculating procedure for defining which expenses should be considered as allocable, allowable and reasonable to be deducted, including an estimation for doubtful accounts.

B. The requirements of the independent accounting records system should be clearly defined and the use of an independent bank account should be clearly stated.

C. The agreement should include penalty clauses in case of non-compliance.

Cause:

There was no clear understanding of the responsibilities assumed by each party involved. BANCOOP considered this project to be like a grant to be used at its discretion.

Effect:

Due to the lack of clear explanation about some requirements and the lack of some others, it is not possible to adequately evaluate the execution and development of the project.

Recommendation:

USAID/Costa Rica should review future agreement to ensure they are clear considering all the possible situations which could arise, and clearly defining which actions to take.

6. Lack of Supervision by MIDEPLAN

Condition:

As commented in findings Nos. 1 to 3, BANCOOP did not comply with all applicable agreement terms and MIDEPLAN had not take corrective measures to comply with the agreement or to obtain the necessary waivers.

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Criterion:

MIDEPLAN was appointed as project coordinator and supervisor by the Government of Costa Rica. Consequently its primary responsibility consists in compliance with agreement terms as well as aiding in the attainment of the projected goals.

Cause:

According to the actual director of MIDEPLAN's implementation unit for PL480 Title I, this unit is new and did not have sufficient personnel to coordinate and supervise all the operations derived from this program, which included some governmental institutions.

Effect:

MIDEPLAN did not comply with its functions as agent of the Costa Rican Government to coordinate and supervise the PL480 Title I proceeds. If this coordination and supervision are not adequate, the project principal goals could not be successfully accomplished.

Recommendation:

MIDEPLAN should restructure its PL480 Title I implementing unit so that it can comply appropriately with its functions.

APPENDIX 1

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