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AUDIT OF USAID/DOMINICAN REPUBLIC'S
LOCAL CURRENCY
FINANCIAL OVERSIGHT
SYSTEM

Audit Report No. 1-517-88-18
April 28, 1988

AGENCY FOR INTERNATIONAL DEVELOPMENT

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April 28, 1988

MEMORANDUM

TO: USAID/Dominican Republic Director, Thomas Stukel

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

SUBJECT: Audit of USAID/Dominican Republic's Local Currency Financial Oversight System

The Office of the Regional Inspector General for Audit/Tegucigalpa has completed its audit of USAID/Dominican Republic's Local Currency Financial Oversight System. Five copies of the audit report are enclosed for your action.

The draft audit report was submitted to you for comment and your comments are attached to the report. The report contains five recommendations. Recommendations Nos. 3(a), and 4(b)(ii) are considered closed upon final report issuance, and require no further action. Recommendations Nos. 1(a), 4(b)(i), 4(c), 5(a), and 5(b) are considered resolved but cannot be closed until completion of planned or promised corrective actions. The rest of the recommendations remain unresolved at final report issuance. Please advise me within 30 days of any additional actions taken or planned to implement the open recommendations.

I appreciate the cooperation and courtesy extended to my staff during the audit.

EXECUTIVE SUMMARY

Approximately $260.3 million in local currency was generated from the Public Law 480 Title I and Economic Support Fund Agreements for 1984, 1985 and 1986. Economic Support Fund local currency proceeds were to be used to finance development activities that directly benefited the Dominican Republic's private sector while Public Law 480 Title I local currency proceeds were to be used to fund self-help measures and development activities that promoted growth in the agricultural sector and enhanced its self-sufficiency. They were administered by the Technical Secretariat of the Presidency.

The Office of the Regional Inspector General for Audit/Tegucigalpa made an economy and efficiency audit of USAID/Dominican Republic's local currency management systems established to oversee the utilization of these local currency funds. The primary objective of the audit was to determine if they were adequate to ensure that local currency proceeds were used for jointly agreed-upon activities.

The audit found that the Mission's Local Currency Financial Management System did not adequately ensure that local currency proceeds were received by implementing agencies and used to fund jointly programmed activities specified in pertinent agreements. Audit results indicated that the Mission needed more in-depth and participatory oversight for its local currency program to ensure that the host government's monitoring was effective and adequately safeguarded local currency resources.

During the audit the Mission initiated a series of management actions that were designed to correct problems revealed through audit as well as to improve the Mission's financial oversight of the local currency program. The Mission hired a Personal Services Contractor in August 1987 to oversee and evaluate the Secretariat's monitoring capability and to enhance the Mission's own coverage of the local currency program. Staffing increases were being considered for the Financial Analysis Branch and Capital Resources Development Office in order to provide better oversight and technical assistance to the program. The Mission was also considering providing the Technical Secretariat's Audit Office short-term technical training to assist it in expanding its coverage of the local currency program as well as to ensure that its auditors were well-versed in local governmental systems and generally accepted governmental auditing standards.

Specifically, the audit disclosed that: USAID/DR's financial oversight and tracking of local currency disbursements was not sufficient to adequately assure itself that local currency disbursements were ultimately received by implementing agencies in the amounts originally released for disbursement; the Mission's financial reviews of local currency projects were infrequent and not sufficiently in-depth; the local currency disbursement system was overly complex, time-consuming and

did not provide an adequate audit trail for tracking local currency disbursements to their end-use; local currency implementing agencies often commingled local currency proceeds with funds from their other operational accounts and projects; and the host country's financial monitoring of the local currency program was inadequate and, because of system deficiencies, reported problems areas often remained uncorrected.

Mission Order No. 11-4 issued on May 2, 1986 requires that the Controller's Office maintain adequate records for approved projects and for local currency funds released. Although the Controller's Office accurately recorded the funds released from the local currency bank accounts, no review was made to determine whether the implementing agencies had actually received the disbursements in the amounts approved for release by the Missions and the Technical Secretariat of the Presidency. This lack of financial oversight was reportedly caused by the Mission's policy of not tracking local currency end-use by executing agencies and a lack of sufficient Mission personnel for closer oversight. As a result, the Mission Controller's Office did not know if total local currency disbursements were received by implementing agencies and could not perform a complete reconciliation. The omission left the funds vulnerable because of the uneven quality of host country financial reviews.

The audit report recommended establishment by the Secretariat of a mechanism to confirm to both parties that local currency proceeds had been received by implementing agencies in the amounts released. The Mission agreed with recommendation 1(a) and requested revision of 1(b), which we have done. Recommendation 1(a) is resolved, 1(b) remains open at final report issuance.

Mission Order Number 11-4, issued on May 2, 1986, assigned the Mission Controller's Office responsibility for conducting financial reviews of selected local currency projects, coordinating other project audits as necessary, and reporting on the effectiveness of Technical Secretariat of the Presidency monitoring capability. Also supplemental guidance contained in recently revised A.I.D. Policy Determination Number 5 now requires A.I.D. to ensure that implementing agencies have sufficient management controls in place prior to the disbursement of local currency funds. Although over $150,000,000 in equivalent local currency had reportedly been released to implementing agencies as of September 30, 1987, the Mission's financial analysis branch had performed no in-depth financial reviews of local currency development projects or of the implementing agencies managing those projects since December 8, 1986. The financial reviews were not made due to the branch's inadequate staffing and the position taken by Controller officials that their role was strictly one of limited financial oversight. Unless the Mission's financial analysis branch conducts periodic reviews of selected local currency projects, it cannot accurately assess the quality of monitoring that is being conducted by the Secretariat. As a result, local currency resources become especialy vulnerable to mismanagement. During our financial review of local currency program recipients, we found instances in which implementing agency management controls were inadequate, local currency funding had been commingled or used for unauthorized purposes, and A.I.D.-approved funding may never have been received by the implementing agency. The report recommended that the Mission provide more frequent and in-depth audit coverage of the local currency program, and that the management controls of an implementing agency be thoroughly reviewed before local currency proceeds were disbursed to it for project purposes. The Mission generally disagreed with this finding and it accordingly remains open and unresolved upon final report issuance.

The Local Currency Memoranda of Understanding required that disbursements from the Government of the Dominican Republic's Central Bank to implementing agencies be accomplished within 10 days. A review of sampled disbursements from local currency bank account statements under Public Law 480 Agreements indicated that disbursements to implementing agencies were taking significantly longer than the required period; were sometimes not in the amounts authorized; and, as a result, often could not be traced through the disbursement system within a reasonable period of time, if at all. We attributed the cause of the delays and inaccuracies to the laborious and overly complicated design of the local currency disbursement system. As a result, not only were disbursements of project funds to implementing agencies delayed, thereby delaying progress of the projects, but, local currency proceeds were commingled with funds from other government general fund accounts and were untraceable. In addition, because accounting systems and internal controls were weak at the implementing agency level, as we found during our audit sample, adequate assurance could not be provided in such cases that the funds would be properly used. The report recommends simplification of the local currency disbursement system and suggests that local currency proceeds be disbursed directly from the Central Bank to the requesting implementing agency. The Mission generally agreed with the recommendation and initiated a dialogue to discuss improvement to the local currency disbursement system. Recommendation 3(a) is considered closed upon final report issuance.

The final two findings discuss the establishment of separate bank accounts for local currency generations and the need for improvements in the implementing agency's audit reporting and follow-up systems. The Mission generally agreed with those two findings and has initiated actions to correct the problems noted during the audit. Recommendation 4(b)(ii) is considered closed upon final report issuance.

USAID/Dominican Republic requested that the following statement be inserted into the Executive Summary Section of this report:

> The IG Report on the local currrency program reflects a fundamental misconception regarding the nature of responsibilities associated with executing a host country-financed local currency program.

Such programs are financed by the Host Country with its own resources. These resources are not U.S. appropriated funds; they are subject to a negotiated agreement between A.I.D. and the host country in their programming and disbursement and to the same laws, procedures, and mechanisms employed to carry out the government's regular programs. The financial oversight and management posture adopted by the Mission was exactly that prescribed at the same time by the original Policy Determination No. 5. While it is true that Agency guidance was significantly revised in October of 1987, the standards set forth in that revision should not be applied retroactively to activities which took place in prior years. A significant part of the guidance applicable to the period covered by the audit (that is the original PD-5) was the understanding that host country-owned local currencies, did, in fact, belong to the host country and were, to the extent possible, to be managed by them. As such these currencies were primarily the responsibility of the host country and subject to their own laws, regulations and even their own disbursement procedures. These are not US-owned or dollar appropriated funds. Agency policy during this period did not provide hands-on management of host country-owned local currencies which were generated under the 1984, 1985 and 1986 agreements. The record clearly shows, however, that USAID/DR carried out a series of measures to help the GODR improve its abilities to manage its own local currency resources. Weaknesses in host government institutions and controls over local currency resoures requires us to help host governments improve their own management capabilities. In no way, however, does weakness in host government institutions management of their own resources imply that the Mission did not perform its oversight functions in keeping with Agency policy in effect at the time.

In response, we would note that since the beginning of USAID/Dominican Republic's most recent local currency program in 1982, the Mission has chosen to be highly involved in the programming of host country owned local currency. This policy of active participation in the programming of local currency resources carried with it a responsibility for the Mission to adequately oversee the local currency program to ensure that proceeds were received by end-users and utilized for jointly agreed upon purposes.

In A.I.D./Washington's Policy Determination Number 5, Programming Public Law 480 Local Currency Generations issued on February 22, 1983, the relationship between a USAID's participation in the programming of local currency resources and its corresponding oversight responsibility is discussed. "When A.I.D. plays a more active role" in the "detailed programming" of local currency and concurs on its disbursement, the USAIDs also have a responsibility for monitoring and evaluating the implementation of the local currency resources. Since USAID/Dominican Republic actively participated in the detailed programming of the local currency and also approved each disbursement of local currency to recipients, in our opinion, USAID/Dominican Republic assumed an obligation to periodically review whether the local currencies were being properly accounted for and used appropriately by intended recipients.

Finally, even though these local currency resources are not U.S. appropriated funds, this is a USAID sponsored program whose relative success or failure is publicly associated with the U.S. Government and its development efforts in the Dominican Republic. We consequently believe that the ultimate ownership of the local currency resources did not diminish the Mission's important responsibility to effectively oversee the program.

Office of the Inspector General

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PART I - INTRODUCTION

A. Background

In 1983 A.I.D. published Policy Determination Number 5 (PD-5) which discussed different ways that USAID/Missions could participate in managing local currency (L/C) programs in their countries. PD-5 stated that A.I.D. involvement could range between two alternatives: recipient governments could assume primary responsibility for allocating their own budget resources, or A.I.D. could play a more active role in resource allocation decisions. Examples of active participation by A.I.D. Missions included requiring Mission approval on proposed host country local currency projects, requiring Mission concurrence for release of disbursements from local currency accounts, establishment of special local currency bank accounts and requiring periodic reporting on the status of financial accounts and individual projects.

For management of the local currency program in the Dominican Republic, the USAID Dominican Republic (USAID/DR) Mission adopted a management posture of limited involvement and oversight over the end-use of local currency resources, even though it participated more actively in other aspects of the local currency program. For example, the Mission required its concurrence in proposed host country development projects, the establishment of a separate bank account for deposits of L/C proceeds, and its approval for release of L/C project disbursements. Memoranda of Understanding governing the use of L/C and USAID/DR Mission Order II-4 gave overall monitoring responsibility for the L/C Program to the Government of the Dominican Republic's (GODR) donor coordinating unit, the Technical Secretariat of the Presidency (Secretaria Tecnica de la Presidencia, STP). The local currency oversight function was assigned to USAID/DR's Capital Resources Development (CRD) Office. In addition, each Mission technical office was to provide expertise in its particular functional area in order to assist STP in monitoring the implementation of particular projects of the local currency program. For example, the Agricultural Office would assist in the implementation of local currency agriculture projects and the Controller's Office would assist in the financial control and review of the program.

In May 1986 USAID/DR organized a Local Currency Program Team to program and oversee the utilization of approximately $260.3 million in L/C generated from the PL 480 Title I 1984, 1985 and 1986 agreements and the Economic Support Fund (ESF) 1985 and 1986 agreements. Local Currency proceeds generated from the PL 480 Title I Program and Economic Support Fund Cash Transfers were often segregated into two budget categories for funding the same project, and the local currency proceeds generated from the two programs were often treated similarly for financial control purposes.

USAID/DR's local currency agreements specified that ESF local currency proceeds were to be used to finance development activities that directly benefited the Dominican Republic's private sector while PL 480 Title I local currency proceeds were to be used to fund self-help measures and development activities that promoted growth in the agricultural sector and enhanced its self-sufficiency.

In May 1986 USAID/DR hired a Personal Services Contractor (PSC) to work as the Mission L/C Program Coordinator. The PSC was responsible for evaluating the overall monitoring capability of the STP, overseeing the programming of approximately $314,000,000 in U.S. equivalent local currency generations for fiscal years 1982 through 1986, and coordinating the implementation of over 140 local currency projects underway at widely scattered locations in the Dominican Republic.

B. Audit Objectives and Scope

The Office of the Regional Inspector General for Audit/Tegucigalpa made an economy and efficiency audit of USAID/Dominican Republic's L/C systems and procedures established to oversee the utilization of local currency funds generated from the PL 480 Title I (1984, 1985, 1986) and Economic Support Fund (1985, 1986) cash transfer agreements. The primary objective of the audit was to determine if they were adequate to ensure that L/C proceeds were used for jointly agreed-upon activities specified in the applicable local currency agreements.

To accomplish this objective, audit procedures included interviews with responsible Mission and host country officials, a review of applicable agreements and memoranda of understanding, analyses of USAID/DR and host country implementing agency books, records, and bank statements, and field visits to selected fund recipients and local currency project site locations. The audit covered Economic Support Fund and PL 480 Title I Agreements that generated local currency valued at approximately $260.3 million. Of that amount, we reviewed approximately $132,000,000 in local currency funding disbursed to implementing agencies. Since A.I.D. was not responsible for overseeing and accounting for host-country PL 480 Title I commodity sales to domestic suppliers, the audit team did not evaluate whether total sales revenue realized from the sales of the commodities was properly accounted for and deposited in L/C bank accounts. We reviewed and evaluated the internal controls of implementing agencies visited during the audit as they pertained to the use of A.I.D.-"generated" local currencies. The audit was conducted during the period June 1987 to November 1987 and was made in accordance with generally accepted government auditing standards.

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PART II - RESULTS OF AUDIT

The audit found that USAID/DR's Local Currency Financial Management System did not adequately ensure that local currency proceeds were received by implementing agencies and used to fund jointly programmed activities specified in 1984, 1985 and 1986 pertinent agreements. Audit results indicated that the Mission needed more in-depth and participatory oversight for its local currency (L/C) program to ensure that the host government's monitoring was effective and that it adequately safeguarded local currency resources.

During the audit USAID/DR initiated a series of management actions that were designed to correct problems revealed through audit as well as to improve the Mission's financial oversight of the local currency program. The Mission hired a Personal Services Contractor (PSC) in August 1987 to oversee and evaluate STP's monitoring capability and to enhance the Mission's own coverage of the local currency program. Staffing increases were being considered for the Financial Analysis Branch and Capital Resources Development (CRD) Office in order to provide better oversight and technical assistance to the program. The Mission was also considering providing the STP Audit Office short-term technical training to assist it in expanding its coverage of the local currency program as well as to ensure that STP auditors were well-versed in local governmental systems and generally accepted governmental auditing standards.

Specifically, the audit disclosed that: a) USAID/DR's financial oversight and tracking of local currency disbursements was not sufficient to adequately assure itself that local currency disbursements were ultimately received by implementing agencies in the amounts originally released for disbursement; b) USAID/DR financial reviews of local currency projects were infrequent and not sufficiently in-depth; c) the local currency disbursement system was overly complex, time-consuming and did not provide an adequate audit trail for tracking local currency disbursements to their end-use; d) local currency implementing agencies often commingled local currency proceeds with funds from their other operational accounts and projects; and e) the host country's financial monitoring of the local currency program was inadequate and, because of system deficiencies, reported problems areas often remained uncorrected.

The audit report recommended establishment by the Secretariat of a mechanism to confirm to both parties that local currency proceeds had been received by implementing agencies in the amounts released. The report also recommended that the Mission provide more frequent and in-depth audit coverage of the local currency program, and that the management controls of an implementing agency be thoroughly reviewed before local currency proceeds are disbursed to it for project purposes. Recommendation Number Three recommends simplification of the local currency disbursement system and suggests that local currency proceeds be disbursed directly from the Central Bank to the requesting implementing agency. A further recommendation requests Mission officials to obtain substantive proof that implementing agencies have established separate bank accounts prior to the Mission's approval for release of local currency project funds to an implementing agency, and that the GODR replenish the special local currency accounts with any local currency proceeds that were used for unauthorized purposes. Finally, the report recommends that STP formalize its audit process and establish an adequate audit reporting and recommendation follow-up system to ensure that audit reports are distributed to all interested parties and that needed corrective actions are effectively taken.

A. Findings and Recommendations

1. USAID/Dominican Republic's Financial Oversight Role Needs to Be Expanded

USAID/DR Mission Order No. 11-4 issued on May 2, 1986 requires that the USAID/DR Controller's Office maintain adequate records for approved projects and for local currency funds released. Although the Controller's Office accurately recorded the funds released from the local currency bank accounts, no controller review was made to determine whether the implementing agencies had actually received the disbursements in the amounts approved for release by USAID/DR and the Technical Secretariat of the Presidency (STP). This lack of financial oversight was reportedly caused by USAID/DR's policy of not tracking local currency end-use by executing agencies and a lack of sufficient Mission personnel for closer oversight. As a result, USAID/DR Controller's Office did not know if total local currency disbursements were received by implementing agencies and could not perform a complete reconciliation. This omission left the funds vulnerable because of the lack of coverage and uneven quality of host country financial reviews.

Recommendation No. 1

We recommend that USAID/Dominican Republic:

a. oversee the establishment of a confirmation procedure that allows the Technical Secretariat of the Presidency to confirm that implementing agencies have promptly deposited in the local currency accounts those local currency proceeds originally authorized for disbursement; and

b. require the Controller's Office to oversee and periodically test the Technical Secretariat of the Presidency's confirmation procedure to ensure that it is adequate.

Discussion

USAID/DR Mission Order Number 11-4, issued May 2, 1986, assigns the USAID/DR Controller's Office responsibility for maintaining adequate records of approved local currency (L/C) projects and the local currency funds released to accomplish those projects. In addition, on October 24, 1986 the Mission Director tasked the Mission's Capital Resources Development Office (CRD) with the responsibility of establishing a data base capable of producing reports that would show the financial status of L/C projects, to include not only the amounts programmed, approved, and released; but also the amount of L/C received by the executing agency and expenditures made by implementing agencies for each project. The memorandum tasks the Controller's Office with maintaining accounting records adequate to monitor L/C generations and deposits as well as to allow both offices to reconcile L/C financial reports with Controller Office records. Discussions with the Mission accountants in charge of tracking the local currency generations indicated that they only reconciled a portion of the system, that is, from the time the funds were deposited in local currency bank accounts at the Central Bank to their subsequent release from those accounts. They did not trace or reconcile local currency disbursements after the funds were released from the Central Bank. They stated that they did not review nor were they notified whether the local currency proceeds were actually received by the implementing agencies in the amounts disbursed.

Mission financial personnel responsible for reconciling the L/C bank accounts stated that, due to limited Mission resources, USAID/DR's policy was not to track the end-use of funds disbursed to implementing agencies. They added, however, that financial oversight over L/C funding could be made more effective if a mechanism were established, such as a bank deposit confirmation notice, that would notify the Controller's office that L/C proceeds had been received timely by implementing agencies in the amounts originally disbursed. If the disbursements were made to the implementing agency in partial amounts, the confirmation notice would alert STP and Controller's office that a portion of disbursed funding was outstanding.

We believe that such an internal control mechanism is needed for the local currency program. Nearly all Mission personnel involved with the local currency program believe that the responsible governmental entity is incapable of providing adequate financial review and audit coverage of the program, and evaluation and audit teams have found the L/C disbursement system to be overly complex and highly vulnerable. Our review confirmed these assessments (see Finding Three). Therefore, to ensure proper oversight it is necessary that the Controller's Office be notified as to the amounts of L/C received by the implementing agencies. Such notification could be accomplished relatively easily and inexpensively through the implementing agency's submission of a confirmation notice to STP and the Controller's Office recording how much L/C funding had been in fact received.

Management Comments

The Mission was in full agreement with Recommendation No. 1(a), however, requested that Recommendation No. 1(b) be revised to task the Technical Secretariat of the Presidency (STP) Office, rather than the Mission Controller's Office, with the responsibility of confirming L/C bank deposits made to implementing agencies. They added that designing such a procedure would be included as part of an overall technical assistance package pending award to Price Waterhouse and Company (PW) International. Mission management also asked that closure of Recommendation No. 1(b) be based on submitting evidence of the Price Waterhouse and Company contract award to RIG/A/T.

The Mission's general comments about Finding No. 1 centered on the draft audit report's interpretation of internal Mission delegations of responsibility for management of the local currency program. Management officials stated that the draft audit report's referenced criteria Mission Manual Order No. 11-4, was later superseded by an October 24, 1985 Mission Director memo that reassigned USAID/DR local currency reporting responsibilities from the Controller's Office to the Mission's CRD Office. This memo, according to Mission officials, "required CRD to establish a data base capable of producing reports on the financial status of projects including not only the amounts programmed, approved and released but also the L/C received by the executing agency and the expenditures the agency has made for each project." The Mission added that the transfer of reporting responsibility had taken place within the offices and that required reports were being prepared with the exception of the project expenditures report. The Mission went on to say that its original intention was to obtain adequate reports directly from the STP rather than to have CRD collect information directly from implementing agencies. But since STP has never been able to provide the Mission with expenditure data, USAID/DR has been unable to report on project expenditures or to carry out complete reconciliations. The Mission further stated that its decision to transfer financial reporting to CRD did not alter the fundamental fact that basic accounting and reconciliation responsibilities of L/C remained with the Government of the Dominican Republic. Mission management noted that its Controller's Office was only responsible for monitoring L/C generations and deposits to ensure that they were deposited in the special accounts, and that "there was no requirement or guidance from AID/W to reconcile implementing agencies receipts with disbursements from special accounts."

Office of the Inspector General Comments

We view the Mission's planned technical assistance package as a positive step in the overall process of improving financial control of the Dominican Republic's Local Currency Program. We agree that the STP is the optimal office for performing reconciliation of implementing agency L/C bank deposits, if indeed the unit can gain the capability to perform such tasks routinely. Our review indicated that as of November 1987, the STP did not have the mechanisms or organizational procedures in place to perform such reconciliations. Recommendation 1(a) is considered resolved but open, pending our subsequent review of PW's suggested procedure as well as a review of STP's latest reconciliation of end-user deposits utilizing the procedure. Recommendation 1(b) was revised to require Mission oversight of STP confirmation procedures to ensure that authorized funds are received by end-users and deposited in their bank accounts.

We disagree with the Mission's statement that the draft audit report did not accurately report USAID/DR local currency management delegations of authority. Mission management policy of the local currency program was continuously explained to audit team members as management along "technical and functional lines." Mission Manual Order No. 11-4 confirmed this management policy and was in effect during the audit. As

Mission Order No. 11-4 clearly explained, the financial oversight of the L/C program was part of the technical and functional responsibility of the Mission Controller's Office.

It is true that the Mission Director's memo of October 24, 1986 tasked the CRD Office with establishing a data base capable of drawing detailed financial data from the STP. But Mission management had been well-briefed by recent independent evaluation teams that the STP was far from having the institutional capability for providing such information. For example, the Rural Development Services Report, published in August 1986, made the assessment that 45 percent of the L/C Program's expenditures were not clearly documented and that STP was a poorly equipped unit that lacked sufficient independence. In our opinion, assigning the Capital Resources Development (CRD) Office the task of establishing an overall local currency project data base in no way relieved the Controller's Office of its responsibility to effectively oversee the financial administration of the program.

2. USAID/DR Controller Financial Reviews Need to Be Made More Frequently And in More Depth

USAID/DR Mission Order Number 11-4, issued on May 2, 1986, assigned the Mission Controller's Office responsibility for conducting financial reviews of selected local currency projects, coordinating other project audits as necessary, and reporting on the effectiveness of Technical Secretariat of the Presidency (STP) monitoring capability. Also supplemental guidance contained in recently revised A.I.D. Policy Determination Number 5 now requires A.I.D. to ensure that implementing agencies have sufficient management controls in place prior to the disbursement of local currency funds. Although over $150,000,000 in equivalent local currency had reportedly been released to implementing agencies as of September 30, 1987 under the PL 480 1984, 1985 and 1986 agreements and ESF 1985 and 1986 agreements, USAID/DR's financial analysis branch had performed no in-depth financial reviews of local currency development projects or of the implementing agencies managing those projects since December 8, 1986. The financial reviews were not made due to the branch's inadequate staffing and the position taken by Controller officials that their role was strictly one of limited financial oversight. Unless the Mission's financial analysis branch conducts periodic reviews of selected L/C projects, it cannot accurately assess the quality of monitoring that is being conducted by STP. As a result, local currency resources become especialy vulnerable to mismanagement. During our financial review of L/C program recipients, we found instances in which implementing agency management controls were inadequate, local currency funding had been commingled or used for unauthorized purposes, and A.I.D.-approved L/C funding may never have been received by the implementing agency.

Recommendation No. 2

We recommend that USAID/Dominican Republic:

a. ensure that its Financial Analysis Branch include in its fiscal year 1988 financial review schedule periodic in-depth audits of local currency implementing agencies, to be conducted by its own staff or contracted out Certified Public Accountant firms, so that the Mission can adequately assess the Secretariat's monitoring capabilities and performance;

b. condition future releases of local currency funding to implementing agencies based upon a review of Technical Secretariat of the Presidency certification that implementing agency recipients have sufficient management controls in place to properly account for and manage local currency funding; and

c. provide the Regional Inspector General for Audit/Tegucigalpa with evidence of the financial commitments made to accomplish recommendations a. and b. above.

Discussion

USAID/DR Mission Order Number 11-4, issued on May 2, 1986, assigned the Controller's Office the reponsiblity for "...undertaking financial reviews of selected projects financed with local currency and ... coordinat[ing] such audits as appropriate." (Prior to May 2, 1986, no Mission Order had been issued regarding management of the local currency program, and only general oversight was being provided by the Mission in functional areas with each technical office providing input and expertise.) Also, revised A.I.D. Policy Determination Number 5, as of October 27, 1987, now requires A.I.D. to ensure that implementing agencies have sufficient management controls in place prior to the disbursement of local currency funds.

Information gathered during the audit indicated that at least four of the six implementing agencies reviewed had financial management systems and internal controls that were inadequate to properly safeguard and account for A.I.D.-"generated" L/C. Complete bank account reconciliations were not made, L/C proceeds were commingled in general accounts and accounting personnel were sometimes not notified that disbursements had been made to their projects from the Central Bank local currency accounts. Audit staff examined the financial review coverage and degree of financial oversight that was exercised over the L/C program by the USAID/DR Financial Analysis Branch. It was found that the Mission's Financial Analysis Branch had not conducted any financial reviews of L/C recipients from December 9, 1986 to November 4, 1987, even though L/C implementing agencies had been authorized to receive over $150,000,000 in equivalent local currency generations under the ESF and PL 480 Title I Program as of September 30, 1987.

Financial reviews were not conducted partly due to inadequate staffing. The Mission's financial analyst position was vacant in January and February 1987, and a period of training was necessary to acquaint the financial analyst hired in March 1987 with the Mission's objectives and the L/C program in general.

The lack of frequent and in-depth financial reviews by the Financial Analysis Branch was also attributed to uncertainty in the minds of branch personnel about their financial oversight duties. Financial analysts assigned to the branch during 1987 stated that they saw their role as providing limited oversight to the STP financial monitoring unit. In-depth financial reviews and audits were to be performed by the STP auditing unit exclusively. However, the financial analyst branch also viewed the STP auditing unit as incapable of adequately performing its monitoring task. The branch held this view because of STP's limited staff, its relative inexperience with GODR financial systems, and the large size of the L/C program -- over 140 widely scattered development projects managed by more than 45 implementing agencies. Branch personnel further stated that, before STP could provide sufficient audit coverage of the L/C program, the monitoring unit would need to overcome several obstacles and make certain structural changes. To make the necessary changes, funding would be needed to contract for project audits and internal control reviews of implementing agencies that the STP auditing unit and the USAID/DR Controller's Office could not make. Without these reviews the Mission cannot assess and evaluate the quality of monitoring that is being conducted by STP, nor can the overall integrity of the L/C program be assured. (See Finding 4 of this report and also Office of the Inspector General Reports Nos. 1-517-88-16, and 1-517-88-17).

Management Comments

The Mission requested that Recommendation No. 2(a) and (b) be revised to assign STP responsibility for monitoring and auditing L/C end-users and for determining if L/C recipients have sufficient management controls in place to properly account for and manage L/C funding. Mission management accepted Recommendation No. 2(c) as written, and requested closure of it based upon RIG/A/T's receipt of the signed PW technical assistance contract.

Management officials also stated that, in accordance with applicable guidance in effect at the time covered by the audit, the responsibility for in-depth financial reviews of L/C projects rested with the GODR, not USAID/DR. Mission officials noted that their responsibility is to monitor the STP Coordinating Unit's (CU) progress and to "assist it to either perform adequate reviews or to contract them out to qualified local CPA firms." The Mission also noted that its efforts as described in its comments to Recommendation No. 2 "demonstrate that it has fulfilled its responsibilities to the extent possible."

Finally the Mission advised that "since the Mission's financial analyst was hired in March 1987, six reviews of implementing agencies have actually been performed by USAID/DR in situations where serious problems came to the Mission's attention." Also, in December 1986 and March 1987, two local contracts were signed with Price Waterhouse and Company and local Coopers & Lybrand affiliate to perform two audits and financial management systems reviews.

Office of the Inspector General Comments

USAID/DR Mission Order 11-4 on local currency management, in effect during the entire course of the audit, specifically tasks the Mission's Controllers Office with undertaking "financial reviews of selected projects financed with [L/C] and request/coordinate audits as appropriate." This Mission policy statement correctly recognized that for USAID/DR to adequately accomplish its financial oversight function and assess STP's monitoring capability, it must also perform in-depth reviews of L/C projects to accurately evaluate the quality and scope of STP's monitoring coverage and to subsequently recommend improvements. Once the Mission has made its evaluation of implementing agencies' capabilities, it has a responsibility to assist the STP in performing "adequate reviews or ...contract[ing] them out to qualified local CPA firms." In our opinion adequate financial oversight of a program also implies that implementing agency recipients have in place adequate accounting and administrative systems before they are given funding. This management control was made mandatory by A.I.D./Washington on October 21, 1987 through issuance of its Supplemental Guidance on Programming Local Currency. Since USAID/DR has chosen since 1982 to jointly program and projectize L/C projects with the host government, it must also have "reasonable assurance that the activities have been designed in accordance with sound technical, financial, (emphasis added) and environmental practices, that implementation and monitoring capabilities of the implementing entities are adequate, and that periodic audits of relevant activities will be undertaken."

Concerning management's response to Recommendation 2(a), we are unable to agree that the PW technical assistance contract will completely relieve the USAID/DR Controller's Office of its oversight responsibility, and its important function of selectively reviewing L/C end-users. We assume that the Mission's Financial Analysis Branch will allocate a reasonable portion of its audit resources for periodically reviewing L/C end-users or at least to contract out that function to qualified CPA firms to accomplish the reviews. Keeping these alternatives in mind, Recommendation 2(a) was revised accordingly.

Recommendation 2(b) has also been revised to allow USAID/DR to oversee STP's review of implementing agency management control systems. In its management response, the Mission inferred that STP's management control reviews would be designed as a part of the Mission proposed PW technical assistance contract. Recommendation 2(b) can therefore be closed based on USAID/DR providing the PIG/A/T with details of STP's management control review system and evidence of a sample STP management control review.

Interviews with responsible Controller personnel on November 6, 1987 and a detailed review of branch workload data indicated that the Financial Analysis Branch had not performed any financial reviews of L/C recipients from December 9, 1986 to November 3, 1987. On November 4, 1987, the Financial Analysis Branch conducted an evaluation of loan funds made to the country's Agricultural Bank as part of the L/C Program. It is our view that the branch's review of the bank was not adequate in that it did not include any independent testing of the bank's financial records, and relied exclusively on financial information provided in the bank's financial statements.

3. Host Country Project Disbursement System Needs to Be Simplified

The PL 480 and ESF Local Currency Memoranda of Understanding required that disbursements from the Government of the Dominican Republic's Central Bank to implementing agencies be accomplished within 10 days. A review of sampled disbursements from local currency bank account statements under PL 480 Agreements indicated that disbursements to implementing agencies were taking significantly longer than the required period; were sometimes not in the amounts authorized; and, as a result, often could not be traced through the disbursement system within a reasonable period of time, if at all. We attributed the cause of the delays and inaccuracies to the laborious and overly complicated design of the local currency disbursement system. As a result, not only were disbursements of project funds to implementing agencies delayed, thereby delaying progress of the projects, but local currency proceeds were commingled with funds from other GODR General Fund Accounts and were untraceable. In addition, because accounting systems and internal controls were weak at the implementing agency level, as we found during our audit sample, adequate assurance could not be provided in such cases that the funds would be properly used.

Recommendation No. 3

We recommend that USAID/Dominican Republic, in consultation with appropriate Government of Dominican Republic Officials:

a. explore means with the Technical Secretariat of the Presidency to establish a disbursement system in which Public Law 480 and Economic Support Fund local currency funds would be disbursed directly from a program account maintained at the Central Bank to the intended implementing agency, thereby eliminating deposits of the local currency proceeds in the National Treasurer's General Fund Account; and

b. if the disbursement system advised in Recommendation 3a. is determined to be unfeasible under Dominican Republic Law or otherwise, negotiate a simplified disbursement system similiar to those recommended in the Arthur D. Little Management Report as a condition precedent to any future Economic Support Fund or Public Law 480 local currency agreement.

Discussion

Disbursement procedures contained in Annex C of the Memoranda of Understanding (MOU) to PL 480 Agreements of 1984, 1985 and 1986 require that under no circumstances will disbursements made from the Central Bank through the National Treasurer to implementing agencies exceed 10 working days. These procedures were established in the MOU's to ensure adequate and timely funding of self-help projects specified in the local currency agreements.

Two evaluations of the L/C Program recommended simplification of the Local Currency disbursement system. The Rural Development Service's Evaluation Report, published in August 1986, highlighted the slowness of the local currency disbursement system in its evaluation and reported that their disbursement transactions were delayed an average of 72 days. Four months later, Arthur D. Little Internationl Inc., a well known consulting group, reported that the L/C disbursement system was unnecessarily complex and involved too many institutional exchanges and approval requirements. At least seven entities had to approve a project disbursement prior to its actual release to the requesting implementing agency. This group recommended that the system be streamlined to operate much in the way it had worked in 1978, when fewer institutional participants were involved, without any loss in control over resources.

To test the reliability, accuracy, and effectiveness of the system, audit staff judgmentally selected 10 disbursement transactions pertaining to the Central Bank accounts established under the PL 480 1984, 1985 and 1986 Agreements. The audit team attempted to trace these 10 sample disbursements through the different stages of the L/C disbursement system, for example:

-- from the initial request for disbursement by the implementing agency to its subsequent approval by the Technical Secretariat of the Presidency and USAID/DR Mission;

-- to the Central Bank's authorization for release of the disbursement from L/C bank accounts;

-- to authorization by the host country's Controller General for deposit of the disbursement in the National Treasurer's General Fund, (effectively commingling L/C proceeds with funds from the country's other operational accounts);

-- to transfer of the funds to the government-operated Reserve Bank, where the L/C funds were held in the GODR's General Fund account, until the implementing agency again formally requested release of the funding.

Due to delays in obtaining required documentation and approval authority from the host-government, only 3 of the 10 sample transaction could be reviewed by the audit team. Two of these transactions could be traced through only part of the system. The requested funding was either released to the implementing agency in different amounts than originally disbursed, or was not received at all. Neither the implementing agency chief accountant nor the L/C project accountants were notified of the original disbursements made by the Central Bank to the implementing institution. Without knowing how much funding should have been received, implementing agency accountants could not make accurate reconciliations of L/C project bank accounts to determine the amount of originally disbursed funds still outstanding. Finally, the third transaction, a disbursement for approximately $170,000 was deposited in an implementing agency's general account within 10 days, but the funds were used for operations that were not related to the L/C program.

Although two independent evaluation teams had recommended that the local currency disbursement system be simplified, little in the way of structural changes had been accomplished to eliminate the unnecessary bottlenecks in the system and facilitate disbursement of the local proceeds to the recipient agencies in a more efficient and effective manner. As of November 16, 1987, the project disbursement system remained essentially unchanged from what it was prior to issuance of the evaluation reports and the majority of the recommendations that pertained to this problem area had not been implemented. Both STP and USAID/DR Mission personnel stated a preference for a simpler system to monitor and oversee local currency funding. They noted that, prior to the present disbursement system, L/C proceeds were disbursed directly from the Central Bank to the implementing agencies, thereby eliminating unnecessary inter-institutional exchanges and approvals, while preserving the integrity of an audit trail for evaluating project progress and financial accountability. STP officials also stated that they wanted to simplify the L/C disbursement system, but had been told that such a simplification was not possible due to International Monetary Fund constraints placed on the country. These restrictions could not be verified and, in any event, would no longer be valid, since an IMF agreement has not been in effect in the Dominican Republic since April 1986.

The present local currency disbursement system not only delayed disbursement of project funds to the implementing agency and project progress, but through its design had also commingled L/C disbursements with funds from other GODR's General Fund Accounts. Once commingled at the National Treasury level, further tracing of a transaction is often not cost-effective or possible. In addition, because accounting systems and internal controls were weak at the implementing agency level, as we found to be the case at four of the six implementing institutions we visited, the necessary management and accounting controls were not in place to prevent local currency proceeds from being spent for unauthorized purposes or potentially diverted without detection.

Management Comments

USAID/DR made the following comments on Finding and Recommendation No. 3:

> Since August 1986 when the new GODR administration took office, the USAID has discussed on numerous occasions with the Technical Secretariat of the Presidency [STP] regarding the desirability of streamlining the GODR legally prescribed disbursement system through which local currency resources flow.

Using the Rural Development Services, Inc. Report, funded by USAID/DR, which in July 1986 first made recommendations regarding the need to modify the system, we made every effort to improve the procedure. In October 1986, the USAID funded an Arthur D. Little study followed by a workshop which included all eight of the GODR agencies directly involved in the disbursement system. Nevertheless, these procedures are governed solely by the regulations of the host country and can only be revised with their consent.

In a letter dated January 18, 1988 to the USAID Director, STP states: "We recognize the need to simplify the project disbursement system, even when encountering difficulties, not always internal, to do so. In consultation with the STP, USAID/DR, contracted the Arthur D. Little consulting firm, which developed a simplified disbursement system which we have encourage the government to adopt.

We should note that the auditor's recommendation that the simplification be achieved by discontinuing the normal funds management procedures used by the host country is not acceptable since the use of different disbursement procedures would short circuit the existing controls of the Controller General of the Republic, National Treasury, National Budget Office, and the Presidency of the Republic...."

Based on this communication with the STP and "other evidence" of the GODR's "firm resistance" to simplifying the system, USAID/DR requested that Recommendations No. 3(a) and (b) be closed.

Office of the Inspector General Comments

We closely reviewed STP's January 18, 1988 letter to the USAID/DR Mission Director and are satisfied with the Mission and STP's good faith attempts at simplifying the L/C disbursement system. Recommendation No. 3(a) is therefore closed upon issuance of this report. We feel, however, that the L/C disbursement system's present design creates such serious vulnerabilities and delays in the control and accounting of funds that any future local currency agreement between the two countries should include a condition precedent to require a more simplified system.

We have also revised the second part of the recommendation to encourage streamlining the present system. The recommendation can be closed through the Mission's submission of evidence that this requirement has been included in USAID/DR's continuing negotiations with the Dominican Republic on any new Economic Support Fund or PL 480 L/C agreement.

4. Implementing Agencies Need to Establish Separate Bank Accounts to Adequately Account for Local Currency Generations

Disbursement procedures established in Local Currency Agreement Memoranda of Understanding for years 1984, 1985 and 1986 required the Government of the Dominican Republic's implementing agencies to establish separate bank accounts to ensure accountability for L/C proceeds used to finance host country development projects. However, 35 of the 69 implementing agencies had not established separate bank accounts for receipt, accountability, and management of local currency proceeds. In addition, at least 20 local currency agreements signed between the Technical Secretariat of the Presidency and implementing agencies contained no provisions requiring separate bank accounts to be established. Neither STP nor USAID/DR had required implementing agencies to submit substantive proof that the intended recipient had opened a separate bank account to segregate local currency funding from the end-user's other funding sources. As a result, approximately half the local currency expenditures could not be clearly documented. Additionally, an accurate evaluation of the project's progress could not be achieved because it was difficult to identify the financial resources used to fund the project cost.

Recommendation No. 4

We recommend that USAID/Dominican Republic, in consultation with appropriate Government of Dominican Republic officials, obtain:

a. from implementing agencies, proof that specific local currency project bank accounts have been established;

b. from the Technical Secretariat of the Presidency, (i) a schedule of reconciliations of all previously commingled accounts of implementing agencies to ensure that local currency proceeds have not funded ineligible activities, and (ii) copies of all A.I.D. related audit reports they have issued; and,

c. from the Government of the Dominican Republic, replenishment of the special account for the amount of any unauthorized uses.

Discussion

Disbursement procedures contained in Memoranda of Understanding (MOUs) for 1984, 1985 and 1986 between the Government of the Dominican Republic (GODR) and the United States of America stipulated that, prior to their disbursement, implementing agencies would establish separate bank accounts to receive, segregate, and properly account for the local currency proceeds programmed for them to accomplish self-help projects specified in L/C agreements. This requirement was inserted in the MOU by USAID/DR in response to the Agency's increased use of special accounts urged by A.I.D. Policy Determination Number 5 (PD-5) issued on February 22, 1983.

Since the time the first disbursements of L/C proceeds were made on November 6, 1984, fewer than half the L/C program's implementing agencies had established special bank accounts to segregate L/C proceeds from their other institutional funds and operational accounts. In June 1986, USAID/DR contracted the Rural Development Services (RDS) Consulting Group to evaluate the USAID/DR local currency program. RDS reported that as of August 1986, 35 of the 69 L/C projects which they evaluated did not have separate project bank accounts established to account for local currency proceeds released under the program. The consulting group also estimated that nearly 45 percent of the total expenditures for the L/C program was not clearly documented since many of the program's implementing institutions had not established special project bank accounts to segregate, control and account for these resources.

On December 8, 1986 USAID/DR's Financial Analysis Branch reported that the Government of the Dominican Republic's parastatal electricity corporation, Corporacion Dominicana de Electricidad (CDE), had failed to establish special bank accounts for over $21,000,000 in L/C proceeds released to it through the PL 480 Title I and Economic Support Fund Programs. The L/C equivalent of $5.3 million could not be traced to jointly programmed projects and were assumed by the STP monitoring unit to have been used by CDE for unauthorized purposes. (For details see Audit Report 1-517-88-16)

From December 1986 to August 1987 CDE received additional L/C disbursements worth approximately $488,506. The Technical Secretariat of the Presidency reported on August 17, 1987 that CDE still had not established a special bank account for receipt of PL 480 and ESF local currency deposits. On October 1, 1987 the USAID/DR Controller recommended that CDE receive no further L/C proceeds until the institution opened a separate bank account and rectified other irregularities.

As part of the audit, we also visited a GODR implementing agency responsible for domestic development of coffee and cacao crops, the Secretariat of State for Agriculture (SEA). SEA had received local currency generations equivalent to about $1.1 million for this project. A review of the institution's bank records and chart of accounts indicated that it had commingled these L/C funds with regular GODR counterpart contributions for the project. The Director of the Institution told the auditors that it was very costly and complicated to establish a special account for local currency proceeds. A further review of the institution's charts of accounts, however, revealed that World Bank contributions were deposited in a special account. When asked about this account, the institution's accounting personnel stated that the World Bank insisted on this arrangement prior to disbursing any funds to the institution.

Finally, a review of the 20 projects signed between the GODR's executing unit for the PL 480 Agreement, STP, and the implementing agency responsible for the particular project indicated that none of the agreements contained any language requiring the implementing agency to establish a separate bank account for the project. (See Exhibit 1).

Adequate program and financial oversight by the USAID/DR Capital Resources Development Office (CRD) and the Controller's Office, which were responsible for program and financial oversight of the L/C Program, would have ensured that separate bank accounts had been established by implementing agencies before they received local currency generations to accomplish the projects. Mission personnel stated that they assumed separate bank accounts had been established for the projects and were surprised to be informed otherwise by the RDS evaluation. They also stated that the Technical Secretariat of the Presidency was the primary monitoring unit of the program and that they should have identified the problem.

It is our opinion that establishing separate bank accounts for local currency projects is neither costly nor complicated. On the contrary, it is essential for effective oversight and monitoring of L/C utilization by implementing agencies which do not have adequate accounting systems to segregate and appropriately allocate fund resources and expenses among different activities and projects. This position has also become a requirement under current USAID/DR Controller policy for approval of disbursement requests to implementing agencies. Since August 24, 1987, the USAID/DR Controller's Office has required STP to provide evidence that implementing agencies requesting local currency funds have established separate bank accounts to properly account for local currency funds. Since that date, the USAID/DR CRD Office in conjunction with STP prepared a form transmittal letter to certify that a special bank account has been opened by an implementing agency when requesting disbursements of L/C proceeds. Although such certification is a step in the right direction, a review of a November 10, 1987 STP certification letter revealed that a copy of the project bank account statement was not provided with the certification, and that the referenced bank account number could have pertained to any of the implementing agency's accounts, or could even be invalid.

Commingling of L/C generations by implementing agencies with their other operational accounts prevents: an accurate evaluation of the project; the establishment of an accurate audit trail for evaluation of a project's progress; and a qualitative review of the project's financial accountability. Commingling of funding can also allow jointly programmed funds to be used for unauthorized purposes.

Management Comments

Mission management again reiterated its position that the STP coordinating unit "is directly responsible for management and oversight of GODR-owned local currency." Mission officials stated that STP's current certification to USAID/DR that separate bank accounts have been established "by program implementing agencies is sufficient to close Recommendation No. 4(a)." Concerning Recommendation No. 4(b), Mission officials responded that previously commingled accounts "may not be available for reconciliation" since project documentation was "as much as 4-6 years old." They added that they were working with the STP on establishing a review system to determine if "project objectives have been met on completed projects." The "project completion review system" would be included as part of PW's technical assistance package. The Mission requested the closure of Recommendation 4(b)(i) be based on providing the RIG/A/T with a copy of the PW technical assistance contract.

With respect to Recommendation No. 4(b)(ii), the USAID/DR said that it was now included on on STP's audit report distribution list, and that it had "already received a list of 55 audits performed by the [STP] as well as a copy of a request for proposals to have local CPA firm do an additional 30 audits." Based on this action, the Mission requested closure of the recommendation. Regarding requirements contained in Recommendation No. 4(c) to replenish the special account for any unauthorized uses, USAID/DR replied that the Mission would include such a provision in PW's "project completion review" system scheduled to be designed under its technical assistance contract. Mission officials requested that closure of this recommendation be based on its submission of the PW contract to the RIG/A/T.

Office of the Inspector General Comments

We agree that the STP Coordinating Unit is directly responsible for management of the L/C program, but also believe that the Mission has an obligation to adequately oversee the direct management of the program to ensure the local currency proceeds are properly used and accounted for. This assignment of responsibility is clearly outlined in USAID/DR's L/C Program Mission Order No. 11-4, in effect during the audit "...The coordinating Unit within the [STP] is the entity that is assigned responsibility for monitoring project executive. . ." Although the Unit is the focal point for monitoring the end use of L/C Program resources, USAID oversees the use of these resources. . . USAID technical offices have the primary responsibility for overseeing implementation of all projects and activities, financed from the LC Program, which fall in their individual sector.... In addition to the technical offices, CRD/LCP will also oversee implementation of selected projects and write reports on its findings." As USAID/DR's own policy statement specifies, the Mission has a very definite oversight responsibility for management of the L/C program. This responsibility is made more important by the fact that the Mission has elected to participate directly in the detailed programming and approval of L/C projects.

Concerning requested closure of Recommendation No. 4(a), the audit team reviewed STP's certification procedure and found it to be partially inadequate. As shown to us by CRD officials, STP certification contained only a referenced bank account number, without any attached bank account statements or other physical evidence that would show the name and address of the accounts. We view the establishment of special bank accounts for L/C projects to be such an important internal control procedure that, in order to properly address this recommendation, STP certification should also include a copy of the L/C account project bank statement demonstrating that the account was opened specifically for the particular L/C project.

Recommendation 4(b)(i) requests that USAID/DR oversee STP's reconciliations of implementing agency commingled accounts to ensure that L/C proceeds have not been used for unauthorized purposes. We acknowledge Mission concern that much of the L/C Program documentation is outdated, and may not be available for reconciliation. Recommendation 4(b)(i) can therefore, be closed after STP demonstrates to USAID/DR a good faith effort to reconcile and schedule the planned reconciliation of as many commingled accounts as possible, showing cause why a particular account cannot be reconciled. This recommendation may be considered resolved but open pending review of the proposed PW "project completion review system" to determine if it has incorporated procedures for reconciling previously commingled accounts. The Mission is also asked to provide RIG/A/T with details on the design of STP's project completion review system and a copy of the planned schedule.

The Mission's prompt action in obtaining a list of 55 STP audits reports, being put on the distribution list for these and future audit reports as well as their request for STP's proposed contracting out of 30 additional audits, will be of great assistance to USAID/DR in the accomplishment of its oversight Mission. As a result, Recommendation 4(b)(ii) can be considered closed upon issuance of the report.

Recommendation 4(c) is considered resolved but open pending Office of the Inspector General review of PW's project completion review system and the subsequent results of its implementation.

5. Local Quality of Audit Reporting And Recommendation Follow-Up System Needed Improvement

The PL 480 Title I and Economic Support Fund cash transfer agreements in force during the period under review required that books and records of fund recipients be audited on a regular basis. Recipients of U.S. appropriated funds must have in place an adequate follow-up system to ensure that recommendations are implemented and that appropriate corrective actions are taken to resolve reported problem areas. Although these criteria do not apply, strictly speaking, to the local currency program in the Dominican Republic, sound financial management and adequate oversight principles urge that similar standards be adopted. The adoption of such standards would also have a developmentally desirable impact on STP and other GODR agencies included in the program. Technical Secretariat of the Presidency audit coverage and reporting on the local currency program varied greatly in quality, but was found to be generally inadequate. In addition, the STP Audit Division did not have in place an adequate system to follow up on audit report recommendations. These deficiencies occurred due to the Mission's limited involvement with the STP financial monitoring unit and inadequate oversight of the monitoring unit's operations, as well as an unwillingness on the part of STP management to adequately staff and equip its audit function. In addition, the STP lacked formal policy guidance governing the preparation of audit reports and proper implementation and follow-up of audit report recommendations. As a result, little or no action was taken to correct problems reported by STP.

Recommendation No. 5

We recommend that USAID/Dominican Republic, in conjunction with appropriate Government of Dominican Republic officials:

a. obtain evidence that the Technical Secretariat of the Presidency has prepared formal, written policies and guidelines to govern the preparation of audit reports in line with the U.S. General Accounting Office's "Standards for Audit of Governmental Organizations, Programs, Activities and Functions";

b. ensure that the Technical Secretariat of the Presidency establish a formal system to issue audit reports to audited entities, that their recommendations be viable and directed to specific areas or functions, and that a follow-up system be established to ensure that such recommendations are implemented in a timely manner;

c. request that the Technical Secretariat of the Presidency include USAID/Dominican Republic on its distribution list for all of Technical Secretary of the Presidency's audit reports on A.I.D. local currency program recipients. As part of the Mission's oversight role, USAID/Dominican Republic officials should periodically review and test STP's recommendation follow-up system to ensure that STP audit report recommendations are consistently implemented or resolved; and

d. earmark up to five percent of each Public Law 480 and Economic Support Fund local currency project for audits by public accounting firms at least once during the life of the project.

Discussion

The PL 480 Title I and ESF Agreements for 1985 and 1986 contained a requirement that the GODR audit the use of funds provided under those agreements. The applicable clause stated that:

> The Borrower will... maintain or cause to be maintained, in accordance with generally accepted accounting principles and practices consistently applied, books and records relating to this Agreement. Such books and records will be audited regularly, in accordance with generally accepted auditing standards and maintained for three years after the last disbursements of proceeds by the Central Bank.

By way of example, the General Accounting Office (GAO) which is responsible for Congressional audits of institutions and agencies receiving U.S. Government appropriations has also established "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" that require some type of adequate mechanism to be in place to follow up on findings and recommendations contained in audit reports.

In addition, Office of Management and Budget (OMB) Circular A-50 requires that the follow-up system: a) include the appointment of a top-level audit follow-up official, b) be timely, c) include criteria for proper resolution and corrective action of the audit report recommendation, and d) track the status of audit reports and recommendations though the entire process of resolution and final corrective actions. Sound financial management and adequate oversight principles require similar standards for local currency programs.

The GODR's Technical Secretariat of the Presidency (STP) created an Audit Division in 1985 to provide audit coverage of the PL 480 Title I and ESF local currency programs and their related projects and activities. Authorized staffing for the auditing unit was only one supervisor and four auditors. However, during most of 1987 the STP Audit Division operated at less than full strength, even though its task of comprehensively auditing over 140 widely-scattered development projects, managed by over 45 different implementing agencies, remained unchanged.

As of July 1, 1987 the STP Audit Division had performed audits of just 31 percent of the L/C program's 144 development projects. Using past performance as an indicator, the STP auditing unit may not be able to audit a significant number of the local currency program's development projects before completion, unless the STP Audit Division's staff resources are increased or a sizeable percentage of the audit workload is contracted out to private sector auditing firms.

Audit reports prepared by the STP audit unit varied greatly in quality. The audit unit did not have any written guidance concerning what information should be included in an audit report and it did not use any standard format to prepare its audit reports. We reviewed 20 audit reports issued by the STP Audit Office, and used GAO "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions" as a guide in order to evaluate audit report accuracy, completeness and effectiveness. The GAO auditing standards require that audit reports meet certain professional attributes and criteria. Results of this analysis found that STP audit reports did not meet over half the attributes tested. (See Exhibit 2.)

Distribution of STP audit reports was not adequate and was generally limited to the chiefs of the STP Audit Division and Coordinating Units. Prior to August 1987, the USAID/DR (CRD) L/C Program coordinators was not included on the distribution list, and, at times, even auditees were not provided copies of final audit reports.

Another problem in the audit process at STP was the lack of an adequate audit recommendation follow-up system. STP did not have in place any formal system to ensure the proper implementation of its audit recommendations and monitor the progress of corrective actions taken by the auditee to resolve a particular problem. As a result, many of the STP Audit Division's recommendations were never implemented and reported problems often remained uncorrected. For example, on May 29, 1987 STP auditors reported that the Dominican Electricity Company (CDE) had used approximately $4.5 million in L/C equivalents for purposes other than those agreed upon in the project agreements. However, no corrective action was taken by STP to correct this deficiency.

No follow-up occurred because STP did not have any formal, written guidance or policies for handling audit report recommendations. Additionally, many audit reports failed to identify internal control and project implementation weaknesses. STP lacked sufficient staff and was also hampered by the lack of formal policy guidance regarding scope of audit coverage, quality of audit reporting and a recommendation follow-up system that would require audit report recommendations to be implemented on a timely basis. As a result, some STP audit reports did not adequately address problem areas and other reported problem areas remained unresolved because recommendations were not implemented.

Management Comments

The Mission had the following response to Finding No. 5:

> The USAID/DR appreciates and generally agrees with the observations of the draft audit. Improvement in this area is of primary focus in the comprehensive technical assistance contract for the [STP] in financial management. It is important, however, to

recognize that these are host country-owned local currencies and that USAID/DR cannot and should not insert itself directly into the management structure "in place of the GODR". We should instead, help it develop adequate systems and then assure ourselves that the systems are working properly through periodic testing.

In addition, it made these comments to Recommendation No. 5 (a) and (b):

> USAID/DR agrees that the auditing function is an important area in which the STP needs to enhance its capacity and performance. We are currently developing, in cooperation with the STP, a technical assistance contract with Price Waterhouse & Co. with specific emphasis on developing STP's abilities to:
>
> 1) Establish clear monitoring and financial oversight capabilities over local currency generations;
>
> 2) Ensure methods whereby the CU [STP] determines whether the implementing agencies have sufficient management controls (including a separate bank account) to adequately safeguard, administer and account for local currency funds before they are disbursed;
>
> 3) Improve the oversight capabilities of the CU [STP] to ensure that local currency funds are not released until all requirements are met; and
>
> 4) Ensure that CU [STP] audits fully comply with U.S. General Accounting Office's "Standards for Government Auditing" and that the appropriate actions are taken with respect to the audits.

Concerning Recommendation No. 5(c), USAID/DR stated that "oversight" of the L/C program should not include a 100 percent review of actions taken by implementing agencies in response to STP audit recommendations. It was noted that now the L/C Program had some 50 implementing agencies and 150 projects. Mission officials requested the recommendation to read "that USAID/DR should ensure that a system to 'review and approval of actions taken' be incorporated into the coordinating unit's management responsibilities." Again, the Mission asked for closure of this recommendation to be based upon RIG/A/T receipt of a pending PW technical assistance contract.

Finally, regarding Recommendation No. 5(d), USAID/DR requested that "up to five percent" rather than five percent of each project's budget be set aside to finance project audits, since the size and complexity of the projects varied. Mission management asked if "the recommendation could be closed upon submission of evidence to the [RIG/A/T] that the GODR had agreed to set aside up to five percent available for the new projects."

Office of the Inspector General Comments

It is true that GODR's L/C Program is financed with host country owned currency. Such ownership, however, cannot and does not absolve the Mission from its association with or responsibility for the success of this A.I.D.-sponsored program. During the audit we noted that the country's newspapers often discussed the relative progress of L/C projects and routinely referred to them, for example, as a USAID Title I or PL 480 development project. As such press reports make clear, the ultimate ownership of the local currencies does not affect or diminish USAID/DR's affiliation with the program, or its responsibility to oversee the probity of its financial administration. We are in full agreement with the Mission's goal of assisting STP in developing adequate financial management systems, and thereafter checking the reliability of these systems through periodic testing. The Mission's planned actions stated in its response to Recommendation No. 5(a) and (b) appear comprehensive and should be sufficient to provide STP with the necessary capability to effectively monitor the program. As a result, Recommendation 5(a) and (b) will be considered resolved but open, pending our review of action taken.

Closure of Recommendation 5(c) may be accomplished by providing RIG/A/T with evidence of USAID/DR's review of STP's recommendation follow-up system, once it becomes operational. Also, Recommendation 5(d) was revised as requested to earmark "up to five percent" of each project's budget to complete project audits. The Mission can close this recommendation by submitting evidence of such set-asides. In addition, the Office of the Inspector General requests a copy of a recently approved L/C project financial plan showing that the required audit was properly budgeted for.

B. Compliance and Internal Controls

1. Compliance

The audit identified two compliance exceptions in the: 1) timeliness of local currency disbursements to implementing agencies, and 2) establishment of special bank accounts to segregate local currency funds from other implementing agency fund resources. Disbursement procedures contained in PL 480 Title I Memoranda of Understanding (MOU) for years 1984, 1985 and 1986 required that disbursements of local currency proceeds from date of initial request to effective receipt by the implementing agencies not exceed 10 days. Actual Local Currency disbursements took substantially longer than this to be received by the implementing agencies (See Finding 3). Further, the design of the disbursement system did not provide an adequate audit trail for tracking the accountability of local currency disbursements.

The MOU's also required implementing agencies to establish separate bank accounts to segregate local currency funds from other implementing agency resources. Audit test results and a review of prior evaluation reports indicated that implementing agencies had not established separate bank accounts for a substantial number of L/C projects (See Finding 4).

2. Internal Controls

Four major internal controls weaknesses were found during the audit. First, the Mission had no reliable mechanism in place to assure itself that implementing agencies had received all the originally disbursed local currency proceeds (Finding 1).

Second, the Mission's Financial Analysis Branch had not provided sufficient review coverage of the local currency program and financial oversight of the Technical Secretariat of the Presidency's Audit Division (Finding 2).

Third, local currency funds were commingled at both the national and implementing agency levels, thereby preventing adequate accountability of local currency proceeds (Finding 4).

Fourth, the Technical Secretariat of the Presidency's Audit Division did not provide sufficient audit coverage of the local currency program, which made local currency resources especially vulnerable to waste, fraud, and mismanagement (Finding 5).

PART III - EXHIBITS AND APPENDICES

LIST OF PROJECT AGREEMENTS IN WHICH THERE WAS NO SEPARATE BANK ACCOUNT REQUIREMENT

Implementing Agency	Project
1. Agricultural Bank	Agriculture/Livestock Credit
2. Agricultural Bank	Cocoa-Coffee Credit
3. Secretariat of Public Works	La Vega-Jarabacoa Road
4. Secretariat of Public Works	Duarte Road
5. Secretariat of Public Works	Neighborhood Roads
6. Secretariat of Public Works	Neighborhood Roads BID
7. National Hydrologic Resources Agency	Nizao-Valdesia, Irrigation
8. National Hydrologic Resources Agency	Zabaneta, Irrigation
9. National Hydrologic Resources Agency	Aglipo, Irrigation
10. National Hidrologic Resources Agency	Rehabilitation Canals
11. National Hydrologic Resources Agency	Yaque del Norte, Irrigation
12. Dominican Electricity Company	Substations
13. Dominican Electricity Company	Gas Turbine-Barahona
14. Dominican Electricity Company	Lopez Angostura
15. Dominican Electricity Company	Diesel Plant
16. Dominican Electricity Company	Rehabilitation-Timbeque
17. Dominican Electricity Company	Tourist Zone Transmission Line
18. Dominican Electricity Company	Falconbridge Interconnection
19. Dominican Electricity Company	Jimenoa Hydroelectric Dam
20. Dominican Electricity Company	Rehabilitation Lines-Santo Domingo

RESULTS OF KEY ATTRIBUTES OF TWENTY
HOST COUNTRY AUDIT REPORTS

		Yes	No
1.	Audit objectives clearly stated	10	10
2.	Audit scope and period delineated	13	7
3.	Clear background section	10	10
4.	Statement of how the audit was conducted	11	9
5.	Evaluation of internal control system	7	13
6.	Report on compliance with D.R. laws	2	18
7.	Report on compliance with AID/DR agreement terms	1	19
8.	Presentaton of financial statements for period covered	15	5
9.	Financial disclosure of disbursements made to and from recipient institutions	13	7
10.	Disclosure of counterpart contributions	9	11
11.	Determination whether disbursements were made for agreed upon purposes or amounts	6	14
12.	Evaluation of the accuracy of financial or other information reported by implementation institutions	8	12
13.	Reconciliation of bank accounts, identification and delineation of other sources of funds	8	12
14.	Adequate finding elements stated (condition, cause, criteria and effect)	1	19
15.	Discussion of pertinent views of responsible officials regarding funding conditions and recommendations	0	20

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	Yes	No
16. Discussion of issues or concerns that need further study, consideraton and determination whether project objectives were met	5	15
17. Audit report issued late, after date specified by law	20	0
18. Recommendation addressed condition and cause	4	16
19. Evaluation of procurement system	1	19
20. Report format includes title page, table of contents	2	18
21. Written audit reports distributed to appropriate personnel	0	20
Total of attributes of the above reports	126	274

UNITED STATES GOVERNMENT

memorandum

DATE: March 25, 1988

REPLY TO ATTN OF: Thomas W. Stukel, Director
USAID/Dominican Republic

SUBJECT: Draft "Audit of USAID/Dominican Republic's Local Currency Financial Oversight System"

TO: Mr. Coinage W. Gothard, Jr., RIG/A/T

We have reviewed the subject draft audit report and are attaching hereto our detailed comments on each recommendation for your consideration. In several instances we have requested specific changes to facilitate implementation of useful recommendations. If RIG elects not to make these changes, we hereby request that the Mission's comments, with respect to that particular item, be incorporated directly into the final report where the recommendation itself is discussed and not just in the annex.

In addition please include the following paragraph directly in the "Executive Summary" section of the final report:

> "The IG Report on the local currency program reflects a fundamental misconception regarding the nature of reponsibilities associated with executing a host country-financed local currency program. Such programs are financed by the Host Country with its own resources. These resources are not U.S. appropriated funds; they are subject to a negotiated agreement between AID and the host country in their programming and disbursement and to the same laws, procedures, and mechanisms employed to carry out the government's regular programs. The financial oversight and management posture adopted by the Mission was exactly that prescribed at the time by the original Policy Determination No. 5. While it is true that Agency guidance was significantly revised in October of 1987, the standards set forth in that revision should not be applied retroactively to activities which took place in prior years. A significant part of the guidance applicable to the period covered by the audit (that is the original PD - 5) was the understanding that host country-owned local currencies did, in fact, belong to the host country and were, to the extent possible, to be managed by them. As such these currencies were primarily the responsibility of the host country and subject to their own laws, regulations and even their own disbursement procedures. These are not US-owned or dollar appropriated funds. Agency policy during this period did not provide hands-on management of host country-owned local currencies which were generated under the 1984, 1985 and 1986 agreements. The record clearly shows, however, that USAID/DR carried out a series of measures to help the GODR improve its abilities to manage its own local currency resources. Weaknesses in host government institutions and controls over local

OPTIONAL FORM NO. 10
REV. 1-80
GSA FPMR (41 CFR) 101-11.6
5010-114

currency resources requires us to help host governments improve their own management capabilities. In no way, however, does weakness in host government institutions management of their own resources imply that the Mission did not perform its oversight functions in keeping with Agency policy in effect at the time."

USAID/DR'S DETAILED COMMENTS
LOCAL CURRENCY OVERSIGHT SYSTEM

RECOMMENDATION NO. 1:
USAID/DR should-

a) Coordinate, with the Technical Secretariat of the Presidency, the establishment of a mechanism that requires implementing agencies to send confirmation notices of receipt of local currency to the Technical Secretariat of the Presidency (TSP);

b) Require the Controller's Office to reconcile these confirmation notices with operational letters that authorized funds disbursed to the projects.

Management Response to "Introduction" and "Results of Audit" Sections:

Steps already taken by the Mission before the audit started were certainly more than a "---series of management actions that were designed to correct problems revealed through audit---" as stated in the draft audit. The audit by RIG did not disclose any significant problems that were not already known to and being addressed by USAID/DR. The auditors were, in fact, advised of such problems and prior actions by the Mission.

The guidance in effect during the period audited, Policy Determination No. 5 (PD-5) dated February 22, 1983, states that "Mission should entrust the recipient country with as much of the work of utilizing and accounting for the country-owned local currency as possible".

Even though it was recognized, correctly, that these LC funds belonged to the host country, the USAID/DR took the position early on that we had to be involved directly in their programming and that the GODR needed assistance to manage these new resources. This is why USAID/DR insisted in December 1981 that a special Coordinating Unit (CU) be created in TSP to manage local currency generated under PL 480 agreements and that it be supported with an extraordinary budget to ensure adequate levels of staff, equipment and operating expense funds. In April 1986 the CU was completely reorganized and strengthened considerably to handle the large increases of local currency emanating from the ESF Agreements. Therefore, USAID/DR did clearly recognize the limits of TSP's capabilities and took additional actions to strengthen TSP's ability to cope with their large and growing LC program.

From 1985 to 1987 the Local Currency Program increased significantly and USAID/DR established a new in-house Local Currency Program Division to provide management oversight over the program. In May 1986 the Mission hired a Personal Service Contractor as Chief of the LC Program Division and began improving its monitoring system. In July 1986, USAID/DR contracted the firm of Rural Development Services, Inc. (RDS) to conduct an evaluation of the LC Program. The RDS assessment report, which included a series of management improvement recommendations, was used to begin strengthening the capacity of the TSP to manage the program.

In October 1986, the TSP, at USAID/DR request, contracted the services of Arthur D. Little, Inc. to review the LC Program disbursement process in order to determine if the process could be simplified and speeded up. Arthur D. Little, Inc. made a series of recommendations which were later the subject of a USAID sponsored workshop which included all GODR agencies involved in the disbursement process. To date, however, the GODR has still not taken actions identified by the workshop as necessary to improving the process and, has in fact, expressed considerable resistance to changing its internal procedures and controls.

At this time, USAID/DR and TSP are completing the final design of a complete Technical Assistance package for the Coordinating Unit to be implemented by Price Waterhouse and Co., International (PW & Co.). All of the problems the Mission has been working on for the last two years and which have been confirmed by the draft report will be addressed by the Price Waterhouse team.

Management Response to Findings, No. 1

The draft audit report does not accurately report USAID/DR delegations of responsibility with respect to local currency management. Mission Manual Order No. 11-4 was superceded by the Director's memo of October 24, 1986 to transfer USAID/DR local currency project reporting responsibilities from the Controller's Office to the Capital Resources Development (CRD) Office. This memorandum required CRD to establish a data base capable of producing reports on the "Financial status of projects including not only the amounts programmed, approved and released but also the amount of LC received by the executing agency and the expenditures the agency has made for each project". This transfer of reporting responsibility within the Mission did take place and the required reports are being prepared with one exception--- project expenditure reporting. Nevertheless, it is important to realize that the intention here was to obtain adequate reports directly from TSP rather than to have CRD collect information directly from implementing agencies. Since TSP has never been able to provide CRD with expenditure data, USAID/DR has been unable to complete its data base report on project expenditures, or carry out complete reconciliations.

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USAID/DR's Detailed Comments

It is also important to note that USAID/DR's decision to transfer financial reporting to CRD did not alter the fundamental fact that basic accounting and reconciliation responsibilities for LC remain with the GODR. The Controller's specifically assigned responsibilities included only the "monitoring of LC generations and deposits" to ensure that they get into the special accounts and that total initial deposits reconcile with the total of CRD's data base. There was no requirement or guidance from AID/W with respect to reconciling implementing agencies receipts with disbursement from the special accounts.

It should also be noted that when the Financial Review Branch conducts a financial review of a DA project or implementing agency, the receipt and use of counterpart funds (i.e. local currency funds) is always verified as part of the review.

Management Response to Recommendation, No.1

1.a) Mission agrees and has incorporated this task into the PW & Co. contract. This recommendation can be closed upon presentation of a copy of the signed contract to RIG.

1.b) This is a responsibility of the Coordinating Unit of the TSP and not of USAID/DR. As such it will be included in the TA contract to be performed by Price Waterhouse & Co and USAID/DR will monitor the CU's performance. We hereby request that the recommendation be revised accordingly. Closure would be requested upon submission of a signed copy of the Price Waterhouse & Co. contract.

RECOMMENDATION NO. 2:
USAID/DR should-

a) Provide a copy of the USAID/Dominican Republic financial analysis branch fiscal year 1988 Financial Review Schedule to the Regional Inspector General for Audit/Tegucigalpa, to ensure that implementing agencies are being reviewed on an in-depth basis at least annually;

b) Condition future releases of local currency funding to implementing agencies upon presentation of evidence by the Technical Secretariat of the Presidency that intended implementing agency recipients have sufficient management controls in place to properly account for and manage local currency funding;

c) Provide the Regional Inspector General for Audit/Tegucigalpa evidence of the financial commitments made to accomplish recommendations a) and b) above.

Management Response to Findings, No. 2:

In accordance with applicable guidance, in effect at the time covered by the audit, the responsibility for in-depth financial reviews of local currency projects, including adequate monitoring of implementing agencies systems and procedures, lies with the GODR, not USAID/DR. It is USAID/DR's responsibility to monitor the Coordinating Unit's progress and to assist it to either perform adequate reviews or to contract them out to qualified local CPA firms. The efforts described in response to recommendation Number 1 demonstrate that the Mission has fullfilled its responsibilities in this regard to the extent possible.

Since the Mission financial analyst was hired in March 1987, six reviews of implementing agencies have actually been performed by USAID/DR in situations where serious problems came to the Mission's attention. In addition, in December 1986 and March 1987, two local IQC's were signed with the local Price Waterhouse and Company representative and with Fernández, Pellerano and Associates (an affiliate of Coopers Lybrand). Two audits have been performed on implementing agencies and two financial management systems designed under these IQCs which focused primarily on dollar appropriated assistance but also covered local currency contributions by the GODR.

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Management Response to Recommendation, No. 2:

2.a) USAID/DR requests that this recommendation be revised to reflect the fact that the Coordinating Unit, not USAID/DR, is responsible for monitoring and auditing of implementing agencies. USAID will continue to monitor CU performance in this important area. The recommendation can be closed upon submission to RIG of a copy of the Price Waterhouse & Co. contract to provide appropriate assistance to the CU.

2.b) USAID/DR requests that this recommendation be revised appropiately to reflect that the determination of the adequacy of implementing agencies capabilities is a direct CU responsibility. USAID/DR will continue to monitor CU's performance. This recommendation too can be closed upon submission of the PW & Co. technical assistance contract.

2.c) Accepted. Recommendation can be closed upon submission to RIG of a copy of the technical assistance contract with Price Waterhouse & Co., International.

RECOMMENDATION NO. 3:
USAID/DR, in conjunction with GODR officials, should-

a) Initiate a dialogue with the Technical Secretariat of the Presidency to establish a disbursement system in which Public Law 480 and Economic Support Fund Local currency funds would be disbursed directly from a program account maintained at the Central bank to the intended implementing agency, thereby eliminating deposits of the local currency proceeds in the National Treasurer's General Fund Account; and

b) If the disbursement system advised in Recommendation 3.a. is determined to be not legally permissable under Dominican Republic Law or otherwise unfeasible, adopt a simplified disbursement system similar to those recommended in the Arthur D. Little Management Report or the Rural Development Services Evaluation Report of the USAID/Dominican Republic local currency program.

Management Comments on Findings, No. 3:

Since August 1986 when the new GODR administration took office, the USAID has discussed on numerous occasions with the Technical Secretariat of the Presidency (TSP) regarding the desirability of streamlining the GODR legally prescribed disbursement system through which local currency resources flow. Using the Rural Development Services, Inc. Report, funded by USAID/DR, which in July 1986 first made recommendations regarding the need to modify the system, we made every effort to improve the procedure. In October 1986, the USAID funded an Arthur D. Little study followed by a workshop which included all eight of the GODR agencies directly involved in the disbursement system. Nevertheless, these procedures are governed solely by the regulations of the host country and can only be revised with their consent.

In a letter dated January 18, 1988 to the USAID Director TSP states: "We recognize the need to simplify the project disbursement system, even when encountering difficulties, not always internal, to do so. In consultation with the TSP USAID/DR, contracted the Arthur D. Little consulting firm, which developed a simplified disbursement system which we have encouraged the government to adopt.

We should note that the auditor's recommendation that the simplification be achieved by discontinuing the normal funds management procedures used by the host country is not acceptable since the use of different disbursement procedures would short circuit the existing controls of the Controller General of the Republic, National Treasury, National Budget Office, and the Presidency of the Republic.---"

USAID/DR's Detailed Comments

Other evidence of continuing dialog by the Mission and firm resistance by the GODR to change is contained in a later study of overall financial management capability of the GODR. This report, by Price Waterhouse and Co., International, confirms that the present government is not inclined to relax its normal internal control procedures, despite their cumbersome nature.

Management Response to Recommendation, No. 3:

3.a) Based upon the ample evidence of USAID/DR's prior and continuing dialog, USAID/DR requests that this recommendation be closed.

3.b) Based upon the evidence provided in the TSP letter and the Price Waterhouse & Co. study mentioned above, USAID/DR requests that this recommendation be closed.

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República Dominicana

Secretariado Técnico de la Presidencia

Santo Domingo, D. N.

NUM.0022

18 de enero de 1988

Señor
THOMAS STUKEL
Director de la Agencia
Internacional para
el Desarrollo (AID)
SU DESPACHO

Ref.: Su comunicación del 4 de diciembre de 1987. Informe de Auditoría

Estimado señor:

Acuso recibo de su comunicación del 4 de diciembre de 1987, en la cual nos transmite copia de los records del Informe de Auditoría del Programa en Moneda Local que conciernen al Secretariado Técnico de la Presidencia.

Este Despacho comparte plenamente la mayoría de las observaciones de los auditores en base a informaciones cortadas al 31 de agosto de 1986, así como las recomendaciones en cuanto a la vigilancia, que se observaban inadecuadas, a las instituciones ejecutoras que manejan fondos en moneda local, particularmente en lo referente a la Secretaría de Estado de Obras Públicas y Comunicaciones y a la Corporación Dominicana de Electricidad. Como observará usted, en la misma comunicación que dictamina esta afirmación, la mayoría corresponden, con excepción de 2 millones de RD$ destinados a López Angostura, a desembolsos efectuados por la pasada administración.

Consecuente con ello, desde un principio de nuestra gestión venimos adoptando providencias que van desde la aplicación de los controles necesarios hasta la sustitución del personal, sin producir por supuesto paralizaciones en el desarrollo del Programa. El superior Gobierno, por su parte dictó el Decreto No.40/87, dirigido a impedir el uso de los fondos externos a propósitos no consignados en los contratos suscritos, hasta el punto que el funcionario que viole esta

ACTION: CRD
DATE DUE: 2-1-88

DR	—
DD	—
CON	—
MGT	
MC	
ADF	
CHD	
RG	
AF	
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HD	
HID	
CHRON	/
F	

República Dominicana

Secretariado Técnico de la Presidencia

Santo Domingo, D. N.

Señor
THOMAS STUKEL
Pág. No.2
18 de enero de 1988

disposición puede considerarse dimitente. Lamentamos, no obs-
tante, no estar en condiciones de reponer dichos fondos a la
cuenta correspondiente, aun cuando ponderamos terminar las -
obras con recursos propios.

A medida que ha transcurrido el tiempo hemos fortale-
cido los controles para corregir progresivamente la adminis-
tración de los mismos, incluyendo particularmente la apertura
de cuentas bancarias separadas.

Hemos tomado nota de las recomendaciones contenidas en
el Record del Informe de Auditoría relacionado con los pagos
tardíos a las empresas y estamos instruyendo a la Unidad Coor
dinadora, de que previa revisión, aplique las penalidades -
correspondientes.

Nos identificamos con la necesidad de simplificar el sis-
tema de desembolsos de proyectos, aun cuando confrontamos con
dificultades, no siempre internos, para materializar este pro
pósito. Consecuentemente con ello, una de nuestra primera dis
posición fue la contratación de la firma consultora Arthur -
D'little, que sugirió un sistema de desembolsos simplificado
que implementaremos proximamente. No obstante, en muchas oca-
siones, la lentitud de los desembolsos responden más bien a -
los propósitos de desmonetización que en oportunidades se han
establecido siguiendo sugerencias de algunos organismos inter-
nacionales. Sin embargo, las recomendaciones de los auditores
en el sentido de que la simplificación sea lograda abandonando
el procedimiento ordinario para el manejo de fondos vigentes
en el país, no es vista con simpatía por este Secretariado, en
vista de que el uso de procedimientos de desembolsos diferentes
estimula la falta de control que necesariamente corresponde a
la Contraloría General de la República, Tesorería Nacional, -
Oficina Nacional de Presupuesto, incluyendo la Presidencia de
la República. Por estas razones, nos hemos inclinado a imple-
mentar las recomendaciones de la Arthur D'little una vez ulti-
mados ciertos detalles relativos a su factibilidad legal.

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República Dominicana

Secretariado Técnico de la Presidencia

Santo Domingo, D. N.

Señor
THOMAS STUKEL
Pág. No.3
18 de enero de 1988

Compartimos los propósitos del Informe de Auditoría sobre el sistema de seguimiento de los proyectos, aun cuando el informe no recoge con exactitud la firmeza de intenciones y los esfuerzos que ha efectuado el Secretariado Técnico de la Presidencia. En el mismo informe de los auditores externos se puede apreciar que fue este Secretariado el que se percató de las anomalías que cita para la Fundación NATURA y la Fundación Dominicana de Desarrollo y que propiciamos los correctivos de lugar. De todas formas nos adherimos al propósito de continuar perfeccionando los mecanismos de control y para lo cual hemos solicitado la colaboración de esa Agencia con miras a fortalecer institucionalmente, en equipos y presupuestos, a la Unidad Coordinadora.

Nos adherimos finalmente a las recomendaciones de los auditores en el sentido de que los informes de auditores de AID sean realizados con mayor frecuencia y mayor profundidad. Para viabilizar esta sugerencia hemos diseñado un volante de aviso de recibo de fondos que vamos a distribuir a las ejecutoras para que acopien esa información y poder transferir a la AID.

Finalmente aceptamos las recomendaciones relacionadas con la segregación de deberes y responsabilidades para adquisición y venta de productos importados y para lo cual esa Agencia contrataría la firma de un Contador Público Autorizado que, partiendo de la separación de las partes correspondientes de cobro y registro de las transacciones de nuestra operación que hemos anticipado, se produzca un manual que contenga mecanismos más elaborados al efecto.

Muy atentamente,

ING. GUILLERMO CARAM
Secretario Técnico de la Presidencia

GC:mts.

USAID/DR's Detailed Comments

RECOMMENDATION NO. 4:
USAID/DR, in conjunction with GODR officials, should obtain-

a) From implementing agencies, proof that separate local currency project bank accounts have been established;

b) From the Technical Secretariat of the Presidency, a schedule of reconciliations of all previously comaingled accounts of implementing agencies to ensure that local currency proceeds have not subsidized ineligible activities;

c) From the Technical Secretariat of the Presidency, a copy of any audit reports they have issued; and

d) From the Government of the Dominican Republic, replenishment of the special account for the amount of any unauthorized uses.

Management Response to Recommendation, No. 4:

4.a) Since the Coordinating Unit is directly responsible for management and oversight of GODR-owned local currency, adequate proof that separate bank accounts have been established is provided by CU's certification to USAID/DR that such an accounts have been opened by implementing agencies.

USAID/DR began requiring this certification on August 24, 1987. USAID/DR therefore requests that this recommendation be closed with the understanding that CU performance will continue to be monitored by the Mission.

4.b) As the draft audit and the prior study by Rural Development Associates, Inc. point out, the documentation from some of these projects, as much as 4 - 6 years old, may not be available for reconciliation. We are working with the CU to establish a review system to determine whether or not project objectives have been met on all completed projects. This completion review system will be included in the Price Waterhouse and Co. technical assistance proposal and the recommendation may be closed upon receipt by RIG of the signed Price Waterhouse and Co. contract.

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USAID/DR's Detailed Comments

4.c) The Mission has already received a list of 55 audits performed by the CU as well as a copy of a request for proposals to have local CPA firms do an additional 30 audits. USAID/DR is now receiving copies of all audits performed by the CU and the Price Waterhouse and Co. contract will help strengthen the CU's ability to perform quality reviews and audits. Based upon these facts, Mission hereby requests that this recommendation be closed.

4.d) This provision will be included, of course, in the system to be completed for project completion reviews under the Price Waterhouse and Co. contract. This recommendation may be closed upon submission of a copy of the Price Waterhouse and Co. contract.

USAID/DR's Detailed Comments

RECOMMENDATION NO. 5:
USAID/DR, in conjunction with GODR officials, should-

a) Obtain evidence that the Technical Secretariat of the Presidency has prepared formal, written policies and guidelines to govern the preparation of audit reports in line with the standards in the General Accounting Office's "Standards for Audit of Gove.nmental ORganizations, Programs, Activities and Functions;"

b) Ensure that the Technical Secretariat of the Prsidency establish a formal system to issue audit reports to audited entities, that recommendations be implementable and directed to specific areas or functions, and that a follow-up system be established to ensure that such recommendations are implemented in a timely manner;

c) Request that the Technical Secretariat of the Presidency include USAID/Dominican Republic on its distribution list for all of Tech..ical Secretary of the Presidency's audit resports made of local currency program recipients. As part of the Mission's oversight role, Mision officials should review and approve actions that are taken to implement Technical Secretariat of the Presidency audit report recommendations: and

d) Earmark five percent of each Public Law 480 and Economic Support Fund local currency project to finance the contrcting of project audits by public accounting firms at least once during the life of the project.

Management Response to Findings, No. 5:

The USAID/DR appreciates and generally agrees with the observations of the draft audit. Improvement in this area is of primary focus in the comprehensive technical assistance contract for the STP in financial management. It is important, however, to recognize that these are host country-owned local currencies and that USAID/DR cannot and should not insert itself directly into the management structure "in place of the GODR". We should instead, help it develop adequate systems and then assure ourselves that the systems are working properly through periodic testing.

USAID/DR's Detailed Comments

Management Response to Recommendation, No. 5:

5.a) USAID/DR agrees that the auditing function is an important area in which the STP needs to enhance its capacity and performance. We are currently developing, in cooperation with the STP, a technical assistance contract with Price Waterhouse & Co. with specific emphasis on developing STP's abilities to:

1) Establish clear monitoring and financial oversight capabilities over local currency generations;

2) Ensure methods whereby the CU determines whether the implementing agencies have sufficient management controls (including a separate bank account) to adequately safeguard, administer and account for local currency funds before they are disbursed;

3) Improve the oversight capabilities of the CU to ensure that local currency funds are not released until all requirements are met; and

4) Ensure that CU audits fully comply with the U.S. General Accounting Office's "Standards for Government Auditing" and that the appropriate actions are taken with respect to the audits.

This recommendation can be closed when RIG receives a copy of the contract signed with Price Waterhouse and Co. to provide the necessary technical assistance.

5.b) See 5.a) above;

5.c) See response to 4.c) and 5.a) above. However, USAID/DR does not agree that "oversight" of the local currency program should include a 100% review of actions taken by implementing agencies in response to the CU's audit recommendations (there are now some 50 implementing agencies and 150 projects). Instead an appropriate follow-up system for the CU will be implemented with the assistance of Price Waterhouse & Co., and USAID/DR will spot check that system on a periodic basis as it continues to monitor the CU's performance. We hereby request that this recommendation be revised to read that USAID/DR should ensure that a system to "review and approval of actions taken" be incorporated into the CU's management responsibilities. This recommendation then could be closed upon submission to RIG of a copy of the Price Waterhouse & Co. technical assistance contract.

5.d) USAID/DR agrees with the intent of this recommendation but requests that it be revised slightly to facilitate implementation. 5% of "each" project may or may not be sufficient for audit depending on the size and complexity of the project. USAID/DR requests that the recommendation be revised to require that "up to five percent" of the total amounts set aside for projects be made available for project audits. The recommendation could be closed upon submission of evidence to RIG that the GODR had agreed to set aside up to five percent of the amount available for new projects.

List of Report Recommendations

Recommendation No. 1

We recommend that USAID/Dominican Republic:

a. oversee the establishment of a confirmation procedure that allows the Technical Secretariat of the Presidency to confirm that implementing agencies have promptly deposited in the local currency accounts those local currency proceeds originally authorized for disbursement; and

b. require the Controller's Office to oversee and periodically test the Technical Secretariat of the Presidency's confirmation procedure to ensure that it is adequate.

Recommendation No. 2

We recommend that USAID/Dominican Republic:

a. ensure that its Financial Analysis Branch include in its fiscal year 1988 financial review schedule periodic in-depth audits of local currency implementing agencies, to be conducted by its own staff or contracted out Certified Public Accountant firms, so that the Mission can adequately assess the Secretariat's monitoring capabilities and performance;

b. condition future releases of local currency funding to implementing agencies based upon a review of Technical Secretariat of the Presidency certification that implementing agency recipients have sufficient management controls in place to properly account for and manage local currency funding; and

c. provide the Regional Inspector General for Audit/Tegucigalpa with evidence of the financial commitments made to accomplish recommendations a. and b. above.

Recommendation No. 3

We recommend that USAID/Dominican Republic, in consultation with appropriate Government of Dominican Republic Officials:

a. explore means with the Technical Secretariat of the Presidency to establish a disbursement system in which Public Law 480 and Economic Support Fund local currency funds would be disbursed directly from a program account maintained at the Central Bank to the intended implementing agency, thereby eliminating deposits of the local currency proceeds in the National Treasurer's General Fund Account; and

b. if the disbursement system advised in Recommendation 3a. is determined to be unfeasible under Dominican Republic Law or otherwise, negotiate a simplified disbursement system similiar to those recommended in the Arthur D. Little Management Report as a condition precedent to any future Economic Support Fund or Public Law 480 local currency agreement.

Recommendation No. 4

We recommend that USAID/Dominican Republic, in consultation with appropriate Government of Dominican Republic officials, obtain:

a. from implementing agencies, proof that specific local currency project bank accounts have been established;

b. from the Technical Secretariat of the Presidency, (i) a schedule of reconciliations of all previously commingled accounts of implementing agencies to ensure that local currency proceeds have not funded ineligible activities, and (ii) copies of all A.I.D. related audit reports they have issued; and,

c. from the Government of the Dominican Republic, replenishment of the special account for the amount of any unauthorized uses.

Recommendation No. 5

We recommend that USAID/Dominican Republic, in conjunction with appropriate Government of Dominican Republic officials:

a. obtain evidence that the Technical Secretariat of the Presidency has prepared formal, written policies and guidelines to govern the preparation of audit reports in line with the U.S. General Accounting Office's "Standards for Audit of Governmental Organizations, Programs, Activities and Functions";

b. ensure that the Technical Secretariat of the Presidency establish a formal system to issue audit reports to audited entities, that their recommendations be viable and directed to specific areas or functions, and that a follow-up system be established to ensure that such recommendations are implemented in a timely manner;

c. request that the Technical Secretariat of the Presidency include USAID/Dominican Republic on its distribution list for all of Technical Secretary of the Presidency's audit reports on A.I.D. local currency program recipients. As part of the Mission's oversight role, USAID/Dominican Republic officials should periodically review and test STP's recommendation follow-up system to ensure that STP audit report recommendations are consistently implemented or resolved; and

d. earmark up to five percent of each Public Law 480 and Economic Support Fund local currency project for audits by public accounting firms at least once during the life of the project.

APPENDIX 5

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