PD-AAZ-901
62968

AUDIT OF VERIFICATION OF ACCOUNTABILITY FOR DOLLARS AND LOCAL CURRENCY ASSOCIATED WITH USAID/PERU PROGRAMS

Audit Report No. 1-527-89-29
September 5, 1989

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

AGENCY FOR INTERNATIONAL DEVELOPMENT
OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

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

September 5, 1989

MEMORANDUM

TO : USAID/Peru Director, Craig G. Buck

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

SUBJECT: Audit of Verification of Accountability for Dollars and Local Currency Associated with USAID/Peru Programs

The Office of the Regional Inspector General for Audit/Tegucigalpa has completed its audit of verification of accountability for dollars and local currency associated with USAID/Peru programs. 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 recommendation is resolved and may be closed when corrective actions planned and underway have been completed. Please advise this office within 30 days of any additional actions taken to implement the report recommendation.

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

EXECUTIVE SUMMARY

Officials who manage A.I.D. dollars or local currency associated with A.I.D. programs must render a full account of their activities to the public. Independent audit is an important internal control technique which serves to verify that funds are properly accounted for and used for authorized purposes. Audits of A.I.D. dollars and local currency associated with A.I.D. programs may be performed by Federal auditors, by non-Federal auditors supervised by the Office of Inspector General, or by non-Federal auditors contracted by organizations receiving assistance. The basic requirements for audit of appropriated dollars and local currency associated with A.I.D. programs are presented in appendix 2.

As of October 31, 1988, USAID/Peru was managing 39 active project agreements with obligations of $162 million. The Mission had spent $100.5 million and advanced $6.2 million under these agreements. The Mission was also monitoring 41 projects funded with local currency deposited under Public Law 480 and Section 416 food assistance programs. Local currency equivalent to approximately $3.4 million had been programmed for these projects, and the equivalent of approximately $1.5 million had been disbursed under the projects.[1]

The Offic of the Regional Inspector General for Audit/Tegucigalpa conducted a performance audit of USAID/Peru's verification of accountability for dollars and local currency. The audit objectives were (1) to evaluate compliance with laws, regulations, and Agency guidance dealing with audit requirements and (2) to evaluate USAID/Peru's system for ensuring that audit requirements were met.

USAID/Peru was in compliance with A.I.D. guidance on audit of local currency projects. However, the Mission had not completely complied with audit requirements applicable to appropriated dollar projects. The audit disclosed instances of noncompliance with the Inspector General Act of 1978, Office of Management and Budget circulars, and A.I.D. guidance. The

---

[1] Exchange rate used is 508 Peruvian intis to 1 U.S. dollar, the exchange rate obtained by the U.S. Embassy as of October 31, 1988 for Treasury checks sold through a bidding system.

Mission also needed to strengthen its system for ensuring that audit requirements were met.

USAID/Peru officials pointed out that management was dealing with many other pressing matters besides enforcing audit requirements. Among the most important matters were: (1) hyperinflation and rapid devaluation of the local currency, (2) intensified terrorism by guerrilla groups in Peru, (3) the imposition of sanctions on the Government of Peru for defaulting on U.S. Government loans, (4) uncertainty over the future of the A.I.D. program in Peru, and (5) the departure of key Mission staff.

The report finding, summarized below, discusses instances of non-compliance with audit requirements for dollar projects.

Audit is a mandatory internal control technique which provides independent verification that all other internal control techniques, operating together, have produced the desired result: A.I.D. funds properly accounted for and used for authorized purposes. Requirements for audit of A.I.D. funds are established by law, Office of Management and Budget circulars, and internal Agency guidance. The current audit found cases where pre-award surveys were not requested and project agreements did not budget funds for audit or did not include required audit provisions. Also, several required audits were not made and the audits which were made did not meet established standards. Mission officials stated that these weaknesses existed because of inadequate Controller's Office staffing and because addressing other problems took priority over enforcing audit requirements. Also, in some cases, Mission officials were not well-informed about audit requirements. Since not all audit requirements were met, USAID/Peru did not have the required degree of assurance of accountability for A.I.D. funds. The report recommends that USAID/Peru (1) strengthen its procedures for scheduling and using audits, (2) revise two project budgets to provide audit funding, and (3) obtain audits for three other project agreements. USAID/Peru generally agreed with the finding and had begun implementing the recommendation.

Office of the Inspector General

AUDIT OF VERIFICATION OF ACCOUNTABILITY FOR DOLLARS AND LOCAL CURRENCY ASSOCIATED WITH USAID/PERU PROGRAMS

TABLE OF CONTENTS

		Page
PART I -	INTRODUCTION	1
	A. Background	1
	B. Audit Objectives and Scope	1
PART II -	RESULTS OF AUDIT	4
	A. Finding and Recommendation	5
	1. Verification of Accountability for A.I.D. Funds Needed Improvement	5
	B. Compliance and Internal Control	11
	C. Other Pertinent Matters	13
PART III -	EXHIBIT AND APPENDICES	
	A. Exhibit	
	1. List of Agreements Reviewed	
	B. Appendices	
	1. Management Comments	
	2. Excerpts from Audit Guidance	
	3. Report Distribution	

AUDIT OF VERIFICATION OF ACCOUNTABILITY FOR DOLLARS AND LOCAL CURRENCY ASSOCIATED WITH USAID/PERU PROGRAMS

PART I - INTRODUCTION

A. Background

Officials who manage A.I.D. dollars or local currency associated with A.I.D. programs must render a full account of their activities to the public. Independent audit is an important internal control technique which serves to verify that funds are properly accounted for and used for authorized purposes. Audits of A.I.D. dollars and local currency associated with A.I.D. programs may be performed by Federal auditors, by non-Federal auditors supervised by the Office of Inspector General, or by non-Federal auditors contracted by organizations receiving assistance. The basic requirements for audit of appropriated dollars and local currency associated with A.I.D. programs are presented in appendix 2.

As of October 31, 1988, USAID/Peru was managing 39 active project agreements with obligations of $162 million. The Mission had spent $100.5 million and advanced $6.2 million under these agreements. The Mission was also monitoring 41 projects funded with local currency deposited under Public Law 480 and Section 416 food assistance programs. Local currency equivalent to approximately $3.4 million had been programmed for these projects, and the equivalent of approximately $1.5 million had been disbursed under the projects. [2]

B. Audit Objectives And Scope

The Office of the Regional Inspector General for Audit/Tegucigalpa conducted a performance audit of USAID/Peru's verification of accountability for dollars and local currency. The audit objectives were (1) to evaluate compliance with laws, regulations, and Agency guidance dealing with audit requirements and (2) to evaluate USAID/Peru's system for ensuring that audit requirements were met.

---

[2] Exchange rate used is 508 Peruvian intis to 1 U.S. dollar, the exchange rate obtained by the U.S. Embassy as of October 31, 1988 for Treasury checks sold through a bidding system.

The audit covered active A.I.D. disbursements of $100.5 million and advances of $6.2 million. The audit also covered local currency projects with the equivalent of approximately $1.5 million in disbursements. However, examinations of these disbursements and advances were limited to those required to accomplish the audit objectives.

The compliance tests performed included reviews of applicable guidance; reviews of documentation such as agreements, correspondence, audit reports, and financial records; and interviews with USAID/Peru officials. The tests covered all active USAID/Peru agreements, all agreements over $500,000 completed between January 14, 1987 and October 31, 1988, and all active local currency projects. A list of the agreements reviewed is presented in exhibit 1.

These tests were performed to determine whether:

-- pre-award surveys of prospective grant recipients were performed,

-- project papers discussed the need for audit coverage of projects,

-- project agreements included required audit provisions and budgeted funds for audit where appropriate,

-- required audits were actually performed,

-- audit reports met U.S. General Accounting Office reporting standards and included audited financial statements showing how A.I.D. funds were used,

-- USAID/Peru had copies of all audit reports and ensured that significant recommendations were implemented, and

-- USAID/Peru had reasonable assurance that audits of Public Law 480 and Section 416 local currency projects would be undertaken.

The review of internal controls covered the general and specific controls employed by USAID/Peru to ensure that audit requirements were met. These controls consisted of (1) written procedures for dealing with Inspector General staff and handling Inspector General audit reports and correspondence and (2) informal procedures for following up recommendations made by non-Federal auditors not supervised by the Inspector General's

Office. To gain an understanding of the internal control system, USAID/Peru internal directives were reviewed and management officials were interviewed. To test the effectiveness of the control system, project documentation was reviewed and project officers were interviewed.

The audit was conducted from May 16, 1989 through June 2, 1989 in Lima, Peru and covered the period from June 28, 1979 through October 31, 1988. The audit was made in accordance with generally accepted government auditing standards.

AUDIT OF VERIFICATION OF ACCOUNTABILITY FOR DOLLARS AND LOCAL CURRENCY ASSOCIATED WITH USAID/PERU PROGRAMS

PART II - RESULTS OF AUDIT

USAID/Peru was in compliance with A.I.D. guidance on audit of local currency projects. However, the Mission had not completely complied with audit requirements applicable to appropriated dollar projects. The audit disclosed instances of noncompliance with the Inspector General Act of 1978, Office of Management and Budget circulars, and A.I.D. guidance. The Mission also needed to strengthen its system for ensuring that audit requirements were met.

USAID/Peru officials pointed out that management was dealing with many other pressing matters besides enforcing audit requirements. Among the most important matters were:

-- hyperinflation and rapid devaluation of the local currency,

-- intensified terrorism by guerrilla groups in Peru,

-- the imposition of sanctions on the Government of Peru for defaulting on U.S. Government loans,

-- uncertainty over the future of the A.I.D. program in Peru, and

-- the departure of key Mission staff.

The report finding discusses instances of non-compliance with audit requirements for dollar projects. The report recommends that USAID/Peru strengthen its procedures for scheduling and using audits, revise two project budgets to provide audit funding, and obtain audits for three other project agreements.

A. Finding and Recommendation

1. Verification of Accountability for A.I.D. Funds Needed Improvement

Audit is a mandatory internal control technique which provides independent verification that all other internal control techniques, operating together, have produced the desired result: A.I.D. funds properly accounted for and used for authorized purposes. Requirements for audit of A.I.D. funds are established by law, Office of Management and Budget circulars, and internal Agency guidance. The current audit found cases where pre-award surveys were not requested and project agreements did not budget funds for audit or did not include required audit provisions. Also, several required audits were not made and the audits which were made did not meet established standards. Mission officials stated that these weaknesses existed because of inadequate Controller's Office staffing and because addressing other problems took priority over enforcing audit requirements. Also, in some cases, Mission officials were not well-informed about audit requirements. Since not all audit requirements were met, USAID/Peru did not have the required degree of assurance of accountability for A.I.D. funds.

Recommendation No. 1

We recommend that USAID/Peru:

a. assign responsibility for requesting pre-award surveys, ensuring that funds are budgeted for audit when required, ensuring that audits are performed when required, and reviewing recipient audit reports to see that they meet established standards;

b. issue a Mission Order on closeout procedures for cooperative agreements, grants, and contracts, which specifies when final audits should be requested;

c. revise the budgets for agreement numbers 527-0244 and 527-0238 to provide funding for audits; and

d. obtain audits of agreement numbers 527-0288-A-00-7305, 527-0316-G-00-7532, and 527-0221.

Discussion

Audit is a primary internal control technique, mandated by law and regulation, which serves to verify that funds are properly

accounted for and used for approved purposes. As discussed in the following sections, audit coverage of USAID/Peru's dollar portfolio was incomplete.

Pre-Award Surveys Were Not Requested

Section 4F.5.c. of Handbook 13, in discussing pre-award surveys, stated that:

> A representative of the cognizant Regional Inspector General/Audit (RIG/A) shall be requested to perform an audit of the recipient if either of the following conditions apply: (1) The total value of the proposed agreement is in excess of $250,000, or (2) The recipient hasn't received a Federal award in the last five years. The audit shall include a review of the recipient's past level of activity, its overall organization and staff, and its management capability for the purpose of assisting in the evaluation of the recipient's general business competence to carry out the proposed undertaking.

USAID/Peru had signed three agreements over $250,000 with non-governmental organizations since this guidance was issued on October 7, 1987, but had not requested pre-award surveys of any of the recipients. However, a financial review of one of the recipients was performed a few months before the agreement was signed. Mission officials were not familiar with the requirement for pre-award surveys. Not performing pre-award surveys can lead to accountability and implementation problems later on. After our audit ended, Handbook 13 was revised to give Missions more discretion on when to request pre-award surveys. USAID/Peru should still assign responsibility for requesting pre-award surveys.

Agreements Did Not Budget Funds for Audit

A.I.D. payment verification policy statement number 6 states that: "Project funds should be budgeted for independent audits unless adequate audit coverage by the host country is reasonably assured or audits by third parties are not warranted as, for example, in the case of direct A.I.D. contracts or direct placement of participants by A.I.D." Since this guidance was issued, USAID/Peru had obligated funds under nine agreements with the Government of Peru (not including limited scope grant agreements). Project funds were budgeted for audit in only three of the nine agreements. In one case, staff thought that

financial reviews could be substituted for audits. In three other cases, the host government was supposed to perform audits with its own funds but did not do so, or performed inadequate audits. Also, in one case, the project paper indicated that the planners intended to include audit funding in the agreement but the agreement only provided money for evaluations. When funds are not budgeted for audit, in our opinion, the likelihood is that audits will not be made. Several of the agreements which did not budget funds for audit have ended or are nearing completion, so no corrective action was needed. However, USAID/Peru should budget funds for audits of agreement numbers 527-0244 and 527-0238 to comply with payment verification policy statement number 6.

Two Agreements Did Not Include Required Audit Provisions

Handbook 13 contains standard provisions dealing with audit and other matters which must be included in agreements with non-governmental organizations. Of the 22 agreements with non-governmental organizations reviewed, 2 included incorrect standard provisions. Also, we could not tell whether the correct standard provisions were included in eight agreements because the Mission did not have copies of the agreements with the standard provisions attached and the grant letters themselves did not specify which provisions were attached.

One of the two agreements which included incorrect standard provisions used a limited scope grant agreement form which should only be used for agreements with foreign governments. The Mission had planned to sign the agreement with the Government of Peru, but the government was unable to sign the agreement within A.I.D.'s three day window for signing agreements. The Mission found a private entity which could implement the project, but there was no time to re-draft the agreement using the correct form before the signing. Since this agreement has since ended, no corrective action was needed.

The other agreement was signed on June 24, 1987 but incorporated standard provisions which were superseded on January 1, 1987. This oversight did not affect audit requirements since the agreement's program description required that annual audits be performed. Nor, as far as we could determine, did this error harm the U.S. Government's interests in any other way, since the provisions that were incorporated in the agreement were actually more stringent than those that should have been incorporated. Accordingly, we are not making a recommendation, although

USAID/Peru may still wish to amend this agreement to incorporate the correct standard provisions.

Audits of Active Agreements Were Not Performed

Ten active agreements required audits to be performed before the time of our audit. (The other agreements reviewed either did not require audits or required them to be performed sometime in the future.) Audits were performed when required for only four of the ten agreements. No audits at all were performed for three agreements, mainly because Mission officials had thought that financial reviews could be substituted for audits. The other three agreements required that audits be performed "regularly," but from five and a half to seven years had passed before the first audit was performed. The project officers did not know why audits were not done sooner. USAID/Peru should obtain audits of the three agreements that had not been audited and assign responsibility for ensuring that audits are made when required.

Final Audits Were Not Requested

A.I.D. Contract Information Bulletin No. 87-5, dated January 14, 1987, requires A.I.D. Missions to establish formal closeout procedures for contracts, grant, and cooperative agreements. The model procedures attached to the bulletin require final audits of cost reimbursement contracts and assistance agreements over $500,000. Since this guidance was issued, two assistance agreements over $500,000 had been completed, but USAID/Peru had not requested final audits of either agreement. (No cost-reimbursement contracts over $500,000 had been completed since the guidance was issued.) The project officers for these agreements were not aware of the requirements for final audits because USAID/Peru had not established formal closeout procedures. Final audit is an important means of ensuring that A.I.D. only pays for reasonable and necessary costs. USAID/Peru should issue a Mission Order on closeout procedures which specifies when final audits should be requested.

Audit Reports Did Not Meet Established Standards

Office of Management and Budget Circular A-73 states that:

> Primary responsibility for audits of federally assisted programs rests with recipient organizations. * * * Federal agencies will rely on recipient audits, provided they are made in accordance with the audit

> standards issued by the Comptroller General and otherwise meet the requirements of the Federal agencies.

The Inspector General Act of 1978 makes Inspectors General responsible for providing policy direction for audits of their agencies. The A.I.D. Inspector General has delegated this responsibility for the Latin America and Caribbean Bureau to the Regional Inspector General for Audit/Tegucigalpa (RIG/A/T). RIG/A/T's policy on recipient audits was communicated in Tegucigalpa 21183, dated December 23, 1987. The policy states, in part, that:

> * * * [H]ost government audits or host government contracted audits that either (1) do not certify an accountability for A.I.D. funds or (2) do not meet the basic audit standards of the U.S. Comptroller General are inadequate for A.I.D. audit purposes and do not meet the requirements for audits in project agreements.

This policy is consistent with A.I.D. payment verification policy statement number 6, which requires A.I.D. Missions to evaluate the adequacy of host government audit coverage.

We reviewed six audit reports which were contracted by organizations receiving A.I.D. assistance and which were relied on by USAID/Peru as meeting the audit requirements included in project agreements. None of these audit reports met established standards. While two of the reports showed how A.I.D. funds were used, none of them met General Accounting Office reporting standards. Two of the reports did not present the results of the auditors' internal control review, three of the reports did not include positive assurance on compliance, and none of the reports provided negative assurance on compliance. (Positive assurance is a statement that, for the items tested by the auditors, the auditee either did or did not comply with applicable laws and regulations. Negative assurance is a statement that nothing came to the auditors' attention that would indicate that untested items were not in compliance with applicable laws and regulations.) No office or individual in USAID/Peru reviewed audit reports to ensure that they met established standards. When audit reports do not meet these standards, they do not provide management the required level of assurance that A.I.D. funds are properly accounted for and used for approved purposes. USAID/Peru should assign responsibility

for reviewing audit reports to see that they meet established standards.

In conclusion, the current audit found instances of non-compliance with audit requirements in the six areas discussed above. Other internal control techniques employed by the Mission (e.g., project officer monitoring, voucher review procedures, evaluations, and financial reviews) can compensate somewhat for weak compliance with audit requirements. However, only audit can provide management independent verification that all other internal controls, operating together, have produced the desired result: A.I.D. funds properly accounted for and used for authorized purposes. USAID/Peru needed to strengthen its procedures for scheduling and using audits, revise the budgets for two agreements to provide audit funding, and obtain audits of three agreements. While determining the adequacy of Controller's Office staffing was outside the scope of our audit, we believe that implementing these recommendations will substantially increase the workload in the Controller's Office.

Management Comments

USAID/Peru generally agreed with the finding and had begun implementing the recommendation. The Mission requested that audits of two agreements be included in RIG/A/T's fiscal year 1990 audit plan.

Office of Inspector General Comments

All parts of the recommendation are resolved and may be closed when the actions described in USAID/Peru's comments have been completed. We have included agreement numbers 527-0316-G-00-7532 and 527-0221 in our 1990 non-Federal audit plan. USAID/Peru will need to provide funding to accomplish these audits.

B. Compliance and Internal Control

1. Compliance

The compliance tests performed included reviews of applicable guidance; reviews of documentation such as agreements, correspondence, audit reports, and financial records; and interviews with USAID/Peru officials. The tests covered all active USAID/Peru agreements, all agreements over $500,000 completed between January 14, 1987 and October 31, 1988, and all active local currency projects.

These tests were performed to determine whether:

-- pre-award surveys of prospective grant recipients were performed,

-- project papers discussed the need for audit coverage of projects,

-- project agreements included required audit provisions and budgeted funds for audit where appropriate,

-- required audits were actually performed,

-- audit reports met U.S. General Accounting Office reporting standards and included audited financial statements showing how A.I.D. funds were used,

-- USAID/Peru had copies of all audit reports and ensured that significant recommendations were implemented, and

-- USAID/Peru had reasonable assurance that audits of Public Law 480 and Section 416 local currency projects would be undertaken.

The compliance tests disclosed several instances of non-compliance with audit requirements for appropriated dollar projects. First, USAID/Peru had not requested pre-award surveys of grant recipients as required by section 4F.5.c. of A.I.D. Handbook 13. Second, project funds were not always budgeted for audit as required by A.I.D.'s payment verification policy statement No. 6. Third, two project agreements did not include audit provisions mandated by A.I.D. Handbook 13. Fourth, several audits required by A.I.D. guidance or the project agreements themselves were not requested or performed. Fifth, the audits that were performed did not meet General Accounting

Office auditing standards, as required by the Inspector General Act of 1978, Office of Management and Budget Circular No. A-73, and policy issued by the Regional Inspector General for Audit/Tegucigalpa. Finally, USAID/Peru lacked a formal system for following up audit recommendations, although no cases were found where significant audit recommendations were not followed up. Office of Management and Budget Circular No. A-50 requires Federal agencies to establish formal systems to ensure the prompt resolution and implementation of audit recommendations. These instances of non-compliance are discussed in detail in the report finding.

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

2. Internal Control

The review of internal controls covered the general and specific controls employed by USAID/Peru to ensure that audit requirements were met. These controls consisted of (1) written procedures for dealing with Inspector General staff and handling Inspector General audit reports and correspondence and (2) informal procedures for following up recommendations made by non-Federal auditors not supervised by the Inspector General's Office. To gain an understanding of the internal control system, USAID/Peru internal directives were reviewed and management officials were interviewed. To test the effectiveness of the control system, project documentation was reviewed and project officers were interviewed.

The major weaknesses disclosed by the internal control review were that the Mission did not systematically ensure that (1) funds for audit were budgeted when appropriate, (2) audits were performed when required, and (3) audit reports met established requirements. These weaknesses are discussed in more detail in the report finding.

C. Other Pertinent Matters

The following sections discuss four other pertinent matters which came to our attention.

No Formal System for Monitoring Implementation of Recommendations Existed

USAID/Peru's Controller's Office kept complete files on audit reports issued by the Inspector General's Office which showed the status of open recommendations and the actions taken to implement recommendations. However, no formal system existed for following up recommendations from audits performed or contracted by recipient organizations. We reviewed three recipient audit reports and found that the Mission had followed up on the significant recommendations. Still, in our judgment, the absence of a formal followup system created a significant risk that recommendations might not be implemented and that management would not be aware that they had not been implemented. The controller was aware of the need for a more formal followup system but stated that he had not been able to implement such a system due to the departure of key staff from his office. While we are not making a formal recommendation, USAID/Peru should implement a formal system for monitoring the status of significant recommendations from recipient audit reports.

A.I.D. Agreements Do Not Require Compliance with General Accounting Office Auditing Standards

The standard provisions for A.I.D. assistance agreements help ensure that only responsible organizations receive assistance from A.I.D. They do not, however, require the use of General Accounting Office (GAO) auditing standards. The Inspector General Act of 1978, Office of Management and Budget Circular No. A-73, and policy issued by the Regional Inspector General for Audit/Tegucigalpa require that audits of federally-assisted programs be made in accordance with GAO standards.

We believe that compliance with GAO standards is an achievable goal in Peru. The Controller General of Peru has adopted the standards issued by the American Institute of Certified Public Accountants (AICPA), and the College of Public Accountants has adopted auditing standards similar to those issued by the AICPA. GAO standards incorporate AICPA standards and also contain requirements unique to audits of Federal programs. These additional requirements, while important, are no more difficult to meet than those imposed by AICPA standards.

We may recommend in a future audit report that A.I.D./Washington modify the standard provisions for A.I.D. agreements to require the use of GAO auditing standards.

Refund Provision for Agreements with Non-Governmental Organizations May Need Revision

Audits sometimes show that recipients have used A.I.D. funds for unauthorized purposes or cannot account for them. Obviously, A.I.D. should obtain refunds when funds are used for unauthorized purposes. It should also obtain refunds when recipients cannot demonstrate to A.I.D.'s satisfaction that funds were used for intended purposes. This right is protected by the standard refund provision for government-to-government agreements, which states that:

> In the case of any disbursement which is not supported by valid documentation in accordance with this agreement, or which is not made or used in accordance with this Agreement, or which was for goods and services not used in accordance with this agreement, A.I.D. * * * may require the cooperating country to refund the amount of such disbursement to A.I.D. in U.S. dollars to A.I.D. * * *.

In contrast, however, the standard refund provision for non-governmental grantees (both U.S. and non-U.S.) does not afford A.I.D. the same level of protection. It states that:

> If, at any time during the life of the grant, or as a result of final audit, it is determined by A.I.D. that funds it provided under this grant have been expended for purposes not in accordance with the terms of the grant, the grantee shall refund such amount to A.I.D.

In order to obtain a refund from a non-governmental organization, then, A.I.D. must be able to determine for what purposes its funds were used. This could be impossible when documentation is inadequate or non-existent.

We may recommend in a future audit report that A.I.D./Washington modify this standard provision to read as follows:

> If, at any time from the effective date of the grant until three years after the termination date, or as a result of a final audit, it is determined by A.I.D. that grant funds were expended for purposes not in

accordance with the terms of the grant, the grantee shall refund such amount to A.I.D. Any expenditure of grant funds not supported by adequate documentation will be disallowed and a refund of such amount may be sought by A.I.D.

Government Audit Provision Does Not Specify Frequency of Audits

The standard audit provision for agreements with foreign governments requires the host government to maintain accounting books and records and provides that "* * * such books and records will be audited regularly * * *." This phrase is ambiguous because it does not specify the interval at which audits should be made. This is surprising since the standard provisions for U.S. non-governmental grantees require audits at least every two years, and the standard provisions for non-U.S., non-governmental grantees require annual audits. Also, audits of state and local governments in the United States (in some ways analagous to audits of foreign governments) are required to be made annually by the Single Audit Act of 1984 (Public Law 98-502). We may recommend in a future audit report that A.I.D./Washington modify the standard audit provision for government-to-government agreements to specify how frequently audits must be conducted.

AUDIT OF VERIFICATION OF ACCOUNTABILITY FOR DOLLARS AND LOCAL CURRENCY ASSOCIATED WITH USAID/PERU PROGRAMS

PART III - EXHIBIT AND APPENDICES

16

LIST OF AGREEMENTS REVIEWED

	Agreement Number	Pre-Award Survey Required But Not Requested	Government-to-Government Agreements Did Not Budget Funds for Audit	Incorrect Standard Provisions Used	Audits Required But Not Performed	Audit Reports Did Not Meet Standards
	Agreements with Non-Governmental Organizations					
1.	527-0230-CA-00-4105					
2.	527-0247					
3.	527-0248					
4.	527-0308-G-00-6583					
5.	527-0309-G-00-6782					
6.	527-0328-G-00-8403	X				
7.	527-0323-G-00-8443	X				
8.	527-0330-G-00-8378	X				
9.	936-5542 (Benthic Resources Research)			X		
10.	527-0317-G-00-7833					
11.	527-0288-A-00-7305			X	X	
12.	527-0298-G-00-5123					
13.	527-0298-G-00-6585					
14.	527-0272-A-00-5139					
15.	527-0261					
16.	527-0269-A-00-6753					X
17.	527-0294-G-00-5111					
18.	527-0311-G-00-6571					
19.	527-0316-G-00-7532				X	
20.	527-0320-G-00-8157					
21.	598-0640-CA-00-5132					
22.	598-0640-A-00-6535					
	Government-to-Government Agreements					
23.	527-0303					
24.	527-0318					
25.	527-0298					
26.	527-0288 (Ministry of Health)					

17

	Agreement Number	Pre-Award Survey Required But Not Requested	Government-to-Government Agreements Did Not Budget Funds for Audit	Incorrect Standard Provisions Used	Audits Required But Not Performed	Audit Reports Did Not Meet Standards
27.	527-0288 (Ministry of Education)					
28.	527-0178				X	
29.	527-0192		X		X	X
30.	527-0321		X			
31.	527-0238		X		X	X
32.	527-0282					
33.	527-0226		X			X
34.	527-0244		X			X
35.	527-0265					X
36.	527-0221		X		X	
37.	527-0285					
38.	598-0640					
39.	598-0622					
	Agreements with Non-Governmental Organizations Completed from 1/14/87 through 10/31/88					
40.	527-0231				X	
41.	527-0293				X	

Exhibit 1
Page 2 of 2

OPTIONAL FORM NO. 10
MAY 1962 EDITION
GSA FPMR (41 CFR) 101-11.6

UNITED STATES GOVERNMENT

Memorandum

TO : Mr. Coinage N. Gothard, Jr.
RIG/A/Tegucigalpa

DATE: August 25, 1989

FROM : Craig G. Buck, Mission Director
USAID/Peru

SUBJECT: Response to Draft Audit Report on Mission Responsibility for Audits

REF : Draft of Audit Verification of Accountability for Dollars and Local Currency Associated with USAID/Peru Programs

The Mission is in basic agreement with the findings of the report. However, as discussed during the Exit Conference, the statement presented on page iii of the Executive Summary and again on page 7 of the Part II, Results of Audit, which states "Since not all audit requirements were met, USAID/Peru did not have adequate assurance of accountability of A.I.D. funds.", is a very broad and potentially misleading statement. Although the statement may be correct on an academic basis, it does not address the materiality of the audit requirements that were not met and, therefore, the degree of the effects on the overall accountability of A.I.D. funds. The Mission recommends that this broad general statement be either eliminated or clarified.

We are in the process of implementing the recommendations presented.

Recommendation No. 1(a) reads:

> Assign the Controller's Office responsibility for requesting pre-award surveys, ensuring that funds are budgeted for audit when required, ensuring that audits are performed when required, reviewing recipient audit reports to see that they meet established standards, and implementing a formal system for monitoring the status of open audit recommendations and ensuring that recommendations are implemented.

The Controller has been charged with the activities listed in the foregoing paragraph and is in the process of updating existing Mission procedures to fully respond to the requirements. A Mission Order establishing a system for monitoring audit recommendations is being revised and infrastructure developed to ensure adequate follow-up. We expect that a revised Mission Order will be issued within 45 days, advising the USAID Project Managers of the system's requirements. The Controller will report on recommendation implementation, but the responsibility for the action will rest with the relevant USAID Office Chiefs and Project Managers.

Buy U.S. Savings Bonds Regularly on the Payroll Savings Plan

The Controller will ensure that the Mission requests pre-award surveys in accordance with Handbook 13, revision effective June 6, 1989. The Project Managers will ensure that project budgets include funding for audits and are performed when required. The Controller will monitor and report on this process.

Recommendation No. 1(b) reads:

> Issue a Mission Order on close-out procedures for cooperative agreements, grants, and contracts, which specifies when final audits should be requested.

The Project Development Officer of the Program Office will develop a Mission Order within 60 days that will fully address close-out procedures and assign responsibilities for required actions.

Recommendation No. 1(c) reads:

> Revise the budgets for agreement numbers 527-0244 and 527-0238, to provide funding for audits.

The Upper Huallaga agreement number 527-0244 has funding included for audit (PIL No. 80, dated June 19, 1989) and a PIO/T request will be forthcoming within 90 days. The APID agreement will be amended to include funds for audit. This will be for a final audit in late 1990, as a Financial Review has been contracted and will begin before the end of August, 1989.

Recommendation No. 1(d) reads:

> Obtain audits of agreements numbers 527-0288-A-00-7305, 527-0316-C-00-7532, and 527-0221.

Agreement 0288 - Narcotics Education and Awareness (CEDRO): The need for audit will be discussed with the Grantee and the request will be forthcoming within 90 days.

Agreement 0221 - Rural Water Supply (PACD: 06/30/89): There remain no funding possibilities within the Agreement. The last remaining action is the project completion reporting.

Agreement 0316 - PRISMA Child Survival. The PACD for this project has been extended to 09/30/89. There are no funds available to meet the audit requirement.

Inasmuch as there are no funds available for final audits of Agreements 0221 and 0316, we recommend that the audit of these two Agreements be included on the FY-90 audit schedule. Should RIG/A/T not be able to include the audit in their own audit plan, and if RIG/A/T considers these audits as essential, the Mission shall make PD&S funds available for this purpose.

The Mission will have all current agreements with non-governmental organizations reviewed to ensure that the correct Standard Provisions are included. This will be done by September 30, 1989 (pages 10 and 11 of Draft Report).

Finally, recent discussions with the Ministry of Economy and Finance, Director General of the Budget, have resulted in an agreement that the Comptroller General of Peru will audit bilateral agreements at least every two years. We will try to include GAO audit standards also. PL-480 Title I generations will be made available to finance the audits, if required. Such budgeting provision will be made for calendar (FY) 1990. (See pages 10, 13, 20 and 22 of the Draft Report.)

EXCERPTS FROM AUDIT GUIDANCE

Excerpts from the Inspector General Act of 1978, as amended on December 29, 1981

Sec. 4.(a) It shall be the duty and responsibility of each Inspector General, with respect to the establishment within which his Office is established -

(1) to provide policy direction for and to conduct, supervise, and coordinate audits and investigations relating to the programs and operations of such establishment * * *.

(b) In carrying out the responsibilities specified in subsection (a) (1), each Inspector General shall -

(1) comply with standards established by the Comptroller General of the United States for audits of Federal establishments, organizations, programs, activities, and functions;

(2) establish guidelines for determining when it shall be appropriate to use non-Federal auditors; and

(3) take appropriate steps to assure that any work performed by non-Federal auditors complies with the standards established by the Comptroller General as described in paragraph (1).

Excerpts from Office of Management and Budget Circular A-73, revised June 20, 1983

Agencies are responsible for providing adequate audit coverage of their programs as an aid in determining whether information is reliable; resources have been safeguarded; funds have been expended in a manner consistent with related laws, regulations, and policies; resources have been managed economically and efficiently; and desired program results have been achieved. Audits of Federal organizations, programs, activities and functions, State and local governments (as required by Circular A-102, "Uniform requirements for grants to State and local governments"), and others (as required by Circular A-110, "Uniform

requirements for grants to universities, hospitals, and other non-profit organizations") will be made in accordance with the standards issued by the Comptroller General * * *.

Primary responsibility for audits of federally assisted programs rests with recipient organizations * * *. Federal agencies will rely on recipient audits, provided they are made in accordance with the audit standards issued by the Comptroller General and otherwise meet the requirements of the Federal agencies. Federal agencies may perform additional audit work building on audit work already performed.

Excerpt from A.I.D.'s Supplemental Guidance on Programming Local Currency, dated October 21, 1987

If A.I.D. should choose to directly associate jointly programmed local currency with host government projects or private sector activities, the Mission should have reasonable assurance that * * * periodic audits of relevant activities will be undertaken.

APPENDIX 3

REPORT DISTRIBUTION

	No. of Copies
Director, USAID/Peru	5
AA/LAC	2
LAC/DR	1
LAC/DP	1
LAC/SAM/BP	1
LAC/CONT	1
LAC/GC	1
RLA	1
AA/XA	2
XA/PR	1
LEG	1
GC	1
AA/M	2
PFM/FM/CAD	2
PPC/CDIE	3
AA/PPC	2
AA/PFM	2
M/SER/PPE	1
PFM/FM/CONT	1
IG	1
AIG/A	1
IG/PPO	2
IG/LC	1
IG/ADM/C&R	12
IG/I	1
RIG/I/T	1
Other RIG/As	1