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**AUDIT OF USAID/NICARAGUA'S
ECONOMIC SUPPORT FUND PROGRAM
MAY 31, 1990 TO NOVEMBER 30, 1990**

**Audit Report No. 1-524-91-32-N
May 24, 1991**

AGENCY FOR INTERNATIONAL DEVELOPMENT

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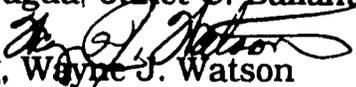
OFFICE OF THE REGIONAL INSPECTOR GENERAL
AMERICAN EMBASSY
TEGUCIGALPA - HONDURAS

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May 24, 1991

MEMORANDUM

TO: D/USAID/Nicaragua, Janet C. Ballantyne

FROM: RIG/A/T Acting,  Wayne J. Watson

SUBJECT: Audit of USAID/Nicaragua's Economic Support Fund Program, May 31, 1990 to November 30, 1990

This report presents the results of a non-Federal financial audit of the Economic Support Fund Program for Nicaragua for the period May 31, 1990 to November 30, 1990. The report includes audit coverage of funding provided under the Economic Recovery Program I (USAID/Nicaragua Project No. 524-0300); the Technical Assistance and Training Project (USAID/Nicaragua Project No. 524-0301.1); the American Institute for Free Labor Project (USAID/Nicaragua Project No. 524-0308); and the Salesian Vocational Education Project (USAID/Nicaragua Project No. 524-0310). The accounting firm of Price Waterhouse prepared the report which is dated March 20, 1991.

The Economic Support Fund Program for Nicaragua was funded under the Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act which included \$300 million in Economic Support Funds to support Nicaragua's economic recovery. The program includes cash transfer assistance for balance of payments/budget support as well as developmental assistance. The audit coverage included \$60 million of cash transfers and \$687,537 for developmental assistance.

The objectives of the audit were to determine whether: (1) the Government of Nicaragua and the implementing entities' fund accountability statement presents fairly the locally executed program receipts and disbursements for the period audited, (2) the internal control structures of the implementing entities were adequate to manage the program activities, and (3) the implementing entities have complied with the terms of the agreements and applicable laws and regulations which may affect the program's goals and incurred costs. The scope of the audit consisted of reviewing the grant agreements and various documents and regulations governing the program; evaluating the Government of Nicaragua's and

the implementing entities' compliance with the agreement terms and applicable laws and regulations; examining the Government of Nicaragua's and the implementing entities' fund accountability statement and related support; and reviewing and evaluating the Government of Nicaragua's and the implementing entities' internal control structure.

Price Waterhouse found that with the exception of questionable costs of \$843,236 (all questioned), the fund accountability statement fairly presents, in all material respects, the locally executed receipts and disbursements for program activities managed by the Government of Nicaragua and the implementing entities for the audit period. The auditors also identified questionable committed grant funds totaling \$532,106 (\$344,050 unsupported). The auditors found material weaknesses in the internal control structure of the Central Bank of Nicaragua, the implementing entity that administers the cash transfer payments. The Bank lacked controls in financial reporting, documentation of use of competitive bidding, and monitoring of program transactions. With respect to compliance the auditors found the Bank complied, in all material respects, with agreement terms and applicable laws and regulations.

The audit report was discussed with the Vice-President of Internal Control of the Central Bank of Nicaragua who generally agreed with its contents.

We are including the following recommendations in the Office of the Inspector General's audit recommendation follow-up system:

Recommendation No. 1

We recommend that USAID/Nicaragua negotiate a settlement with the Central Bank of Nicaragua for questionable costs totaling \$1,375,342 included in the Price Waterhouse audit report dated March 20, 1991. The questionable costs consist of \$1,031,292 of ineligible costs and \$344,050 of unsupported costs. Included in the total questionable costs are \$532,106 of funds that have been committed but not yet paid.

Recommendation No. 2

We recommend that USAID/Nicaragua ensure that the Central Bank of Nicaragua develops improved internal control procedures in the areas of financial reporting, documentation of use of competitive bidding procedures, and monitoring program transactions.

Please advise this office within 30 days of actions planned or taken to resolve and close the recommendations.

FINANCIAL AUDIT OF THE FISCAL YEAR 1990
ECONOMIC SUPPORT FUND (ESF) PROGRAM FOR
NICARAGUA FOR THE PERIOD
MAY 31 TO NOVEMBER 30, 1990

* * *

MARCH 20, 1991

FINANCIAL AUDIT OF THE FISCAL YEAR 1990
ECONOMIC SUPPORT FUND (ESF) PROGRAM FOR
NICARAGUA FOR THE PERIOD
MAY 31 TO NOVEMBER 30, 1990

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Price Waterhouse

March 20, 1991

Mr. Reginald Howard
Regional Inspector General for
Audit (RIG/A/T)
U.S. Agency for International
Development
Tegucigalpa, Honduras, C. A.

Dear Mr. Howard:

This report presents the results of our audit of the Economic Support Fund (ESF) Program for Nicaragua for the period May 31, to November 30, 1990.

BACKGROUND

On May 25, 1990, the President of the United States signed into law the Fiscal Year (FY) 1990 Dire Emergency Supplemental Appropriations Act which included US\$300.0 million in Economic Support Funds (ESF) to support Nicaragua's economic recovery. The program included two major categories of assistance:

- a. Cash transfer assistance for balance of payments/budget support to assist in implementing a rational economic program to stabilize and reactivate the Nicaraguan economy.
- b. Disbursements over a longer period of time in support of the new government's economic recovery and social programs.

The initial cash transfer assistance provided under the program was for the purpose of financing essential commodities primarily for the private sector, such as petroleum, agricultural inputs (excluding pesticides), spare parts, intermediate goods, capital goods, and other imports needed to keep the economy functioning.

The principal Nicaraguan Government entity involved in the cash transfer portion of the assistance is the Central Bank of Nicaragua. Other entities, some of which are headquartered outside Nicaragua, will be involved in the implementation of individual development projects.

1

On May 31, 1990, a grant agreement was signed for the Economic Stabilization and Recovery Program, USAID/Nicaragua Project No. 524-0300, to finance critical commodity imports under the responsibility of the Central Bank of Nicaragua (BCN). On June 4, 1990, \$60.0 million was disbursed to an account established with the Federal Reserve Bank of New York in the name of BCN.

On September 26, 1990, a second grant agreement was signed for the Economic Stabilization and Recovery Program, USAID/Nicaragua, Project No. 524-0311 under which \$68.0 million of commodity imports and \$50.0 million for the repayment of debt to the World Bank and the Inter-American Development Bank were authorized.

Out of nine development projects originally identified by USAID/Nicaragua the following four had reached the agreement stage by November 30, 1990:

1. Economic Growth and Development - This project provides \$32.3 million for various economic and social recovery subprojects of an emergency nature. These include:

a. Technical Assistance and Training - On June 4, 1990, USAID/Nicaragua signed with the Central American Institute of Business Administration (INCAE) a cooperative agreement for \$1.1 million. The purpose of this agreement was to assist INCAE in its efforts to provide technical assistance to the Government of Nicaragua and training to both the public and private sectors. This assistance will support the highest priorities of the new government, including the government's macroeconomic program which aims to promote short and long-term economic recovery within the framework of a market oriented economic system.

b. Employment Generation - The purpose of this \$10.0 million project is to utilize a portion of Nicaragua's unemployed to work on the repair of basic infrastructure. The project will be implemented through the National Institute for Municipal Development (INIFOM), which represents Nicaragua's 143 municipalities.

Working closely with the municipalities, INIFOM will execute contracts with private sector entities for the repair and maintenance of local infrastructure. To meet stated project objectives, INIFOM will receive technical assistance to ensure proper administration of project funds.

c. Public Sector Support - This \$5.0 million grant, signed on September 25, 1990 will provide commodities - office equipment, including computers, typewriters, desks, etc.,

and a vehicle for several ministries and government offices. Except for furniture all procurement must be of U. S. source and origin.

- d. Community Hospitals - OPG with Project HOPE - An agreement for \$2.5 million to provide support to four community hospitals in Nicaragua to improve the quality of care by funding supplies and medicines, promoting an interchange program of medical specialists from both within and outside Nicaragua, and securing certain training. Project HOPE has agreed to make a counterpart contribution of medicines worth at least \$3.5 million.
 - e. Textbooks under the Regional Technical Aid Center (RTAC II) - this regional project has the objective of increasing the availability and use of U. S. technical books and materials in Spanish to university students and development professionals in Central America. With regards to Nicaragua, the project aims at: a) provide spanish language primary and secondary school textbooks to the Ministry of Education (approximately 6,200,000 books over the life of the project); and b) provide technical assistance and services to university bookstores, the Ministry of Education, and USAID/Nicaragua.
2. AIFLD-CUS - This grant of \$700,000 to the American Institute for Free Labor Development (AIFLD) will support a program of the Confederation of Labor Unity (CUS) and other independent democratic unions for the planning of leadership roles in Nicaragua's organized labor movement. More specifically the grant will fund technical assistance to CUS and other independent labor unions; training, workshops and activities for union members; institutional strengthening for independent labor unions; and administrative and institutional financing of AIFLD.
 3. NED - Delphi International - This \$235,000 grant to the National Endowment for Democracy will fund the costs of purchasing and shipping a new transmitter, communications tower, and studio equipment that will enable Radio Corporation to resume its country-wide operations as soon as possible, and function as a forum for free discussion and the advancement of democratic ideas.
 4. Nor. - Formal Vocational Education - This \$1.7 million grant to be administered by the Salesian Society's Centro Juvenil Don Bosco, provides resources for vocational training through six schools located in Managua, Granada and Masatepe. The funds will be used for: a) vocational training materials and support

for education in moral, civic and democratic values; b) pay part-time instructors and auxiliary personnel; c) purchase equipment, tools and supplies, and d) remodel some shops and classrooms.

AUDIT OBJECTIVES

The general objective of this work is to audit the Fiscal Year 1990 Economic Support Fund (ESF) Program for Nicaragua as of November 30, 1990. The specific objectives of the financial audit were to determine whether:

- a. The fund accountability statement presents fairly the financial activities of the Program incurred within Nicaragua as of November 30, 1990 and costs reported as incurred were allowable, allocable and reasonable in accordance with the terms of the agreements and applicable laws and regulations;
- b. The internal control structures of the implementing entities are adequate to manage the program's operations; and
- c. The implementing entities have complied with the terms of the agreements and applicable laws and regulations which may affect the program's goals and incurred costs.

SCOPE OF WORK

To meet stated audit and review objectives, our work included the following:

a. Preliminary steps -

Review the following documents to become familiar with the program:

1. Program Assistance and Approval Document (PAAD) for USAID/Nicaragua's Program No. 524-0300 and PAAD for Program No. 524-0311.
2. Grant Agreements - Economic Stabilization and Recovery Programs I and II, AID Program No. 524-0300 and 524-0311 with Project Implementation Letters (PILs), if any, and relevant correspondence.
3. State Cable 194322 - Subject: Financial Management Guidance on Dollar Separate Account for ESF Cash Transfers and ESF, DA and DFA Funded Non-Project Sector Assistance Cash Disbursements.
4. Nicaragua Economic Stabilization and Recovery Program I Separate Account Operating Procedures, Project No. 524-0300, June 1, 1990.

5. Internal Control Assessment - Central Bank of Nicaragua, May 11, 1990, Controller's Office USAID/Nicaragua.
 6. Programa de Estabilización y Recuperación Económica, Proyecto 524-0300, Reporte Financiero No. 90-48 (borrador) del 25 de septiembre de 1990, Controller's Office USAID/Nicaragua.
 7. A.I.D. Commodity Eligibility Listing (1989 Edition).
 8. Cooperative Agreement No. 524-0301-CA-90-01, dated June 4, 1990, with the Central American Institute of Business Administration (INCAE).
 9. Amendment No. 10, dated June 19, 1990, to Contract No. LAC-0011-C-00-6081-10 with Aguirre International, San Mateo, California (buy-in for RTAC-II under Project No. 524-0301).
 10. Office of Management and Budget (OMB) Circulars A-122 and A-110.
 11. Mandatory Standard Provisions for both U.S. and Non-U.S., Non-Governmental Grantees.
 12. A.I.D. Handbooks 3 (Project Assistance) 11 (Host Country Contracts), and 13 (Grants).
 13. Contracts and subcontracts with third parties, as applicable.
 14. File documentation maintained in USAID/Nicaragua Controller's Office regarding the procedures and status of the \$60.0 million commodity import assistance (524-0300) and each of the existing project agreements under the program.
- b. Financial audit of the program's local execution/disbursements -
1. Examine the fund accountability statement for the overall local execution of the program from inception to November 30, 1990. Our work included the evaluation of program implementation actions and accomplishments to determine if commodities had been properly managed and costs reported as incurred were allowable, allocable, and reasonable under the terms of the agreements.

Although that was not the purpose of our financial audit, we were alert to situations or transactions that would be indicative of fraud, abuse or illegal expenditures or acts.

2. Evaluate the implementing entities' internal control structure as considered appropriate. For this purpose we conducted compliance and substantive tests to determine the extent to which established procedures and controls were functioning as intended and the adequacy of the accounting and information systems, procurement procedures and practices, inventory controls, bank account controls, and controls to assure that charges to the projects and programs were proper and adequately documented.

In fulfilling the audit requirements relating to an understanding of the internal control structure and assessing risk, we followed the guidance contained in applicable AICPA Statements on Auditing Standards. Therefore our work included:

- a. Obtaining sufficient understanding of the internal control structure of each implementing entity to plan the audit and to determine the nature, timing, and extent of other tests; and
 - b. Obtaining sufficient understanding of policies and procedures that pertain to the implementing entities' ability to record, process, summarize, and report financial data consistent with the assertions of management in the fund accountability statements.
3. Evaluate whether the Government of Nicaragua (GON) and the implementing entities complied with the terms of the agreements and with applicable laws and regulations.

RESULTS OF AUDIT

Fund Accountability Statement

Except for the effects of the matters mentioned in the following paragraph, the fund accountability statement examined by us presents fairly, in all material respects, the cash receipts and the locally made disbursements of the FY 1990 ESF Program for Nicaragua for the period May 31 to November 30, 1990.

As further described in Note 3 to the fund accountability statement, disbursements amounting to \$843,236 have been questioned for the reasons explained therein. In addition, our work disclosed that funds already committed under the program for a total of \$532,106, if paid with grant funds, should also be questioned for the same or similar reasons, also explained in Note 3.

Internal Control Structure

Our evaluation of the internal control structure of the program implementing units disclosed certain reportable conditions which are summarized as follows:

Central Bank of Nicaragua -

- The monthly financial reports figures submitted to USAID/Nicaragua were not supported nor reconciled with the accounting records.
- The letter of credit files did not contain complete and sufficient documentation to demonstrate the application of competitive bidding procedures.
- There was lack of appropriate and formally defined follow-up and monitoring procedures over Program transactions. These responsibilities had not been assigned to a special control unit.

American Institute for Free Labor Development (AIFLD) -

- The documentation on file did not include reconciliations of all advances received from the central office.
- Fund advances with more than 60 days were not liquidated opportunely.
- Fund advances liquidation were not reflected opportunely in the accounting records.

The Salesian Society (Centro Juvenil Don Bosco) -

- The accounting system does not allow for the immediate and easy identification of expenditures by line item.
- The local office does not have financial accounting and administrative procedures manuals to be used as guidance for the recording of fixed assets and transactions paid for with USAID supplied funds.
- Checks are issued to the name of the project coordinator who cashes them and makes cash payments directly, instead of issuing checks payable to the intended beneficiaries.

Compliance with Agreement Terms and Applicable Laws and Regulations

Our tests for compliance with agreement terms and applicable laws and regulations disclosed the following conditions:

Central Bank of Nicaragua (BCN) -

- a. Not all necessary documents in support of disbursements were maintained by BCN, in contravention of section IV.B.1.2. of the approved procedures;
- b. Certain documents related to import permits and liquidations, as well as certificates of origin and source required by section IV.B.1 of the approved procedures, were not on file.

MANAGEMENT COMMENTS

At an exit conference held on March 20, 1991, at which Ms. Maria Elena Flores representing the Office of the Regional Inspector General for Audit (RIG/A/T) was in attendance, Mr. Ramiro Balladares, Vice-president of Internal Control of the Central Bank of Nicaragua, expressed general agreement with the findings and conclusions of the audit report.

Rance Witzhose

Price Waterhouse

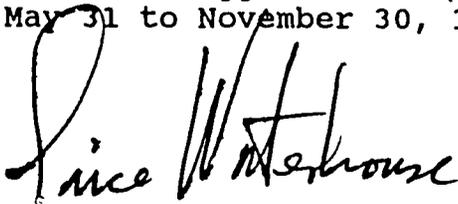
FISCAL YEAR 1990 ECONOMIC SUPPORT FUND (ESF)
PROGRAM FOR NICARAGUA FOR THE PERIOD
MAY 31 TO NOVEMBER 30, 1990
FUND ACCOUNTABILITY STATEMENT
INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying fund accountability statement (cash basis) for the local execution of the fiscal year 1990 Economic Support Fund (ESF) program for Nicaragua for the period May 31 to November 30, 1990. This fund accountability statement is the responsibility of the Government of Nicaragua (GON) and the Program implementing entities. Our responsibility is to express an opinion on this statement based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and the Government Auditing Standards issued by the Comptroller General of the United States (1988 Revision). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the fund accountability statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the fund accountability statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As further explained in Note 3 to the fund accountability statement, our audit tests disclosed questionable costs in the amount of \$843,236.

In our opinion, except for the effects of the matters discussed in the preceding paragraph, the fund accountability statement referred to above presents fairly, in all material respects, the cash receipts and the locally incurred disbursements of the 1990 Economic Support Fund (ESF) Program for Nicaragua for the period May 31 to November 30, 1990.


February 7, 1991

FISCAL YEAR 1990 ECONOMIC SUPPORT FUND (ESF)

PROGRAM FOR NICARAGUA

FUND ACCOUNTABILITY STATEMENT FOR THE

LOCAL EXECUTION OF THE PROGRAM

MAY 31 TO NOVEMBER 30, 1990

(expressed in U.S. Dollars)

T I T L E	U N A U D I T E D					QUESTIONABLE COSTS
	BUDGET	AMOUNT OBLIGATED	DISBURSED ACCORDING TO USAID/NICARAGUA	USAID DIRECT DISBURSEMENTS	LOCAL EXECUTION	
CASH TRANSFERS:						
Economic recovery Program I	\$60,000,000	\$60,000,000	\$60,000,000		\$50,653,088	\$843,236
Economic recovery Program II -						
Commodity Imports	68,000,000	68,000,000				
Repayment of GON Debt Arrearages	50,000,000	50,000,000				
Sub-Total Cash Transfers	178,000,000	178,000,000	60,000,000	-	50,653,088	843,236
ECONOMIC GROWTH AND DEVELOPMENT:						
Technical Assistance and Training	1,100,000	1,100,000	466,825		396,841	
Employment Generation	10,000,000	10,000,000				
Public Sector Support	5,000,000	5,000,000				
Medicines - PASA	1,500,000					
Community Hospitals	2,500,000	2,500,000	59,674	59,674		
Textbooks	12,200,000	12,200,000	4,596,562	4,596,562		
AMERICAN INSTITUTE FOR FREE LABOR	700,000	700,000	380,116	254,423	125,693	
NATIONAL ENDOWMENT FOR DEMOCRACY	300,000	235,000	235,000	235,000		
SALESIAN VOCATIONAL EDUCATION	1,700,000	1,700,000	259,932		165,003	
FAMILY PLANNING	5,000,000					
PVO/CO - FINANCING	8,000,000					
NATURAL RESOURCES MANAGEMENT	8,000,000					
STRENGTHENING DEMOCRATIC INSTITUTIONS	3,000,000					
INVESTMENT AND EXPORT PROMOTION	9,000,000					
Sub-Total Development Projects	68,000,000	33,435,000	5,998,109	5,145,659	687,537	
REPATRIATION OF REFUGEES	47,000,000	47,000,000	-	-	-	
USAID MISSION EXPENSES:						
Project development and support	2,000,000	242,563	6,758	6,758		
Operating expenses	5,000,000	3,865,618	1,575,943	1,575,943		
Sub-Total Mission expenses	7,000,000	4,108,181	1,582,701	1,582,701	-	
TOTAL FY 1990 SUPPLEMENTAL	\$300,000,000	\$262,543,181	\$67,580,810	\$6,728,360	\$51,340,625	\$843,236

SUPPLEMENTAL INFORMATION

Deposits of fundings earned
interest as follow:
 Central Bank of Nicaragua
 INCAE

(1,718,444)

(2,426)

(1,720,870)

FISCAL YEAR 1990 ECONOMIC SUPPORT FUND (ESF)

PROGRAM FOR NICARAGUA FOR THE PERIOD

MAY 31 TO NOVEMBER 30, 1990

NOTES TO THE FUND ACCOUNTABILITY STATEMENT

NOTE 1 - BACKGROUND:

On May 25, 1990, the President of the United States signed into law the Fiscal Year (FY) 1990 Dire Emergency Supplemental Appropriations act which included US\$300 million in Economic Support Funds (ESF) to support Nicaragua's economic recovery. The program includes two major categories of assistance:

- a. Cash transfer assistance for balance of payments/budget support to restore productive capacity, and
- b. Economic growth and development projects in support of the new government's economic recovery and social programs.

The initial cash transfer assistance provided under the program was for the purpose of financing essential commodities primarily for the private sector, such as petroleum, agricultural inputs (excluding pesticides), spare parts, intermediate goods, capital goods, and other private sector imports needed to keep the economy functioning. Follow-on cash transfer assistance includes an element of debt repayment.

The principal Nicaragua Government entity involved in the cash transfer portion of the assistance is the Central Bank of Nicaragua. Other entities, some of which are headquartered outside Nicaragua, will be involved in the implementation of individual development projects.

NOTE 2 - RATE OF EXCHANGE AND EXCHANGE RESTRICTIONS:

According to the exchange control law of September 9, 1978 all foreign currency acquired must be reported to the Central Bank of Nicaragua and all remittances must have the approval of this bank.

On May 3, 1990 the Central Bank of Nicaragua (BCN) established a new monetary unit (Cordoba Oro) equivalent to the U.S. dollar; however the old monetary unit (Cordoba) is still in circulation.

The BCN has allowed the operation of a free market for currency exchange provided transactions in this market are handled by authorized agents. As at November 30, 1990 the free rate of exchange in this market was C\$2,000,000 (old Cordobas) to US\$1.00.

NOTE 3 - QUESTIONABLE COSTS:

The following disbursements pertaining to Agreement No. 524-0300 represent incurred costs that are questionable for the reasons explained:

<u>Document</u>	<u>Concept of the disbursement</u>	<u>Amount</u>	<u>Reason for Questioning</u>
C.C. 1277-90	Purchase of spare parts for vehicles Toyota, Honda, Datsun, Mazda, and Nissan	\$ 10,072	2
C.C. 1278-90	Purchase of spare parts for japanese vehicles	40,120	2
C.C. 1301-90	Purchase of insecticides	11,205	2
C.C. 1302-90	Purchase of Goodyear tires manufac- tured in Canada	19,180	1
C.C. 1307-90	Purchase of aluminum sulfate of German origin	31,600	1
C.C. 1314-90	Purchase of spare parts for pump of italian origin	57,198	1
C.C. 1315-90	Purchase of a model 1980 used truck	24,236	3
C.C. 1442-90	Purchase of used machinery to rectify and calibrate cylinders	33,000	3
C.C. 1445-90	Purchase of raw materials (pesticides)	4,046	2
C.C. 1479-90	Purchase of fungicides and insecticides	36,339	2
Draft 07423	Purchase of a computer	20,095	2
MSGE 5687-RLC T/C 246-90	Purchase of spare parts for japanese vehicles	17,460	2
C.C. 1330-90	Purchase of 12-ounce beer bottles	271,118	2
C.C. 1614-90	Purchase of Mack trucks	<u>267,567</u>	3
	Total	<u>\$843,236</u>	

The following transactions, representing the commitment of grant funds (Agreement No. 524-0300), could be questioned when paid.

<u>Document</u>	<u>Concept</u>	<u>Amount</u>	<u>Reason for Questioning</u>
C.C. 1634-90	Purchase of photographic equipment, including paper and film	\$344,050	4
C.C. 1697-90	Purchase of machinery and equipment for a brewery, including a reconstructed packing machine and spare parts	<u>188,056</u>	2/3
		<u>\$532,106</u>	

REASONS FOR QUESTIONING

<u>Reference</u>	<u>Explanation</u>
1	Country of origin not eligible according to agreement.
2	Articles or products not eligible according to agreement.
3	Used items.
4	Invoices with no indication as to brands, trademarks or origin of the purchased articles.

Price Waterhouse

FISCAL YEAR 1990 ECONOMIC SUPPORT FUND (ESF)

PROGRAM FOR NICARAGUA FOR THE PERIOD

MAY 31 TO NOVEMBER 30, 1990

INTERNAL CONTROL STRUCTURE

INDEPENDENT AUDITOR'S REPORT

We have audited the fund accountability statement of the Economic Support Fund (ESF) Program for Nicaragua for the period May 31 to November 30, 1990 and have issued our report thereon dated February 7, 1991.

We conducted our audit in accordance with generally accepted auditing standards and the Government Auditing Standards issued by the Comptroller General of the United States (1988 Revision). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the fund accountability statement is free of material misstatement.

In planning and performing our audit of the fund accountability statement of the above indicated Program for the period May 31, to November 30, 1990, we considered the internal control structure applied to the Program in order to determine our auditing procedures for the purpose of expressing an opinion on the fund accountability statement, and not to provide assurance on the internal control structure.

The management of BCN and of the implementing entities are responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent

limitations in any internal control structure errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories: a) accounting and budgetary control systems; b) cash management; c) management information system; d) issuance of and control over letters of credit; e) procurement of goods and services; and f) administration of inventories and fixed assets.

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they had been placed in operation, and we assessed control risk.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under the standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the fund accountability statement. The reportable conditions noted are described under findings Nos. 1 to 2 in the following pages.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the fund accountability statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. We believe, however, that the reportable condition described as findings No. 1 in page 17 is a material weakness.

This report is intended for the information of the Government of Nicaragua, the program implementing entities and the U.S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter of public record.

Faice Waterhouse

February 7, 1991

FISCAL YEAR 1990 ECONOMIC SUPPORT FUND (ESF)

PROGRAM FOR NICARAGUA FOR THE PERIOD

MAY 31 TO NOVEMBER 30, 1990

REPORT ON INTERNAL CONTROL STRUCTURE

FINDINGS

1. The Central Bank of Nicaragua (BCN) Lacks Adequate Control Procedures in Areas of Significance to the Program

Condition:

Our evaluation of BCN's internal control structure disclosed the following reportable conditions:

- The monthly financial reports figures submitted to USAID/Nicaragua were not supported nor reconciled with the accounting records.
- The letter of credit files did not contain complete and sufficient documentation to demonstrate the application of competitive bidding procedures.
- There was lack of appropriate and formally defined follow-up and monitoring procedures over Program transactions. These responsibilities had not been assigned to a special control unit.

Criteria:

BCN was required to apply an adequate internal control structure and to take timely actions, as necessary, to correct the weaknesses mentioned in the condition.

Cause:

The lack of administrative support by an effective internal control unit caused the above mentioned conditions to go unnoticed.

Effect:

It is possible that the above weaknesses may render the Program related financial data inappropriate for USAID/Nicaragua purposes and may result in questionable costs.

Recommendation:

BCN should take immediate action to strengthen established control procedures and remedy the weaknesses revealed by the condition.

2. The Internal Control Structures of the Local Offices of the American Institute for Free Labor Development and Salesian Society Require Improvement

Condition:

The accounting records kept to account for project transactions and cash disbursements were not appropriate, as further explained below:

- a. The American Institute for Free Labor Development (AIFLD)
 - The documentation on file did not include reconciliations of all advances received from the central office.
 - Fund advances with more than 60 days were not liquidated opportunely.
 - Fund advances liquidation were not reflected opportunely in the accounting records.
- b. The Salesian Society (Centro Juvenil Don Bosco)
 - The accounting system does not allow for the immediate and easy identification of expenditures by line item.
 - The local office does not have financial accounting and administrative procedures manuals to be used as guidance for the recording of fixed assets and transactions paid for with USAID supplied funds.
 - Checks are issued to the name of the project coordinator who cashes them and makes cash payments directly, instead of issuing checks payable to the intended beneficiaries.

Criteria:

The local offices of AIFLD and the Salesian Society are responsible for maintaining appropriate records capable of generating complete, timely and reliable information on total project execution. Also, action memorandum with AIFLD require monthly disbursements to be made only upon satisfactory accounting and evaluation of previous activities.

Cause:

Since general controls are maintained by the AIFLD parent association abroad, it has not been considered necessary to locally implement complete control procedures. In relation to the Salesian Society its present accounting system and related procedures are considered adequate for their internal purpose.

Effect:

The lack of opportune advances liquidation affects the integrity and accuracy of the budget financial execution.

Recommendation:

Both the Salesian Society and AIFLD should take appropriate action to remedy the internal control weaknesses mentioned in the condition.

Price Waterhouse

FISCAL YEAR 1990 ECONOMIC SUPPORT FUND (ESF)
PROGRAM FOR NICARAGUA FOR THE PERIOD
MAY 31 TO NOVEMBER 30, 1990
COMPLIANCE WITH AGREEMENT TERMS AND
APPLICABLE LAWS AND REGULATIONS
INDEPENDENT AUDITOR'S REPORT

We have audited the fund accountability statement of the Economic Support Fund (ESF) Program for the period May 31 to November 30, 1990 and have issued our report thereon dated February 7, 1991.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards issued by the Comptroller General of the United States (1988 Revision). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. Compliance with laws, regulations, contract or grant applicable to the fiscal year 1990 ESF Program to Nicaragua is the responsibility of the Government of Nicaragua (GON) and the management of the implementing entities involved with the Program. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the GON and implementing units' compliance with certain provisions of laws, regulations, contracts, and grants. However, our objective was not to provide an opinion on overall compliance with such provisions.

The results of our tests indicate that, with respect to items tested, the GON and the program implementing units complied, in all material respects, with the provisions referred to in the preceding paragraph. With respect to items not tested, nothing came to our attention that caused us to believe that the GON and the program implementing units had not complied, in all material respects, with those provisions. Our work disclosed, however, those instances of noncompliance identified under finding No. 1 in the following pages.

This report is intended for the information of the Government of Nicaragua, the Program implementing units and the U.S. Agency for International Development. This restriction is not intended to limit the distribution of this report which, upon acceptance by the Office of the Inspector General, is a matter of public record.

Paice Waterhouse

February 7, 1991

FISCAL YEAR 1990 ECONOMIC SUPPORT FUND (ESF)
PROGRAM FOR NICARAGUA FOR THE PERIOD
MAY 31 TO NOVEMBER 30, 1990
REPORT ON COMPLIANCE WITH AGREEMENT TERMS
AND APPLICABLE LAWS AND REGULATIONS

FINDINGS

The Central Bank of Nicaragua (BCN), Financial Agent of the Government of Nicaragua (GON) Did not Comply With All Terms Included in Agreement No. 524-0300

Condition:

The following instances of noncompliance were revealed by our tests:

- a. Not all necessary documents in support of disbursements were maintained by BCN, in contravention of section IV.B.1.2. of the approved procedures;
- b. Certain documents related to import permits and liquidations, as well as certificates of origin and source required by section IV.B.1 of the approved procedures, were not on file.

Criteria:

BCN, as representative of the GON, is responsible for determining the eligibility of disbursement for imports and is required to comply in full with agreement terms.

Cause:

The lack of an internal control unit at BCN charged with the responsibility of following up on project execution and providing support to management allowed the cases of noncompliance mentioned in the condition.

Effect:

Because of the reported conditions, \$843,236 of incurred costs have been questioned as at November 30, 1990. Additional amounts could be questioned for similar conditions on transactions and disbursements made subsequent to that date.

Recommendation:

BCN should take whatever action is necessary to correct the situations mentioned in the condition or reimburse amounts not properly accounted for or not properly documented in compliance with agreement terms.

FISCAL YEAR 1990 ECONOMIC SUPPORT FUND (ESF)

PROGRAM FOR NICARAGUA FOR THE PERIOD

MAY 31 TO NOVEMBER 30, 1990

LIST OF REPORT RECOMMENDATION

INTERNAL CONTROL STRUCTURE

Recommendation 1:

BCN should take immediate action to strengthen established control procedures and remedy the weaknesses revealed by the condition.

Recommendation 2:

Both the Salesian Society and AIFLD should take appropriate action to remedy the internal control weaknesses mentioned in the condition.

COMPLIANCE WITH AGREEMENT TERMS AND APPLICABLE
LAWS AND REGULATIONS

Recommendation 1:

BCN should take whatever action is necessary to correct the situations mentioned in the condition or reimburse amounts not properly accounted for or not properly documented in compliance with agreement terms.

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