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**AUDIT OF
THE PANAMA ASSISTANCE PROGRAM
FUNDED BY PUBLIC LAW 101-302
AS OF MAY 31, 1991**

**Audit Report No. 1-525-91-014
September 12, 1991**

While A.I.D. designed the Assistance Program to meet provisions of the Act and additional Congressional guidance and generally followed its established policy, in certain instances, the normal processes required by A.I.D. policy were implemented through alternative methods or bypassed.

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AGENCY FOR INTERNATIONAL DEVELOPMENT

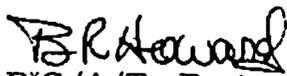
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MEMORANDUM

TO: USAID/Panama Director, Thomas W. Stukel

FROM: 
RIG/A/T, Reginald Howard

SUBJECT: Audit of the Panama Assistance Program Funded by Public Law 101-302 and Fiscal Year 1991 Appropriations as of May 31, 1991, Audit Report No. 1-524-91-014

Enclosed are five copies of the subject audit report. We provided your office with a draft of the subject report and both your written and oral comments were considered in preparing this final report. The report's two recommendations are unresolved.

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

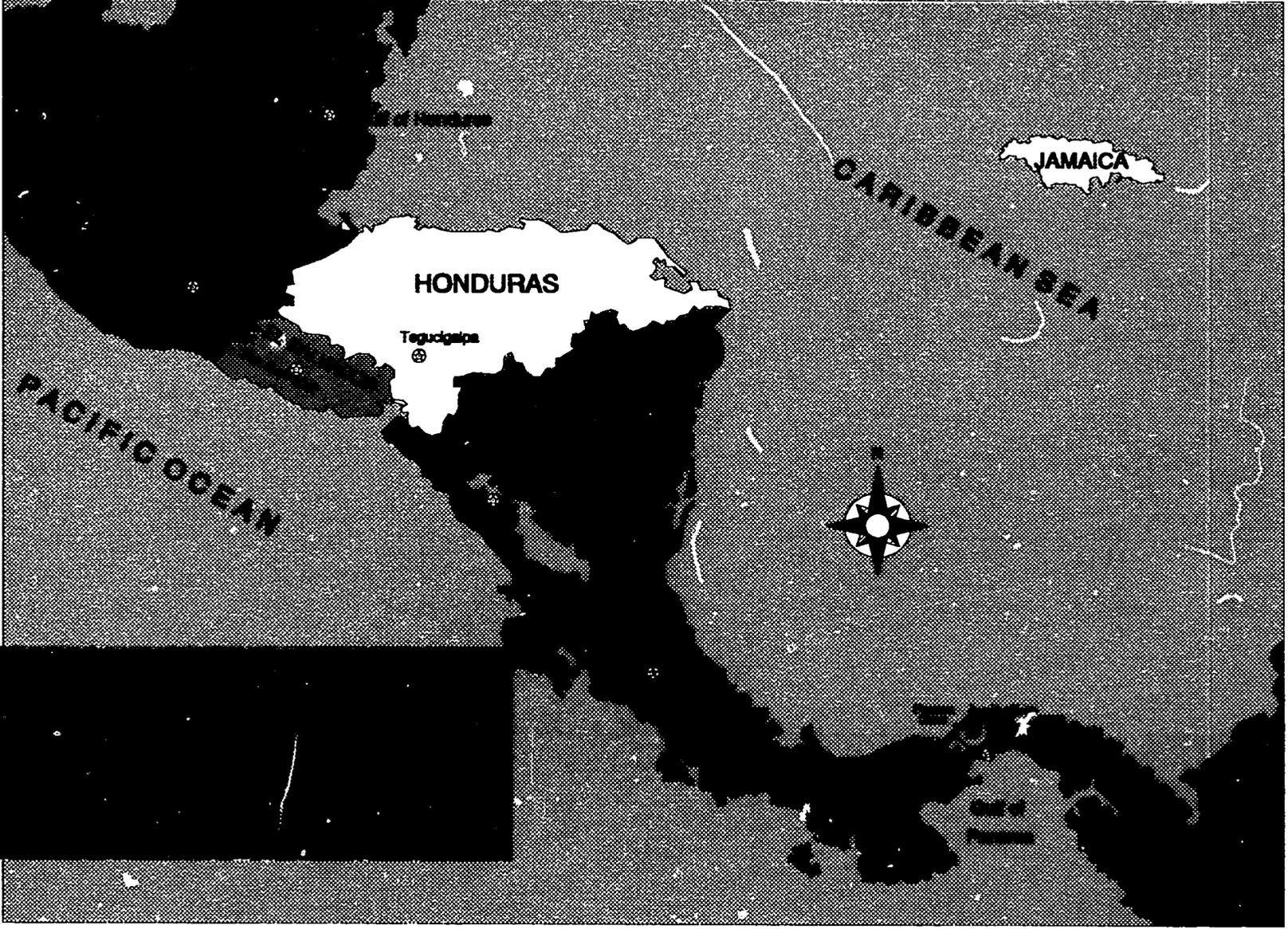
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GLOSSARY

Act	Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act
A.I.D.	Agency for International Development
A.I.D. Evaluation Handbook	A.I.D. Handbook 3, Supplement to Chapter 12
A.I.D./Washington-FM	A.I.D.'s Financial Management Office
Assistance Program	Panama Assistance Program
CDSS	Country Development Strategy Statement
COSPAAE	Private Sector Council for Educational Assistance
Discussion Paper	Supplemental Package Discussion Paper
DOJ	Department of Justice
FAA	Foreign Assistance Act
ICD	Interbank Certificate of Deposit
ICITAP	International Criminal Investigative Training Assistance Program
LAC Bureau	A.I.D./Washington/Latin America and Caribbean Bureau
MACS	Mission Accounting and Control System
OMB	Office of Management and Budget
PAAD	Program Assistance Approval Document
PID	Project Identification Document
PVO	Private Voluntary Organization



EXECUTIVE SUMMARY

PURPOSE

The Congress passed the Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act (Act), and it was signed into law on May 25, 1990. The Act included \$420 million in Economic Support Fund assistance to Panama. This assistance was to help Panama restore democracy and its economy which was weakened after several years of internal strife. The Congress, in order to meet the urgent needs within Panama, could not follow the normal appropriation process. Normally funds are appropriated after A.I.D. submits a budget request based upon a country development strategy statement and action plan. In this case however, because of the urgent need, funds were made available in the absence of budget requests.

The Act requires the Inspector General, Agency for International Development (A.I.D.) to audit funds provided under the Act in order to assess the financial management and administrative systems established by the Agency to control such programs.

This report covers the above Assistance Program activities from inception of the Act through May 31, 1991. We conducted the audit from March 4, through July 3, 1991, in accordance with generally accepted government auditing standards (see Appendix I).

Our audit objectives were to determine whether:

- A.I.D. followed the Act and additional Congressional guidance in designing the Assistance Program.
- A.I.D. was following its established policies and procedures which control the implementation of individual Assistance Program activities.
- A.I.D.'s system for monitoring, evaluating, auditing, and reporting was being implemented with regard to Assistance Program activities.
- A.I.D. obligated, expended, and accounted for the Assistance Program funds in accordance with Agency policies and procedures.

BACKGROUND

In providing the Assistance Program funds, the Congress set forth certain provisions in the Act as well as additional guidance concerning specific uses of funds. The Act and this additional guidance provides: (1) up to \$15 million for a debt-for-nature swap and immediate environmental needs; (2) up to \$10 million for A.I.D. administrative expenses for both Panama and Nicaragua; (3) up to \$1.2 million for police training in Latin America excluding Panama and \$5.5 million for Panama with a \$5 million limit on procurement of non-lethal law enforcement equipment; (4) that progress be made towards reaching a Mutual Legal Assistance Treaty; (5) that A.I.D. provide private sector development and budget support; (6) that A.I.D. show concern for child survival, health and education; and (7) that a market economy and a political democracy be encouraged.

To achieve these and other goals, A.I.D. has designed and developed 2 cash transfer programs and 16 development projects. As of May 31, 1991, A.I.D. had obligated \$390.5 million and had accrued expenditures totaling \$69.4 million. The majority of these funds, \$351.75 million, was budgeted for the two cash transfer programs which provide U.S. dollars to the Government of Panama for budget support, to help clear the Government of Panama's arrears with international financial institutions, and to reactivate the private sector.

RESULTS IN BRIEF

Due to the urgent need for assistance to Panama and before it could reestablish a presence in Panama after an absence of two years, A.I.D. began implementation of the Assistance Program using temporary duty personnel from Washington. A.I.D./Washington transferred responsibility for implementation of the Assistance Program to the newly established Mission in February 1990. A.I.D. faced significant challenges during this early period with staffing the Mission and obtaining office space and equipment while concurrently attempting to establish and implement required financial management and administrative control systems. It was during this period that much of the initial control processes that centered around the designing, planning, granting, and contracting of the Assistance Program were established.

While A.I.D. designed the Assistance Program to meet provisions of the Act and additional Congressional guidance and generally followed its established policy, in certain instances, the normal processes required by A.I.D. policy were implemented through alternative methods or bypassed.

The audit found that A.I.D. followed its normal financial management and administrative control systems except that it did not: (1) develop the normal strategy documents prior to beginning assistance activities; (2) always prepare the normal planning documentation for development projects as called for by A.I.D. handbooks but instead followed less stringent documentation guidance issued by the A.I.D./Washington/ Latin America and Caribbean Bureau; (3) issue a mission order formally establishing its monitoring and evaluation system; (4) prepare information plans as part of its assistance designs; (5) track the use of cash transfer dollars to the individual transaction level; and (6) effectively seek delinquent financial data on one project.

Furthermore, we believe that: in planning for the second cash transfer program, a private sector needs analysis should have been performed; and the implementation of this program should have been carried out in accordance with agreement terms.

PRINCIPAL FINDINGS

Planning for the Second Cash Transfer Program

Although A.I.D. followed its policies and procedures in preparing the proper design documentation for its Private Sector Reactivation Program, it had not performed a demand study to determine private sector need for the credit being offered under this \$107.9 million Program. A.I.D. policy calls for design documentation to provide statistical support for resources that are requested. Design documents, while stating there was an "urgent" and "pent-up" demand relating to new private sector economic activity, did not provide support for these statements. As of May 31, 1991, approximately \$40 million had been provided to the private banking system.

Implementation of the Second Cash Transfer Program

The Private Sector Reactivation Program Agreement contained detailed criteria regarding expenditure of Program funds. Specifically, banks wishing to obtain Program funds were first to submit a description of the private sector lending they planned to make within the next 30 days. The implementing agent would then review this plan to see if the proposed lending met Program requirements, e.g., lending for new construction. If so, the implementing agent would agree to provide the bank with Program funds in the amount of 50 percent of the value of the subsequent actual new lending made in accordance with the bank's plan. Had the Program been implemented in this manner, a linkage would have been established

showing how A.I.D. funds were related to the proposed private sector lending activity. However, Program funds were being provided to banks based on their past lending activity rather than proposed incremental lending as required by the Program Agreement. For example, after a February 1991 change in Program requirements allowing the purchase of "new private corporate bonds" as an eligible lending activity, two banks received \$4 million in Program funds for bond purchases they made on October 1 and 7, 1990. Receipt of Program funds in this case clearly increased the banks' medium-term liquidity, however, the bank's purchase of bonds occurred prior to their participation in the Program. Consequently, A.I.D. funding was not linked to this private sector activity. Because the terms of the Agreement were not being followed, A.I.D. was denied whatever level of assurance those terms provided that the private sector needs were being met through Program funds.

RECOMMENDATIONS

We recommended that USAID/Panama:

- make an analysis to determine the specific needs of the private sector, and
- restructure its cash transfer assistance for promoting private sector development, so that it can be assured that Act funds are having a direct impact on that intended result.

AGENCY COMMENTS AND OUR EVALUATION

In commenting on the draft report the Mission did not disagree with any of the factual information. They did, however, disagree with the report conclusions regarding compliance with A.I.D. policies and procedures, the second cash transfer program's affect on private sector reactivation, and the tracking of cash transfer dollars. The Mission made no comment regarding the report recommendations.

In regard to compliance issues the Mission presented both additional mitigating information as to why compliance was not always feasible and its position that compliance with A.I.D. handbooks was not required.

In regard to the Private Sector Reactivation Program the Mission stated that to analyze needs, A.I.D. Personnel conducted interviews with bankers as well as businessmen which clearly identified a need to reactivate the

banking system so it could serve its traditional role as lender to stimulate private sector growth. The Mission stated that the interviews showed that banks faced a problem of lack of medium-term funds to support working capital needs, investment in plant and equipment, maintenance, and expansion. The Mission cited a recently completed Mission-funded evaluation of the Program as providing clear evidence that the Program not only stimulated increased medium-term lending but also leveraged increased medium-term lending with the banks own resources. The Mission stated that it had disbursed the full \$107.9 million as of August 16, 1991 and believed that this provided evidence of a pent-up demand for medium-term credit to support private sector reactivation.

With regard to the tracking of cash transfer dollars, the Mission stated that this issue should be brought to the attention of A.I.D. management through a different channel than this audit report.

The report Sections relating to A.I.D. policies and procedures simply disclose the extent of compliance or noncompliance. Certain extenuating circumstances for noncompliance are discussed in the report and the Mission's comments expand on these circumstances.

Of overriding concern, however, is the second cash transfer of \$107.9 million which was made for two purposes. The first purpose was to have funds available to help mitigate a "run" on the Panamanian banking system when deposits were unfrozen on July 10, 1990. The second purpose was to provide medium-term liquidity to the banking system to enable banks to make medium-term loans to reactivate private sector development. As no "run" on the banks occurred, no funds were used for that purpose, leaving the entire \$107.9 million to be used for the second purpose. However, no analysis was made to determine that this was the best available alternative for A.I.D. to use in reactivating private sector development or that credit demands were such that they would not be met through normal banking operations. Also, the Mission was unable to provide us with any documentation of interviews with bankers or businessmen relating to either a lack of medium-term liquidity or private sector credit needs.

A.I.D., in addition to not performing a needs study, did not trace transactions to obtain assurances that funds were used for intended purposes, i.e., to reactivate private sector development, and allowed the implementing agency to bypass controls in the agreement that would have linked the use of A.I.D. funds to proposed private sector lending activity. There was no auditable evidence that such lending activity was due to A.I.D. funding or that it would not have otherwise occurred through normal banking business practices.

The two cash transfer program agreements did not provide for the tracking of A.I.D. funds to their final acceptable end use. Accordingly, there is no basis to audit program funds beyond their transfer into a commingled account, in the case of the first cash transfer, or beyond the purchase of interbank certificates of deposits for the second cash transfer.

Copies of this report are being sent to the Chairmen, Senate and House Committees on Appropriations, Senate Committee on Foreign Relations, and House Committee on Foreign Affairs; the Administrator, Agency for International Development; and other interested parties.

Office of the Inspector General
Office of the Inspector General
September 12, 1991

INTRODUCTION

Background

Due to the U.S. military activity which took place in Panama in December 1989, the Congress took up the issue of emergency assistance for Panama in January 1990. As a result, without a specific budget request from A.I.D., the President signed into law "The Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act" (Act), Public Law 101-302 on May 25, 1990. The Act provided \$420 million of new economic assistance for Panama. The Act and associated Congressional committee reports intended the \$420 million to:

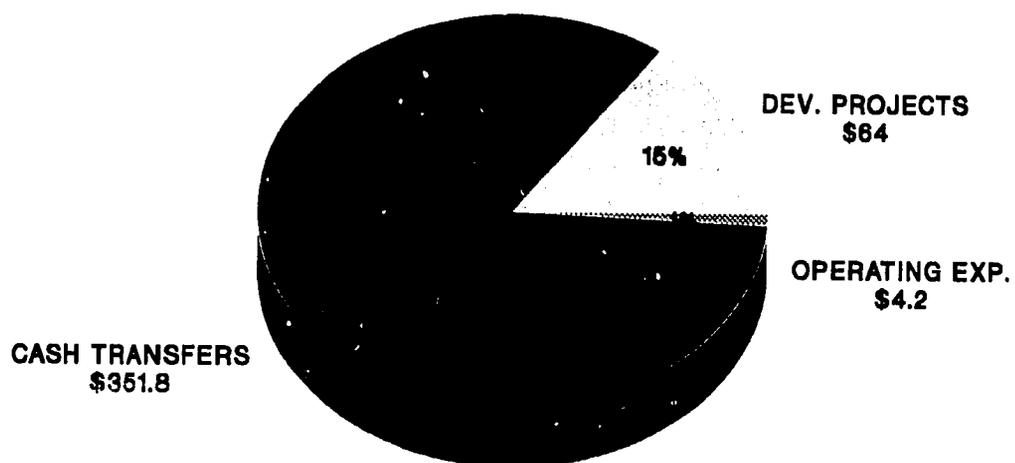
- assist and encourage the Government of Panama in taking the necessary steps to enable the proper functioning of a market economy and a political democracy,
- encourage the Government of Panama to reach agreements on exchange of records on international currency transactions in connection with narcotics investigations, and towards signing a Mutual Legal Assistance Treaty, and
- provide assistance in such areas as police services, environmental protection, child survival, health, education, private sector development, and budget support.

To accomplish these tasks, A.I.D. designed and developed the Panama Assistance Program (Assistance Program) consisting of two cash transfer programs and sixteen projects. The majority of the funding, \$351.75 million, was budgeted for the two cash transfer programs. The first, the Economic Reform Program, includes two major subprograms. One subprogram consists of a \$130 million payment to help Panama clear its arrears to the International Monetary Fund, the World Bank, and the InterAmerican Development Bank. The other subprogram earmarks \$113.85 million as budgetary support for justice, education, health, and other public sectors, as well as for infrastructure repairs and

improvements. This first cash transfer program also included significant conditions which Panama was required to meet prior to disbursement of the funds.

The second cash transfer program, funded at \$107.9 million, is titled "Private Sector Reactivation". This program has two subprograms. The first was to provide immediate short-term liquidity to Panama's banking system in the event that a "run" on the banks would occur as a result of lifting deposit withdrawal restrictions. The second subprogram was to provide liquidity to the banking system in support of medium- to long-term lending to the private sector. The following graph shows total A.I.D. assistance to Panama of \$420 million as of May 31, 1991.

TOTAL A.I.D. ASSISTANCE



(In Millions)

The Act requires the A.I.D. Inspector General to, "... at least semiannually, beginning six months from the date of enactment of this Act, audit the Economic Support Fund programs provided under this Act for Nicaragua and Panama to assess the financial management and administrative systems established by the Agency to control such programs...." This audit responds to this requirement and presents the results of the second semiannual audit covering Assistance Program activities through May 31, 1991.

Audit Report No. 1-525-91-005, dated February 8, 1991, covered the first six months (May 25, 1990 through November 30, 1990) of the Assistance Program's implementation. That audit provided our preliminary assessment of vulnerability for each program and project activity, based upon the actual or planned controls to be incorporated into the agreements with external implementing entities. Appendix III shows the apparent weaknesses that were disclosed by that audit and their current resolution status.

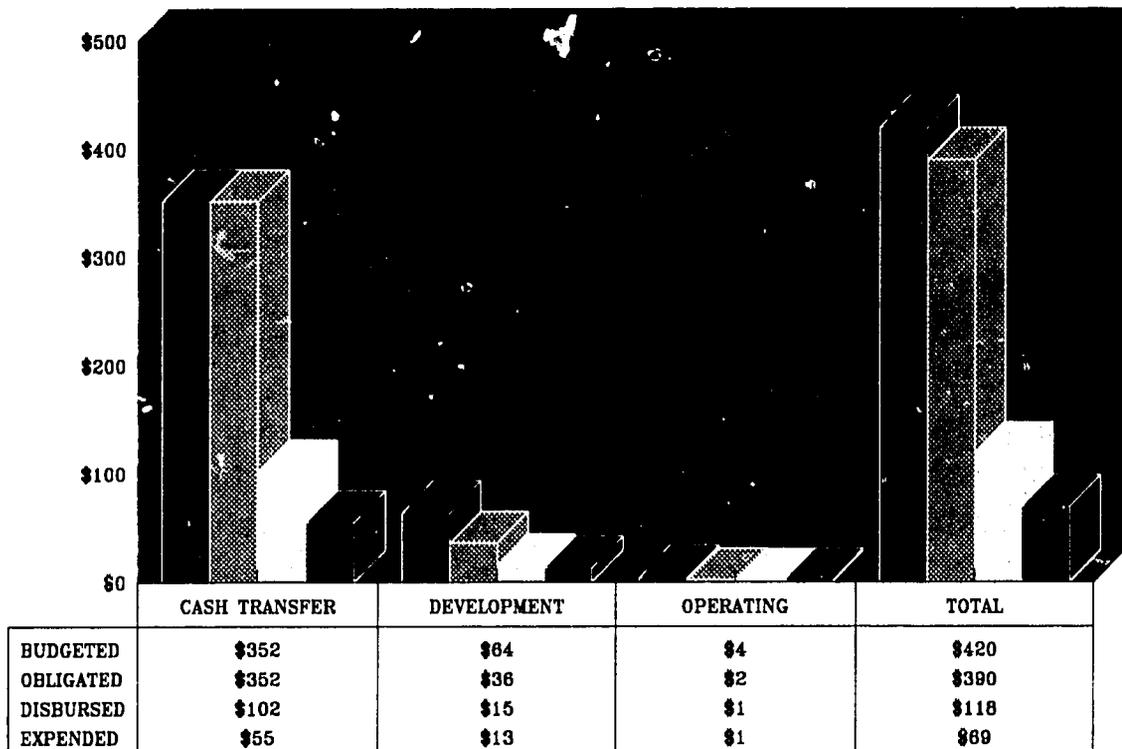
In addition to our internal audit efforts, two external non-Federal audits have been contracted. The first is an audit of Immediate Recovery Project activities which provided food and replacement housing to persons displaced by the December 1989 military action in Panama. The audit period cut-off date is May 31, 1991 and a report has not yet been issued. The second is an audit of the activities of selected entities which are implementing the Assistance Program under the Act. The audit period for that effort is May 25, 1990 to September 30, 1991.

This internal audit examines whether A.I.D. designed the Assistance Program to meet the requirements of the Act and additional Congressional guidance and whether it followed its policies and procedures in implementing, monitoring, and accounting for Assistance Program activities.

As of May 31, 1991, the Mission had obligated \$390.5 million of the Act's funds and had accrued expenditures totalling \$69.4. According to

information gathered during the audit, the following summarizes the financial status of the Assistance Program in Panama.

**UNAUDITED FINANCIAL STATUS
PANAMA ASSISTANCE PROGRAM
THROUGH MAY 31, 1991**



(In Millions)

Act funds are to be completely obligated by September 30, 1991. A financial summary of Assistance Program activities through May 31, 1991 is included as Appendix IV.

Audit Objectives

The Office of the Regional Inspector General for Audit/Tegucigalpa audited A.I.D.'s systems for managing the Assistance Program funded by the Act to answer the following audit objectives.

1. Did A.I.D. follow the Act and additional Congressional guidance in designing the Assistance Program?
2. Was A.I.D. following its established policies and procedures which control the implementation of individual Assistance Program activities?
3. Was A.I.D.'s system for monitoring, evaluating, auditing, and reporting being implemented with regard to Assistance Program activities?
4. Did A.I.D. obligate, expend, and account for the Assistance Program's funds in accordance with Agency policies and procedures?

Our fieldwork to answer these objectives was conducted at USAID/Panama and its accounting station USAID/Costa Rica. Therefore, we have answered the objectives mainly in terms of the conditions noted at these A.I.D. field Missions. While we did not conduct fieldwork in A.I.D./Washington, this report includes references to A.I.D./Washington's role in the Assistance Program to the extent that was verifiable from official documents or supported by interviews with Mission management. In this regard, when reference is made to A.I.D., this most generally refers to USAID/Panama, but in certain instances could also apply to the Agency as a whole.

In answering the audit objectives, we tested whether A.I.D. (1) followed applicable internal control procedures and (2) complied with certain provisions of laws, and agreements. Such tests were sufficient to provide reasonable, but not absolute, assurance of detecting abuse or illegal acts that could significantly affect the audit objectives. However, because of limited time and resources, we did not continue testing when we found that, for the items tested, A.I.D. followed its procedures and complied with

legal requirements. Therefore, we limited our conclusions concerning these positive findings to the items actually tested. But when we found problem areas we performed additional work:

- to determine that A.I.D. was not following a procedure or not complying with an A.I.D. policy, and
- to make recommendations to correct the condition or cause of the problem.

Appendix I contains a complete discussion of the scope and methodology for this audit.

REPORT OF AUDIT FINDINGS

Did A.I.D. follow the Act and additional Congressional guidance in designing the Assistance Program?

A.I.D. followed the Act and additional Congressional guidance in designing the Assistance Program for Panama.

With regard to specific provisions of the Act:

Debt-for-Nature Swap - The Act provides that: "...up to \$15,000,000 may be used for a debt-for-nature swap and for immediate environmental needs."

A.I.D. designed an \$18 million Natural Resources Management Project which contains an \$8 million debt-for-nature element.

Forestry Protection - The Act provides: "None of the funds appropriated in this Act...should be used for any project that would result in any significant loss of tropical forests."

The audit disclosed no evidence that the Assistance Program would result in any significant losses of tropical forests.

A.I.D. Administrative Expenses - The Act provides: "Up to \$10,000,000...may be used for the purpose of paying administrative expenses incurred by the Agency for International Development in connection with carrying out its functions...."

The \$10 million limit imposed by the Act is a cumulative figure for administrative expenses at both the Panama and Nicaragua Missions. The combined budget shows that \$10 million of the Act's funds will be used for this purpose -- \$3.3 million for Panama and \$6.7 million for Nicaragua. The Missions report having \$5.4 million of accrued expenditures as of May 31, 1991 (\$1.2 million for Panama and \$4.2 million for Nicaragua).

Police Training and Law Enforcement Equipment - The Act provides: "...(1) up to \$1,200,000 may be provided to carry out the purposes of section 534(b)(3) [police training] of the Foreign Assistance Act of 1961 for countries in Latin America and the Caribbean other than Panama; (2) assistance may be provided...with the objective of creating a professional civilian police force...except that such assistance shall not include more than \$5,000,000 for the procurement of equipment for law enforcement purposes in Panama, and shall not include lethal equipment...."

A.I.D. entered into a Memorandum of Agreement transferring \$6.7 million in Act funds to the U.S. Department of State which agreed to allocate those funds to the U.S. Department of Justice for the following purposes:

- \$1.2 million for regional activities of the International Criminal Investigative Training Assistance Program (ICITAP), and
- \$5.5 million for the ICITAP Fiscal Year 1990 Program for Panama.

The agreement specified that no more than \$5 million could be used for the procurement of non-lethal law enforcement equipment. The budget included \$2.3 million for equipment and supplies with no provision for procurement of lethal items.

With regard to additional Congressional guidance:

Mutual Legal Assistance Treaty - The House of Representatives Conference Report No. 101-493, dated May 22, 1990, provides: "...that the United States Government and the Government of Panama: (1) reach agreement for exchanging records on international currency transactions in connection with narcotics investigations and proceedings, and (2) make steady progress towards signing a Mutual Legal Assistance Treaty....the conferees strongly urge that no more than 80 percent of the funds for Panama be provided unless the above conditions are met."

Both provisions 1 and 2 were included by the Mission as conditions precedent to the disbursement of funds in their first cash transfer program with Panama. The Mutual Legal Assistance Treaty was initialled by representatives of the United States and Panama on April 11, 1991. At that time 28 percent of the Act's funds had been provided to Panama. Although not a condition to disbursement, the Treaty had not been ratified by the two Governments as of May 31, 1991. ¹

¹ *The Government of Panama subsequently ratified this Treaty on July 15, 1991.*

Private Sector Development and Budget Support - Conference Report No. 101-493 also provides: "Private sector development and budget support are needed for both countries, but assistance for child survival, health and education are also critical needs in both countries. The conferees expect to receive notifications on assistance to Panama and Nicaragua that show a concern for the social as well as the private sector development needs in these countries."

A.I.D. designed two cash transfer programs to strengthen the public and private sectors and restore the productive capacity of the Panamanian economy. To address the backlog of public investment needs, A.I.D.'s first cash transfer program budgeted \$113.85 million as a Special Priority Investment Fund in support of Panama's 1990 and 1991 public sector budgets. The cash transfer agreement contains several conditions which the Government of Panama is required to fulfill prior to release of funds. These conditions precedent to disbursement include having a plan to manage public sector finances. The second cash transfer program with \$107.9 million, provides liquidity to the banking system for the purpose of expanding credit to the private sector. Of this amount, \$72 million has been disbursed by A.I.D. as of May 31, 1991.

The Mission's overall Assistance Program design also includes several development projects, which support the public sector budget. These include, for instance, \$4.5 million for a Financial Management Reform Project. This Project is designed to improve financial management and audit systems, and to promote accountability of government officials in managing public resources.

Child Survival, Health, and Education - Although the Mission does not have any projects in these areas, the Government of Panama has programmed \$20.7 million of the funding received from the first cash transfer program to these areas.

Market Economy and Political Democracy - The Committee on Appropriations Report No. 101-434, dated March 27, 1990 provided: "This assistance should be used to encourage and assist the Government of Panama in taking the necessary steps to enable the proper functioning of a market economy and a political democracy."

A.I.D. incorporated into the first cash transfer program conditions precedent to disbursement regarding the privatization of public enterprises and the lowering of tariffs and elimination of trade restrictions and price controls. A.I.D. is also planning the Economic Policy Development Project partially funded with \$3.1 million under the Act. The purpose of this Project

will be to improve Panama's economic policy environment and develop incentives for private sector growth. Regarding the fostering of a political democracy, A.I.D. has begun a Democratic Initiatives Project budgeted at \$2.1 million to strengthen Panama's legislative, electoral, civic development, and journalistic processes. Additionally, A.I.D. has a \$12 million project to improve the judicial administrative systems in Panama, which is budgeted to receive \$6.9 million from the Act.

Was A.I.D. following its established policies and procedures which control the implementation of individual Assistance Program activities?

A.I.D. followed its policies and procedures for implementing project and nonproject assistance except that it (1) deferred the preparation of the normal assistance strategy documents due to the need to start assistance activities; and (2) for several project activities, prepared planning documentation which did not address all of the elements specified by A.I.D. handbooks. In addition, although specified planning documentation was prepared for the second cash transfer program, funds were being applied to a subprogram which had not been fully analyzed.

To answer this objective, six criteria were reviewed: two were complied with, two were partially complied with, and two were not complied with. For this audit objective we reviewed whether policies and procedures relating to the preparation of major planning documents, (i.e. Country Development Strategy Statement, Action Plan, and final design documents on individual assistance activities) had been followed, whether Congressional Notifications had been made in advance of obligating funds for new assistance activities, and whether assistance agreements incorporated relevant aspects of the approved assistance designs and applicable legal and standard provisions. The specific criteria reviewed and results are detailed in Appendix V.

A.I.D. had not prepared a Country Development Strategy Statement or Action Plan prior to initiating assistance activities. The A.I.D./Washington/LAC Bureau did, however, approve with certain modifications the Mission's proposed portfolio of Act-funded activities and in May 1991 the Mission submitted a Country Development Strategy Statement and Action Plan to guide its future activities. A.I.D. notified Congress on all its assistance activities where required. Regarding

assistance agreements, the relevant provisions of final design documents have been incorporated and, where standard agreement language and provisions have been specified in A.I.D. handbooks, they have been included.

The instances where A.I.D. did not follow its policies and procedures as well as instances where the Mission, although following policies and procedures, could strengthen controls are detailed in this report under the captions:

- The Mission, with LAC Bureau Approval, Initiated the Assistance Program without a Country Development Strategy Statement or Action Plan
- Final Design Documents Did Not Always Meet Handbook Standards
- Planning for the Second Cash Transfer Program Was Not Fully Analyzed

The Mission, with LAC Bureau Approval, Initiated the Assistance Program without a Country Development Strategy Statement or Action Plan

A.I.D. is required to provide assistance within its development strategy for each country. This strategy, developed by A.I.D. missions and approved by their Geographic Bureau in A.I.D./Washington, is called the Country Development Strategy Statement (CDSS). The CDSS is a five-year document which is updated as needed to reflect changes in A.I.D.'s objectives or the country's situation. Handbook 3, Chapter 1 states the agreed upon CDSS provides the framework for a mission to respond to a country's development problems. Projects responding to priority development problems which arise, but are not included in the strategy statement, may be identified and proposed for funding. Such proposals, however, should be accompanied by the functional equivalent of a supplementary CDSS justification. Guidance relating to the development of such strategies is included in Handbooks 1 and 2, and in Agency cables.

Action Plans serve as a bridge between the missions' CDSSs and their operational programs. They link the strategies with projects and focus management attention on the effectiveness of the program in achieving CDSS goals. Guidance on the development of Action Plans is provided in Agency cables and memoranda.

In April 1990, during the initial development phase of the Assistance Program, Mission officials presented a "Supplemental Package Discussion Paper" (Discussion Paper) to the LAC Bureau. The Discussion Paper detailed the Mission's proposal for the portfolio of programs and projects which would be allocated the expected funding under the Act. With modifications the Discussion Paper was approved on June 11, 1990, by the LAC Bureau. The Mission considered that the approved Discussion Paper temporarily served the role of a CDSS. The Mission was preparing its formal CDSS during the period of our audit and, in May 1991, submitted it to the LAC Bureau for approval.

An Action Plan was also not prepared. The Mission intended its Discussion Paper to also serve as the functional equivalent of an Action Plan in planning further assistance activities. The Mission was preparing its Action Plan for Fiscal Years 1992 and 1993 during the audit and submitted it to the LAC Bureau in May 1991.

Although required, the Mission did not prepare a CDSS and Action Plan prior to initiating Assistance Program activities. This decision was made with the approval of the LAC Bureau. Furthermore, the Mission did not follow the normal A.I.D. process regarding these documents because the normal process would be to prepare the CDSS, which supports the Agency's budget for eventual submission to the Congress. The Congress then would make appropriations based on that request. However, in this case, due to the U.S. military activity in Panama in December 1989, the Congress took up the issue of emergency assistance for Panama, without a specific budget request from A.I.D., and appropriated the funding. Since the Mission has now submitted the two assistance strategy documents, no recommendation is necessary.

Mission Comments and Our Evaluation

The Mission stated that it fundamentally disagreed with the implication in the report that the Mission did not comply with program and project design documentation standards. It is the Mission's position that its Discussion Paper was accepted by A.I.D./Washington and was sufficient to serve in the place of a Country Development Strategy Statement and Action Plan.

The legislation requires that we assess the Agency's, not the Mission's, systems used to control the Program. Accordingly, in conducting our audit we assessed the Agency's compliance with its established policies and procedures and disclosed the results of our assessment. While our report notes extenuating circumstances under which the Mission was operating, it also notes that due to certain actions by the Mission and the LAC Bureau the Agency did not always implement its administrative controls over the Assistance Program.

Final Design Documents Did Not Always Meet Handbook Standards

Unless an exception applies, A.I.D. procedures require that assistance agreements be preceded by a detailed analysis and full-scale development of the assistance design. For project assistance financed with Economic Support Funds, an exception to the requirement for a Project Paper, the detailed design document for such assistance, is permitted in recognition that there may be political considerations, timing, or other factors which may be overriding. If this exception is exercised, the A.I.D. handbooks still require that a preliminary design document, a Project Identification Document (PID) or its equivalent, be prepared.

Handbook 3 states that a basic purpose of a PID is to convince A.I.D. management that: the preliminary proposal has merit, it seems better than alternative solutions to the problem, and it makes sense to devote personnel and financial resources to further develop the project. Project development leads to the completed project design and is thus one of the most important phases in the overall project design cycle. As part of this process, PIDs should establish goals to be supported and purposes to be achieved by the project, identify intended beneficiaries, give preliminary indications of the shape and cost of the project, and identify major issues. A.I.D. Handbook 3 identifies 18 areas that a PID should cover.

The Mission submitted a "Supplemental Package Discussion Paper" (Discussion Paper) to the A.I.D./Washington/LAC Bureau which described, in general terms, the projects, programs or activities to which the expected funding under the Act would be allocated. This Discussion Paper did not treat each program and project separately nor include much of the information and analyses specified in A.I.D. handbooks for preliminary design documents. However, after the LAC Bureau reviewed the Discussion Paper, it stated the Discussion Paper served as the PID for all the identified activities. It then directed the Mission to submit detailed design documents on only four of the activities identified for funding.

The Mission's two cash transfer programs and 9 of 12² planned development projects had final designs by May 31, 1991.

² For purpose of this discussion we are excluding four projects shown in Appendix IV. Three of these, i.e. project Nos. 525-0305, 525-0310 and 525-0311, involved budget transfers to other U.S. Government entities to implement their activities. A.I.D. Handbook 12 on use of Federal agencies does not provide guidance for such situations so it was not clear that these should be considered as projects for purposes of following the project documentation requirements of A.I.D. Handbook 3. The fourth project (525-0300) was designed prior to the Act, with Act funds reimbursing the original sponsor. We therefore considered the project design process on this project to be outside the scope of our review.

Following A.I.D. policy, the Mission's two cash transfer programs were preceded by Program Assistance Approval Documents (PAADs), the detailed design document for such assistance. However, for one of the cash transfer programs, the \$107.9 million Private Sector Reactivation Program, only one of the two subprograms had been fully analyzed. Because expected conditions did not develop for using the funds under the initial subprogram, the entire \$107.9 million is now being used for the subprogram which had not been fully analyzed.

The final design documents for five of the nine development projects that had reached this stage did not meet A.I.D. Handbook 3 standards. Of the five projects that did not meet standards, three involved amending existing project agreements. These amendments were preceded by discussions with the implementing entities and in two cases by implementing entity proposals. However, A.I.D. Handbook 3 requires, at a minimum, that abbreviated PIDs be prepared in such cases. The fourth project was an umbrella project involving four subprojects. Two subprojects are add-ons to cooperative agreements for regional projects and two are direct grants. Agreements had been signed on three of these subprojects and those were preceded by unsolicited proposals. Supplement A to A.I.D. Handbook 3 requires PIDs in these cases. A Project Paper was required for the fifth project, but an unsolicited proposal was prepared that lacked much of the information specified in Handbook 3 for a Project Paper.

The assistance activities mentioned above are now underway and the assistance designs set. Accordingly, we are not making a recommendation.

Mission Comments and Our Evaluation

It is the Mission's position that its Discussion Paper served the basic purpose of a PID which was to:

...convince A.I.D. management that the preliminary proposal has merit, that it seems better than alternative solutions to the problem, and that it makes sense to devote personnel and financial resources to further develop the project.

Additionally, the Mission expressed concern that the report imposes a more stringent reading of the handbooks than justified by their text and that such interpretation denies A.I.D. flexibility in the conduct of foreign assistance.

Our report discloses that the Discussion Paper and other final design documents used or prepared by the Mission did not include information

and analyses specified in A.I.D. handbooks for preliminary design documents. We do not know the reasons for the LAC Bureau's acceptance of the Discussion Paper in lieu of a fully developed PID. Regarding the Discussion Paper we believe it did not contain sufficient information to fulfill the handbook's stated purpose of convincing A.I.D. management that the proposal had merit and seemed better than alternative solutions. For example, the Discussion Paper did not discuss alternatives to the proposed programs and projects, and one subproject was only referred to as an activity to be determined.

Administrative and financial controls set forth by A.I.D. are contained in handbooks, cables, and memorandums. It is seldom possible to categorically state that any given control is required rather than provided as guidance. Accordingly, we used our best judgement in selecting those controls we considered essential in assuring Assistance Program funds were used in the most appropriate manner and safeguarded to the extent possible.

Planning for the Second Cash Transfer Program Was Not Fully Analyzed

The Private Sector Reactivation Program was initiated without fully analyzing the need for credit expansion in the Mission's final planning document. We were unable to determine why such analysis was not made. It is A.I.D. policy that the need for cash transfers be supported. Without a full analysis, the entire \$107.9 million obligated under this Program could be expended without assurance that this was the best available method of meeting private sector development needs or that needed credit would not have otherwise been available through normal banking activity.

Recommendation No. 1: We recommend that USAID/Panama make an analysis to determine the specific needs of the private sector.

The Mission submitted its final planning document, the Program Assistance Approval Document (PAAD), to A.I.D./Washington for approval of the Private Sector Reactivation Program. It was approved on July 16, 1990. The PAAD was prepared to justify two objectives: (1) to provide immediate temporary short-term liquidity to private banks requiring resources to meet the withdrawal demands of their depositors, and (2) to provide liquidity to private banks to support the expansion of medium-to-long-term credit for the private sector.

In justifying the first objective of the Program, the PAAD detailed, with tables, calculations, and analyses, how the cash transfer program might be

needed as a quick-disbursing "safety-net" to cover a banking system short-term liquidity problem if a "run" on the banks occurred upon the lifting of term-deposit withdrawal restrictions by Panama. When these restrictions were lifted on July 10, 1990, no "run" occurred. Consequently, no Program funds were expended for this purpose.

Regarding the second objective, the Mission believed that by increasing medium-to-long-term liquidity of the banking system, it could in turn support the reactivation of the private sector economy. In an effort to support this objective the PAAD stated there is an "...urgent need to increase the lending activity of banks.", and there is a "pent-up demand" for credit. However, the PAAD did not support these statements of private sector need with detailed analyses. A.I.D. Handbook 4, Chapter 2, Section 2E.3.a.(1) calls for "...statistical data supporting the need for the resources being requested." The Action Memorandum from the Bureau's Office of Development Resources recognized that a credit-demand study had not been made, nonetheless, it recommended approval of the PAAD.

The Program Agreement required (1) that the \$107.9 million be disbursed by A.I.D. in three tranches; (2) that after release of the first \$36 million on September 5, 1990, each subsequent disbursement be conditioned on the implementing entity having committed all of the funds already received; and (3) that all funds be requested by July 23, 1991. During the initial six-month period after the agreement was signed, only \$7.5 million of the first tranche had been expended by the implementing entity. Accordingly, in order to accelerate the use of Program funds, the Project Officer recommended in a February 1, 1991 memorandum to the Mission Director, approval of five changes to the Program. The memorandum stated that banks' reasons for the low level of activity "... range from lack of demand to the cost of funds." These changes allowed:

- larger financial concessions to banks that lend to small businesses,
- the reduction in cost of funds to the banks (interest rate charged under the Program) by one-half percent,
- banks' access to Program funds up to their net worth instead of paid in capital,
- for the funding of new private corporate bonds, and
- portfolios with maturities of less than one year if they are for small businesses.

These changes were approved on February 4, 1991, and in the following month \$16 million was expended. As discussed starting at page 23, we reviewed approximately \$9.5 million of this \$16 million and found that these expenditures were based on past bank lending activity not current private sector demand. As of May 31, 1991, of the \$72 million disbursed by A.I.D., approximately \$40 million had been expended under the Program.

In summary, we believe that the Mission needs to make an analysis of specific private sector needs and how A.I.D. can best meet these needs.

Mission Comments and Our Evaluation

The Mission disagrees that planning for the credit subcomponent of this cash transfer program was inadequate, and stated that as part of its design process, "...A.I.D. personnel conducted extensive interviews with bankers as well as businessman which clearly identified the need to reactivate the banking system so it could serve its traditional role as lender to stimulate private sector growth." Based on these interviews the Mission stated that banks needed medium-term funds to support working capital needs, investments in plant and equipment, maintenance and expansion. The Mission also stated that the banks indicated they had mismatched their portfolios with regard to the term structure of deposits and loans. According to the Mission, "This created severe cash flow problems causing banks to force customers to pre-pay loans and cut off credit...".

Interviews do not constitute statistical data supporting the need for the resources being requested as required by A.I.D. Handbook 4. Neither the approved planning document nor the Mission's files disclosed the detailed analysis we believed necessary to justify this \$107.9 million Program. Also, the Mission was unable to provide us with any documentation of its interviews with bankers and businessmen. Accordingly, we were not able to verify any of the Mission's statements regarding banking needs or shortage of private sector credit.

While a \$107.9 million infusion of medium-term funding could have some effect on reactivating the banking system, our audit could not establish a linkage between these funds and an increased level of credit to the private sector. Whether an infusion of \$107.9 million of medium-term funding could have any measurable impact on even the banking system itself is questionable, considering its June 1991 liquidity base of \$10.9 billion as cited by the Mission.

In fact, our audit indicated that certain expenditures of funds were not used to increase private sector development. For example, an official at one bank (which had received 21.5 percent of the Programs funds or \$8.6 million as of May 31, 1991) stated that funds received under the Program allowed his bank to invest in short-term instruments in the United States. He also stated that the Program funds allowed the bank to strengthen its balance sheet. Officials at another bank that had received 22.7 percent of the Program's funds (\$9.1 million) also stated that Program funds allowed their bank to improve the financial appearance of its balance sheet.

The Mission stated that a recently completed evaluation report, prepared by an independent contractor, proves their initial analysis that there was a strong, pent-up demand for medium- and long-term credit to support private sector reactivation.

We were provided this Mission-funded evaluation report after completion of our fieldwork. While we have not made a detailed analysis of this report, we note that its economic hypothesis did not directly link A.I.D. funds to an increase in credit to the private sector development or that such an increase actually occurred. We also noted that the contractor performing the evaluation is an official of an agency currently receiving A.I.D. funds, which could impair his independence.

Was A.I.D.'s system for monitoring, evaluating, auditing, and reporting being implemented with regard to Assistance Program activities?

The Mission followed A.I.D.'s policies and procedures for monitoring, evaluating, auditing, and reporting except that it did not: (1) issue a mission order formally establishing its monitoring and evaluation system, (2) prepare information plans as part of its assistance designs, and (3) track the use of cash transfer dollars to the individual transaction level. Also, although the Agency policies and procedures were followed, in certain instances controls could be strengthened. We noted that: (1) for the second cash transfer program, funds were not being expended in accordance with program agreement terms; and (2) evaluations were deferred for cash transfer programs.

To answer this objective six criteria were reviewed: two were complied with, two were partially complied with, and two were not complied with. The specific criteria reviewed and results are detailed in Appendix V.

Regarding the preparation of plans related to monitoring and evaluation, it should be noted that while Handbook 3 specifies a general requirement for information plans for all programs and projects, further specific requirements for the different types of assistance vary. Nevertheless, of 11³ agreements that had been signed through May 31, 1991, each had some degree of planning for monitoring, 8 had evaluation plans, and 5 had requirements for financial audits contracted by the implementing entity. However, with regard to audit, coverage was increased to 10 agreements by including recipient audits that are planned outside the terms of the agreements, and a planned Mission-funded financial audit of Assistance Program activities that can be verified to records in Panama.

With respect to legal and policy requirements for cash transfer dollars, the Mission had followed the requirement to establish noncommingled bank accounts into which the dollars would be deposited. With regard to reporting, the Mission had met its reporting requirements to A.I.D./Washington.

Concerning the Mission's monitoring of implementing entity compliance with agreement reporting requirements, we reviewed the Mission's two cash transfer programs and a development project and a subproject. Reporting on one cash transfer program and the subproject was timely and in accordance with the agreement terms. Reporting on the remaining cash transfer program and development project had been delinquent but in each case the problem was resolved during the audit period.

Our review of the Mission's two cash transfer programs and the project and subproject activities showed that the Mission's monitoring was adequate for the subproject. Monitoring for the project was also adequate except that the Mission did not resolve delinquent reporting in a timely manner. Regarding the cash transfers, by design and with A.I.D./Washington/LAC Bureau approval, the Mission tracked assistance dollars only to commingled accounts in Panama and was relying upon the Government of

³ This count excludes four agreements. Three of these four, project Nos. 525-0305, 525-0310 and 525-0311, were budget transfers to other U.S. Government entities. A.I.D. Handbook 12 on use of Federal agencies does not provide guidance for such situations so it was not clear that these should be considered as projects for purposes of following the monitoring requirements specified for project assistance in A.I.D. Handbook 3. The fourth project (525-0300) was designed prior to the passage of the Act and implementation activities were completed shortly after the Act-funded Assistance Program began. Act funds merely reimbursed the original sponsor. We therefore considered the monitoring, evaluating and reporting processes for this project to be outside the scope of our review.

Panama to do further detailed monitoring which includes an A.I.D. funded independent audit contracted by the Government of Panama for one of the cash transfer programs. The Mission's monitoring up to the point of commingling the funds was adequate. Except in one instance reported later as a problem area, our review did not examine the adequacy of the Mission's monitoring beyond the point of commingling.

Under the following captions we provide more detail on these areas where compliance with certain A.I.D. policies was questioned or where improvements were needed:

- **A Mission Order Formally Establishing a Monitoring and Evaluation System Had Not Been Issued**
- **The Mission Did Not Prepare Information Plans as Part of Its Assistance Designs**
- **Cash Transfer Dollars Could Have Been Tracked in Greater Detail**
- **The Second Cash Transfer Program Is Not Functioning as Intended**
- **Cash Transfer Evaluations Were Deferred**

A Mission Order Formally Establishing a Monitoring and Evaluation System Had Not Been Issued

Because of the range of information needs and the diversity of problems confronting A.I.D. recipient countries, A.I.D. considers uniform requirements for monitoring and evaluation activities to be inappropriate. Therefore, the A.I.D. Evaluation Handbook requires missions to establish and maintain their own monitoring and evaluation system and to prepare a mission order describing the organization and assignment of responsibilities within its system. The Mission had not issued a mission order meeting this requirement. Mission management stated that an order had not been issued because of higher priority concerns associated with starting up the Assistance Program. Mission management noted that they now have a person on long-term temporary duty for this purpose. Consequently, we are not making a recommendation in this regard.

The Mission Did Not Prepare Information Plans as Part of Its Assistance Designs

The A.I.D. Evaluation Handbook (A.I.D. Handbook 3, Supplement to Chapter 12, Section 1) states that final planning documents for projects and programs must include an information plan specifying the data collection, monitoring, and evaluation activities to be conducted and the resources and other arrangements necessary to implement the plan. The Mission's two cash transfer programs and 9 of 12⁴ planned development projects had final designs by May 31, 1991. None of the Mission final design documents or agreements contained an information plan. However, certain aspects of information plans were sometimes covered as part of other plans, e.g. implementation, monitoring and evaluation plans, or were evident from the narrative of the final design document or agreement. We are not making a formal recommendation in this regard as the Mission stated action would be taken to address this issue.

Cash Transfer Dollars Could Have Been Tracked in Greater Detail

Section 592(b) of the 1990 Appropriations Act requires that cash transfer dollars be placed in a separate account (noncommingled bank account). A.I.D. policy is that financial records shall document the withdrawal and disposition of dollar funds from the separate account and their tracking to final acceptable uses. Separate account and dollar tracking requirements were instituted to prevent abuse and diversion of dollar proceeds.

A.I.D. Handbook 1, Part IV shows that, in supporting the macroeconomic purpose of balance of payments assistance, A.I.D.'s overall preference is to use cash transfers for import financing. Further, the A.I.D. policy provides that cash transfer funds be tracked to individual transactions. Specifically, the Handbook states that if the imports financing arrangement is used, "Reimbursements [from the noncommingled separate account] must be for specific import transactions and should be part of a timely sequence for completing such transactions. This type of reimbursement is to be distinguished from ex post attribution made after release of dollars from the separate accounts..." Thus, it can be seen that tracking from a noncommingled account to specific transactions was envisioned by this Handbook.

The cash transfers in Panama's Assistance Program, however, were for different macroeconomic purposes not covered by A.I.D. policy and,

⁴ See footnote 2, p. 11.

therefore, no specific guidance existed regarding control mechanisms. The macroeconomic purposes of these cash transfers were public sector budget support and increasing liquidity in the banking system. In designing the two cash transfer programs, the Mission, with LAC Bureau approval, decided to track the funds only to the extent where it could be shown they would be applied to their macroeconomic purposes. Specifically, \$113.85 million from the first cash transfer program was to support the Government of Panama's public sector investment budget, the Mission decided to track the funds to a commingled account established in the National Bank of Panama to receive Government of Panama, A.I.D. and other donor funds to partially finance this budget.

For the other cash transfer program, the end use of the funds (\$107.9 million) was defined to be the purchase of interbank certificates of deposit (ICDs) and thereby introduce additional liquidity into the banking system for reactivating the private sector. As discussed in the next Section of this report, A.I.D., by defining the end use to be the purchase of ICDs, could not be assured its funds were having the desired impact.

During design of the Assistance Program we advised the Mission that, as designed, the first cash transfer program would likely require an exception to A.I.D.'s "tracking to end use requirement" and suggested that A.I.D. notify Congress as to its intentions. A.I.D. did so. However, because the second cash transfer program was at an earlier stage of design, the Mission's description to us at the time regarding end use of funds, as it turned out, did not match the implemented program. Further, the Congressional Notification for the second cash transfer program stated that the end use would be rediscounting of loans and not the purchase of interbank certificates of deposit.

We believe that tracking dollars only to their use for a macroeconomic purpose defeats the control that separate accounts were meant to provide. However, we are not making a recommendation since there is no A.I.D. policy regarding the use of cash transfer funds for the macroeconomic purposes of the Mission's two cash transfer programs and, therefore, there is no specific A.I.D. criteria by which to measure compliance.

Mission Comments and Our Evaluation

The Mission stated that, since their cash transfer program design proposals were discussed with, cleared and approved by A.I.D./Washington officials, the issue of trackability should not be addressed to them, but rather to A.I.D./Washington through another reporting vehicle. The Mission stated

that this audit report should focus only on whether the Mission complied with what was approved.

Our audit was to assess the financial and administrative systems established by the Agency to control its Assistance Program in Panama. In this regard the Mission has responsibility along with A.I.D./Washington for ensuring that appropriated funds are used as intended. As noted in our report, dollar tracking requirements were established to prevent abuse and diversion of dollar assistance. For example, the monitoring or tracking of A.I.D. funds merely to the purchase of a certificate of deposit, rather than tracking them to a specific final acceptable end use, such as a loan for an eligible private sector developmental objective, denies A.I.D. assurance that its funds were used as intended.

The Second Cash Transfer Program Is Not Functioning as Intended

The Private Sector Reactivation Program was not being implemented in accordance with the key controls established in Program Agreement. Under this cash transfer agreement, funds would be provided to banks for current increases in their medium- or long-term lending to the private sector. However, Program funds were actually provided to banks based on their past lending activity. This occurred because A.I.D. did not have a system to ensure agreement provisions were met. As a consequence, \$107.9 million in Act funds could be expended without promoting private sector development as intended by the cash transfer program.

Recommendation No. 2: We recommend that USAID/Panama restructure its cash transfer program assistance for promoting private sector development, so that it can be assured that Act funds are having a direct impact on that intended result.

Proper monitoring by a mission helps ensure A.I.D. assistance provides its intended effect. In this regard Handbook 1, Part IV and cable guidance on cash transfer assistance require:

...adequate monitoring and audit rights agreed to by the recipient, a monitoring commitment by A.I.D. staff, periodic substantive reporting by the recipient, and dollar redeposit or other remedial action in cases of noncompliance with the agreement on uses.

Regarding such oversight, the Mission's final planning document, the Program Assistance Approval Document (PAAD), for the \$107.9 million Private Sector Reactivation Program states, "...A.I.D. cannot and will not

monitor, audit, or account for any of the loans made by the private banking system". On the other hand, the PAAD under the heading of "Monitoring", stated that "...program success will be measured on the basis of the annual increase in loans outstanding to the private sector".

The Program Agreement did, however, contain very specific criteria regarding the basis for expenditures of program funds. This criteria provided:

Banks that plan to expand their medium and long term portfolio (loans between one and five years) may submit to the BNP [the National Bank of Panama--the Government of Panama's implementing agent] a description of such incremental lending that they plan to make in the next thirty days. The proposed increase in medium and long term lending must be for investments in plant and equipment for new project activity, construction, mortgages for newly constructed buildings or for incremental working capital. If the proposed increase in medium and long term portfolio meet the requirements of the program, BNP will agree to purchase [with Act funds] Interbank Certificates of Deposits (ICDs) from the PB [participating bank] equal to one half of the value of the subsequent actual new medium and long term credit extended by the PB... The purchase of ICDs will take place after the PB submits documentation... evidencing the actual increase in new medium and long term lending.

This Agreement wording--"...lending that they plan to make in the next thirty days... proposed increase... newly constructed buildings....[and] subsequent actual new medium and long term credit...."--clearly establishes how Program funds leverage and are linked to proposed increases in lending to the private sector.

The Mission permitted the National Bank of Panama to develop and use procedures which significantly deviated from the Agreement. For example, the procedures did not provide for participating banks to submit a description of incremental lending they plan to make in the next 30 days, nor did it provide for the purchase of ICDs from these banks based upon implementation of this planned lending activity--two very critical agreement terms. For example, although the agreement refers to lending activity that participating banks plan to make within next thirty days (and then actually make), the National Bank's procedures define new loans as those made after July 24, 1990, the date the Program Agreement was signed. By following these procedures the National Bank was unable to provide Program funds based on its prior review of agreed upon lending activity as

required by the Program Agreement, because proposed future lending was not part of the application process.

By purchasing the participating banks' ICDs which were supported only by prior lending activity, the National Bank did not meet the Agreement terms which are critical to linking program expenditures to incremental lending activity that would not have occurred absent the A.I.D. program. Consequently, A.I.D. was not assured, in the absence of monitoring the basis for Program expenditures, that those expenditures were, in fact, relatable to reactivating the private sector as intended.

To obtain a more complete understanding of what the expenditures of program funds were actually based upon, we reviewed five application forms from participating banks requesting Program funds. These applications represented over 25 percent (\$9.4 million) of Program expenditures through April 30, 1991. The review showed that in all five cases the banks' lending activity described in the applications occurred before the banks' request for Program funds from the National Bank.

In the first case, a bank, on June 29, 1990, had disbursed a \$90,000 loan for a mortgage on a private residence. The bank's files showed the house was originally deeded in 1986. On March 11, 1991, based on this lending activity, the bank requested and later received \$45,000 in Program funds.

In the second and third cases, two different banks, after the Mission's February 4, 1991 approval of a change to Program guidelines allowing new bond purchases as a lending activity, submitted documentation of their October 1990 bond purchases totalling \$8 million in order to obtain \$4 million in Act funds. These bonds financed the expansion of a brewery and the purchase of associated equipment and machinery from Germany valued at about \$3.4 million.

The fourth case involves a bank's February 5, 1991, application for Program funds supported by a \$10.7 million loan it had made for a 737 jet aircraft. For that loan, which was made on December 28, 1990, the bank received \$5.35 million in Act funds.

Lastly, the fifth case involves a bank's March 11, 1991, application for Program funds backed by a loan it had made on August 1, 1990--a \$108,000 mortgage loan on a commercial building completed in 1989. This loan was included in a \$4.3 million portfolio of loan applications which resulted in the bank receiving \$2.2 million of Act funds. A representative of the bank stated that about 25 percent of that amount was for mortgages of existing structures, not new construction.

The cited purchases of banks' ICDs clearly show that program funds were released based upon prior loan activity rather than on their planned increases in lending for new economic activity as required by the Program Agreement.

In light of the fact that Program is not functioning as stated in the agreement and considering that A.I.D. lacks assurance that the Program is fulfilling a justified need (see discussion on page 15), we believe the Mission should take the necessary steps to ensure that remaining Act funds actually assist private sector development.

Mission Comments and Our Evaluation

The Mission disagreed that the Program was not functioning as intended and stated that:

It appears that the basis for the RIG's position is a different interpretation of the statement in the Agreement that "Banks that plan to expand their medium and long term portfolio... may submit to the BNP (National Bank of Panama) a description of such incremental lending that they plan to make in the next thirty days." The RIG has interpreted this to mean that Program funds can only be disbursed after receipt and concurrence with a bank's lending plan.

The Mission disagrees. The operative phrase in the Agreement is "may submit." Such a phrase does not establish a requirement. In fact, the Agreement goes on to state that "The purchase of [ICDs] will take place after the participating bank submits documentation... evidencing the actual increase in new medium and long-term lending."

The Mission's comment that the words "may submit" do not impose a requirement on participating banks to submit documentation of proposed lending activity, removes any direct linkage between the Program and leveraging private funds for private sector development. Furthermore, in proposing this Program to A.I.D./Washington for approval, the Mission stated that:

Banks that plan to expand their medium and long term loan portfolios will submit [emphasis added] to the BNP [National Bank of Panama] a description of the incremental lending they plan to make within the next 30 days.

Also, in quoting the Agreement, the Mission excluded a key Agreement control (as reported on page 24) which provided that the purchases of ICDs would occur when subsequent actual new medium- and long-term credit is extended by the participating banks.

The Mission further commented that:

The RIG has also focused on a concern that Program activity be restricted to "new" loans.... "New" is any activity which occurred subsequent to the signing of the Program Agreement since that is when funds became available to contribute to the reactivation process.

The Agreement did not provide for "new" lending as being that which occurred after signing of the Agreement on July 24, 1990. Both the Agreement and the proposal for the Program contain controls in an effort to help A.I.D. tie its funding to increased private sector development by providing for submission and approval of proposed loans **before** the loans were made. As discussed in this report, this key control mechanism was bypassed thereby allowing banks to obtain A.I.D. funds based upon loans already in their portfolios. Accordingly, banks desiring these funds needed only to review their existing portfolios and submit an application based on loans made after July 24, 1990.

As a result, we believe that the funds expended under this Program cannot be linked to reactivation of the private sector. By not requiring that the Program be implemented in accordance with the terms of the Agreement, a linkage was not established and A.I.D. was denied whatever assurance those terms provided that A.I.D. funding was benefitting private sector reactivation.

The Mission stated that the implementing agency's requirement that the banks make their loans prior to receiving Program funds imposed a criterion more stringent than called for by the Agreement.

As shown on page 24, the Agreement required banks to provide evidence that "actual" lending had been made prior to receipt of Program funds.

Cash Transfer Evaluations Were Deferred

Evaluations, called for by the cash transfer program agreements to be conducted shortly after the end of 1990, had been deferred. Mission personnel stated that this was done because it was too early in program

implementation to perform evaluations. However, after discussion with Mission management of our concerns of the Private Sector Reactivation Program, they contracted for an evaluation of this Program.

Did A.I.D. obligate, expend, and account for the Assistance Program's funds in accordance with Agency policies and procedures?

A.I.D. is obligating, expending, and accounting for the Assistance Program's funds in accordance with Agency policy and procedures. However, the Mission Accounting and Control System information, maintained by the Mission's accounting station, USAID/Costa Rica, was not current for funds expended on one project because of delays in receiving transaction documentation from A.I.D./Washington/FM.

To answer this objective six criteria were reviewed: five were complied with and one was partially complied with. The specific criteria reviewed and results are detailed in Appendix V.

A.I.D. policies and procedures for obligating, expending, and accounting for funds are found in A.I.D. Handbook 19 and the Controller's Guidebook. Our review focused on A.I.D.'s accounting system as it applies to Economic Support Fund assistance. Specifically, we reviewed the accounting controls relating to funds control and payments. Funds control relates to organizational control points and assures fund availability prior to any commitment to expend. Payment controls ensure that no funds are disbursed unless properly authorized and that cash advances are not in excess of recipient needs. For the items tested, we found these controls implemented and complied with.

However, A.I.D./Washington/FM was not promptly transmitting financial information relating to one of the Mission's projects and project personnel had not taken effective action to obtain the missing information as discussed next.

Mission Accounting and Control System Information Could Be More Accurate for One Project

GAO's Standards For Internal Controls in the Federal Government require that transactions and other significant events be promptly recorded. However, the financial status of projects receiving advances by Letter of Credit was not current in the Mission Accounting and Control System. This occurred because A.I.D./Washington/FM did not promptly notify the Mission or its accounting station USAID/Costa Rica that payments had been processed. In addition, vouchers needing administrative approval by the Mission, and also needed by the Mission's accounting station for the purpose of more accurately accruing expenditures, were retained by A.I.D./Washington/FM for periods up to nine months before being transmitted.

Project payments made by Letter of Credit are made from the accounts of A.I.D.'s Financial Management Office in Washington, D.C. (A.I.D./Washington/FM). In the A.I.D. accounting system, an accounting event, such as processing an expense voucher, must be documented. These actions are then promptly recorded as required under the Federal Managers' Financial Integrity Act of 1982 with reference to the GAO standards for internal controls.

A mission or its accounting station must receive information regarding project payments liquidating draws on Letters of Credit from A.I.D./Washington/FM before it can record such payments. The accounting station for USAID/Panama was not receiving this information or associated expense vouchers for the Mission's Central American Peace Scholarship Project from A.I.D./Washington/FM for periods of up to nine months.

These vouchers required administrative approval by the Mission's Project Officer, and were needed by the Mission's accounting station for updating previous Project Officer estimates of accrued expenditures for this Project. Three vouchers, totalling \$2.3 million⁵, arrived on April 22, 1991, shortly after our inquiry, and were administratively approved on May 2, 1991.

Though, these vouchers were not being sent, the Project Officer had been preparing estimates of Project expenditures for entry as accrued expenditures into the MACS.

⁵ Although the Central American Peace Scholarship Project was provided \$5.45 million in Act funding, the audit did not determine whether the cited \$2.3 million were provided under the Act or were from earlier appropriations.

According to accounting station personnel, the Project Officer's estimate totalled \$2.7 million as of March 31, 1991, and that amount was used for the quarterly reporting of accrued expenditures to A.I.D./Washington. A more accurate accrual estimate would also have been possible had the Project Officer received the quarterly financial reports from the Project implementing entity as required by the contract. Although the Project Officer stated that inquiries were made requesting these reports (also up to nine months behind) and the vouchers, the files disclosed just one documented request dated April 12, 1991, which stated "as per the auditors request...".

We believe additional follow-up effort by the Mission is possible in situations such as the above. However, for the present, this matter is resolved and the accruals are current. Consequently, no recommendation is considered necessary.

Issues Needing Further Study

As discussed in Appendix III, several issues noted during our first audit for the period ended November 30, 1990 were not resolved during the current audit period nor addressed by a specific recommendation in the present audit. These unresolved issues are:

- Under the Private Sector Reactivation Program, in order to provide liquidity to Panama's banking system, A.I.D. continues to purchase interbank certificates of deposit (ICD's) for one half of the qualifying loans made by private banks. The ICD's are backed only by the good faith of the institutions. Thus, should an institution fail a loss of program funds could occur. As of May 31, 1991, about \$40 million in Act funding had been used to purchase ICDs from private banks. The Mission believed the Government of Panama's agreed-to reviews of its banking system would minimize this risk. However, no reviews had been completed as of May 31, 1991. Mission officials stated that the Government of Panama reviews have been started. Consequently, an assessment needs to be made as to the adequacy of these reviews.
- The Immediate Recovery Project Amendment provided \$1.9 million of food and shelter assistance to displaced families. Primarily this assistance is for catered food deliveries, through two local restaurants, to four Project feeding sites. The Mission orders a specific number of

meals from the restaurants who make delivery of the food in bulk. There is no contract specifying serving sizes and no procedures to verify that the bulk amount of food delivered equals the number of meals ordered. This procedure remained the same through the end of our audit period. The Mission plans to discontinue catered food deliveries as of June 30, 1991.

- Under the Private Sector Scholarships Project, the implementing entity, the Private Sector Council for Educational Assistance (COSPAE), has not demonstrated that it has the ability to contract and account for the training activities to be conducted through U.S. organizations. Therefore, COSPAE may not be able to adequately control and account for Agency funds. Although COSPAE had made some progress in this regard during this reporting period, additional review is needed to evaluate whether further improvements are needed in accounting, procuring, contracting, organizing training programs, and generating training funds.

In addition the following issue was partially reviewed during the present audit and requires further study.

- A.I.D. Handbook 3 guidance, specifies five elements to be included in a project design to permit evaluation. While this audit did not review this area in detail, we did note that two bilateral projects and one operational program grant for which agreements had been signed through May 31, 1991 did not include logical frameworks as required per Handbook guidance.

REPORT ON INTERNAL CONTROLS

Scope of Our Internal Control Assessment

We have audited USAID/Panama's Assistance Program funded by Public Law 101-302, through May 31, 1991, and have issued our report thereon dated September 12, 1991. This Section is a summary of our assessment of internal controls for the audit objectives.

We performed our audit in accordance with generally accepted government auditing standards, which require that we (1) assess the applicable internal controls when necessary to satisfy the audit objectives and (2) report on the controls assessed, the scope of our work, and any significant weaknesses found during the audit. We limited our assessment of internal controls to those controls applicable to the audit's objectives and not to provide assurance on the auditee's overall internal control structure.

We classified significant internal control policies and procedures applicable to each audit objective by categories. For each category, we identified the relevant policies and procedures and determined whether they have been placed in operation--and we assessed control risk. We have reported these categories as well as any significant weaknesses under the applicable section heading for each audit objective.

General Background on Internal Controls

Under the Federal Managers' Financial Integrity Act of 1982 and the Office of Management and Budget's implementing policies, A.I.D.'s management is responsible for establishing and maintaining adequate internal controls. The General Accounting Office has issued "Standards for Internal Controls in the Federal Government" to be used by agencies in establishing and maintaining internal controls.

The objectives of internal controls and procedures for Federal foreign assistance are to provide management with reasonable--but not absolute--assurance that resource use is consistent with laws, regulations, and

policies; resources are safeguarded against waste, loss, and misuse; and reliable data is obtained, maintained, and fairly disclosed in reports. Because of inherent limitations in any internal control structure, errors or irregularities may occur and not be detected. Predicting whether a system will work in the future is risky because (1) changes in conditions may require additional procedures or (2) the effectiveness of the design and operation of policies and procedures may deteriorate.

Conclusions for Audit Objective One

Our first objective was to determine if A.I.D. followed the Act and additional Congressional guidance in designing the Assistance Program. This involved gathering and verifying information on the programs and projects which make up the Mission's Assistance Program portfolio. For this objective the applicable internal controls are covered under audit objective two, i.e., design planning and implementation. However, regarding the audit objective A.I.D. planned the Assistance Program to include the activities intended by the Congress.

Conclusions for Audit Objective Two

Our second objective was to determine if A.I.D. followed its policies and procedures which control the implementation, to include planning, of individual Assistance Program activities. For this objective, the following control processes were assessed:

- the Country Development Strategy Statement and Action Plan process,
- the planning documentation process,
- the Congressional notification process, and
- the agreement process.

Our review of the Agency's internal controls for these processes showed that the Mission had not always followed certain general controls, but, except for the reportable problem noted below which was an analysis issue in applying a general control, the failure to follow the controls was being corrected by the Mission or the implementation process had reached a point whereby correction was not possible.

- The Mission's planning efforts did not justify the need for the credit expansion subprogram of the Private Sector Reactivation Program. Without demonstrating and supporting the need for this subprogram,

there is an increased risk that program funds may be expended and not fulfill a justified need.

Conclusions for Audit Objective Three

Our third objective was to determine if A.I.D.'s system for monitoring, evaluating, auditing, and reporting was being implemented with regard to Assistance Program activities. For this objective the following control processes were assessed:

- the monitoring and evaluating processes,
- the auditing process, and
- the reporting process.

Our review showed the Mission had not followed certain of the Agency's internal controls related to monitoring and evaluation but that it had followed controls for reporting. Regarding monitoring and evaluation the Mission had not (1) issued a Mission Order formally establishing its monitoring and evaluation system, (2) prepared information plans as part of its assistance designs, or (3) conducted an evaluation of the first cash transfer program as specified in the assistance agreement. However, we did note the following two reportable problems where the design or application of the Mission's monitoring was not adequate.

- The Mission had permitted the Private Sector Reactivation Program to be implemented outside the terms of the program agreement. In this manner, there was no link between program expenditures and intended results. As a consequence there is a risk that program expenditures will not further the program purpose.
- In designing both cash transfer programs the Mission, with A.I.D./Washington/LAC approval, decided to track most of the dollars only to the extent that it could be shown that the dollars would be applied to macroeconomic purposes. We believe that tracking dollars only to their use for a macroeconomic purpose defeats the control aspect of placing dollars in noncommingled bank accounts (required by Section 592(b) of the 1990 Appropriations Act) prior to their disbursement for final acceptable uses. Since the final acceptable uses are defined at such a high level, A.I.D. is not in a position to detect abuse or diversion of dollar proceeds.

Conclusions for Audit Objective Four

Our final objective was to determine if A.I.D. obligates, expends, and accounts for the Assistance Program's funds in accord with Agency policies and procedures. For this objective the following control processes were assessed:

- the funds control process,
- the payment process,
- the closing process, and
- the reporting process.

Our review showed, for the items tested, the Mission had applied the Agency's internal controls related to these processes.

REPORT ON COMPLIANCE

Scope of Our Compliance Assessment

We have audited USAID/Panama's Assistance Program funded by Public Law 101-302, through May 31, 1991, and have issued our report thereon dated September 12, 1991. This Section is a summary of our assessment of compliance for the audit objectives.

We conducted our audit in accordance with generally accepted government auditing standards, which require that we plan and perform the audit to fairly, objectively, and reliably answer the audit objectives. Those standards also require that we:

- assess compliance with applicable requirements of laws and regulations when necessary to satisfy the audit objectives (which includes designing the audit to provide reasonable assurance of detecting abuse or illegal acts that could significantly affect the audit objectives) and report all significant instances of noncompliance and abuse, and all indications or instances of illegal acts that could result in criminal prosecution that were found during or in connection with the audit.

We tested the Mission's compliance with the Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act, the Federal Manager's Financial Integrity Act of 1982, the Foreign Assistance Act of 1961, the Foreign Operations, Export Financing, and Related Programs Appropriations Act of 1990 (the 1990 Appropriations Act), and A.I.D./host country/implementing agency agreement provisions as they could affect our audit objectives. However, our objective was not to provide an opinion on the Mission's overall compliance with such legal or agreement provisions.

General Background on Compliance

Noncompliance is a failure to follow requirements, or a violation of prohibitions, contained in statutes, regulations, contracts, grants and

binding policies and procedures governing entity conduct. Noncompliance constitutes an illegal act when there is a failure to follow requirements of laws or implementing regulations, including intentional and unintentional noncompliance and criminal acts. Not following internal control policies and procedures in the A.I.D. Handbooks generally does not fit into this definition of noncompliance and is included in our report on internal controls. Abuse is distinguished from noncompliance in that abusive conditions may not directly violate laws or regulations. Abusive activities may be within the letter of the laws and regulations but violate either their spirit or the more general standards of impartial and ethical behavior.

Compliance with the Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act, the Federal Managers' Financial Integrity Act of 1982, the Foreign Assistance Act of 1961, the 1990 Appropriations Act, and agreement provisions is the overall responsibility of the Mission's management.

Conclusions on Compliance

The Mission complied with the Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act, the Federal Managers' Financial Integrity Act of 1982, the Foreign Assistance Act of 1961, the 1990 Appropriations Act, and agreement provisions as they applied to our audit objectives.

SCOPE AND METHODOLOGY

Scope

We audited the Mission's Assistance Program funded with the \$420 million provided by Public Law 101-302 in accordance with generally accepted government auditing standards. This Assistance Program consists of two cash transfer programs and sixteen development projects. We conducted the audit from March 4 through July 5, 1991, and covered the Assistance Program's design in relation to Public Law 101-302 and associated Congressional committee reports, as well as A.I.D. systems and procedures relating to implementation, monitoring and accounting for program components, activities, and funds. The audit period was May 25, 1990 through May 31, 1991. Fieldwork was conducted in the offices of USAID/Panama, USAID/Costa Rica (the official accounting station for USAID/Panama), the National Bank of Panama, Panama's National Banking Commission, and six private Panamanian banks.

The audit objectives did not cover the following areas:

- Our audit tests of whether the Assistance Program was implemented in accordance with A.I.D.'s policies and procedures was limited to reviewing the Mission's planning for its activities, except for a judgmentally selected sample of programs and projects for which we reviewed the Mission's monitoring of Assistance Program implementation. Due to time limitation we did not always extend audit testing to determine the negative effects of A.I.D. not following handbook provisions.
- We excluded four projects from the scope of our review. Three of these, project Nos. 525-0305, 525-0310 and 525-0311, were budget transfers to other U.S. Government entities. A.I.D. Handbook 12 on use of Federal agencies does not provide guidance for such situations so it was not clear that these should be considered as projects for purposes of following the guidance contained in A.I.D. Handbook 3

on project assistance. However we did request the Department of Justice (DOJ) to audit project No. 525-0305 to determine whether the DOJ's implementation, monitoring and accounting for the project is in accordance with the DOJ's policies and procedures. The fourth project (525-0300) was designed prior to the passage of the Act and implementation activities were completed shortly after the Act-funded Assistance Program began. Act funds merely reimbursed the original sponsor. We therefore considered this project to be outside the scope of our review.

- We did not audit controls over project development and operating expenses because we believe that the Congressional intent is to audit the direct assistance provided to Panama.
- We did not audit the computerized segment of the Mission Accounting and Control System (MACS). Thus we were only able to observe its workings in terms of original input documents and report outputs.

In addition, we have used and reported A.I.D.-provided, but unaudited data, e.g., that disclosed at Appendix IV.

Methodology

Our audit was conducted in accordance with generally accepted government auditing standards. The methodology for each audit objective follows.

Audit Objective One

To accomplish the first audit objective, we obtained and reviewed the Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act, Public Law 101-302 (Act), selected sections of the House Conference Report 101-493 with the attached Joint Explanatory Statement of the Committee of Conference; and excerpts from the House Committee on Appropriations Report 101-434, the Senate Committee on Appropriations Report 101-272, and the Congressional Record dated May 22, 1990, regarding the Conference on H.R. 4404. We examined the Mission's portfolio of activities planned or in progress designed to carry out the intentions of the Congress for using the \$420 million provided by the Act. The planned purposes and objectives of these activities were compared with the requirements of the

Act and the above associated guidance to determine whether the actions A.I.D. is taking are responsive.

Audit Objective Two

To accomplish the second audit objective, we reviewed A.I.D. criteria and identified key control processes applicable to program and project implementation. As available, we reviewed the Country Development Strategy Statement, the Action Plan, the final design document, the agreement, and the Congressional Notification control documentation to evaluate their compliance with A.I.D. policy. We analyzed the Assistance Program's two cash transfer programs and nine of the development projects funded under Public Law 101-302 that, as of May 31, 1991, had approved final design documents.

Audit Objective Three

To accomplish the third audit objective, we determined whether the monitoring, evaluating, auditing, and reporting of the Mission's Assistance Program was done in accordance with guidance found in A.I.D. Handbooks 3, 4, and 13, and supplemental policy.

In performing the analysis of project monitoring, we reviewed Handbook criteria, telex, and other supplemental guidance. For cash transfer assistance we reviewed legal and A.I.D. policy requirements relating to the establishment of noncommingled accounts and tracking of US dollars to their end use.

We reviewed the two cash transfer programs and nine of the development projects which had final design documents, as of May 31, 1991, to assess whether Handbook requirements on planning for monitoring and evaluation activities had been followed. Also we selected the two cash transfer programs and, on a judgmental basis, a development project and subproject for detailed review to assess problems regarding the implementation of monitoring and evaluation activities for these programs and projects and to assess the Mission's monitoring of agreement reporting requirements. Judgmental sampling techniques were used because we believed they were adequate to achieve the audit objective.

Our work included interviews with officials of A.I.D. and certain implementing entities and organizations receiving the benefits of the Assistance Program. We also reviewed Mission general assessment

reporting under A.I.D.'s Payment Verification Policy No. 1 and a recent project implementation status report submitted by the Mission to the A.I.D./Washington/LAC Bureau.

Audit Objective Four

To accomplish the fourth objective, we reviewed selected criteria contained in A.I.D. Handbooks and we interviewed officials at the Mission, at the Mission accounting station at USAID/Costa Rica, and at A.I.D./Washington/FM. We examined Mission record files and accounting system reports documenting the budget allowance ledgers, the project agreements and amendments, the project ledger, element control ledgers, earmark control records and earmarking documents, commitment liquidation records, cash advance records, payment and liquidation vouchers, and advices of charge. Our accounting system review for development projects focused on the accounting processes for funds control and payments. System review for cash transfers was limited to the Mission's responsibility to certify compliance with conditions precedent prior to disbursement by A.I.D./Washington/FM into a separate account of the Government of Panama.

MANAGEMENT COMMENTS

AGENCY FOR INTERNATIONAL DEVELOPMENT
PANAMA CITY, PANAMA

UNITED STATES GOVERNMENT
MEMORANDUM

DATE: August 30, 1991

TO: Reginald Howard, RIG/A/T

FROM: Thomas W. Stukel, Mission Director 

SUBJECT: Mission Comments on Audit of The Panama Assistance Funded
By Public Law 101-302 as of May 31, 1991

USAID/Panama welcomes this opportunity to comment on the draft report of the subject audit. We recognize that the RIG/A/T staff dedicated considerable time and effort in preparing the report. We especially appreciated the opportunity to review the final draft in detail during your recent visit to Panama from August 20-22. After reading this draft, we are pleased to see that some of our oral comments were incorporated into the report. There remain, however, differences of opinion on some of your findings which we believe are not adequately reflected in the report. As a result, the reader does not have sufficient information to understand why the Mission proceeded as it did.

We have three principal comments on the report, each of which was discussed previously with RIG/A/T staff. They pertain to compliance with procedures established in Handbooks and policy guidance, the design analysis and implementation of the Private Sector Reactivation Program, and the extent to which cash transfer dollars are tracked.

In addition to these three areas, which are discussed in detail below, we believe more emphasis should be given to the context surrounding the Panama program. The Executive Summary provides some of that context, but more is needed. The U.S. Government invested considerable resources and made significant sacrifices (including the lives of 23 military personnel) in liberating Panama from the dictatorship of Manuel Noriega. Following those events, it also made a major commitment to supporting the economic recovery of the country.

The Administration sent several high level teams to Panama in late December, 1989 and early January, 1990, to identify immediate recovery needs as well as longer term reactivation requirements. Congress supported this commitment when, in February, 1990, it made funds available through the Urgent Assistance for Democracy in Panama Act, and followed that with the Dire Emergency Supplemental

which was signed by the President on May 25, 1990. Until late February, 1990, A.I.D. did not even have an accredited Mission in Panama.

The emergency produced by U.S. Government action required a rapid response. In order to meet the foreign policy imperative for immediate assistance to Panama, A.I.D. had to exercise great flexibility, a fact demonstrated by its action during the early days of operation as well as by decisions made in Panama and in AID/W.

Compliance with Program and Project Design Documentation Standards

We fundamentally disagree with the implication in the report that USAID/Panama did not comply with program and project design documentation standards.

Congress appropriated funds for Panama without a request from A.I.D. The Dire Emergency Supplemental was signed only three months after USAID/Panama was established. For that reason, the Mission submitted a Discussion Paper for AID/W review and approval instead of a traditional CDSS and Action Plan. AID/W recognized the extenuating circumstances faced by the Mission and accepted this document.

We believe the report should clearly recognize the circumstances under which the Mission was operating and explicitly accept the Mission's position (noted in the report on p. 9) that the Discussion Paper was sufficient to serve in the place of a CDSS and Action Plan. The report gives the reader the impression that the Mission simply ignored basic procedures when it is clear that circumstances dictated the course of action. Furthermore, to have prepared the Discussion Paper under those circumstances yet still provide the basis for AID/W decision makers to concur with the content of a major program initiative was a significant accomplishment that deserves to be recognized as such.

The discussion (pp. 10-11) on the extent to which Mission design documents satisfied Handbook standards is another example where the lack of context can confuse the reader. The discussion concludes on p. 11 by acknowledging that since the designs are set no recommendation is necessary, leaving the clear implication that the Mission did not comply with guidance. However, as the report notes on p. 10, Handbook 3, Chapter 2B states that a basic purpose of a PID is to "convince A.I.D. management that the preliminary proposal has merit, that it seems better than alternative solutions to the problem, and that it makes sense to devote personnel and financial resources to further develop the project." If, in fact, a final design effort is undertaken (i.e., a PP or PAAD is prepared), by definition A.I.D. management has decided that the fundamental purpose for a PID has been satisfied.

Moreover, the logical issue is not whether a PID or its equivalent exists or whether such a document includes the

information or analyses contained in Handbook 3; rather, concern should be with the quality of the final design since it is at that stage that the investment decision is made. This includes documentation for unsolicited proposals. Further, we find no reference in Handbook 3 which requires specific documentation; rather, as with all Handbooks, it provides guidance on what should be done while allowing for some flexibility when the circumstances dictate.

It is of great concern to us that the report imposes a more restrictive reading of the Handbooks than justified by their text. Such readings deny any flexibility whatsoever to A.I.D. and the Executive Branch in the conduct of foreign assistance in emergency situations such as the one in Panama. Contrary to what is implied in the report, foreign aid does not exist in a vacuum, and A.I.D.'s efforts in Panama are good examples of the types of innovative actions taken within legislative and regulatory constraints that are often necessary and appropriate to accomplish an immediate foreign policy objective.

In the same vein, while not taking issue with the fact that a Mission Order was not issued to formally establish a monitoring and evaluation system and that assistance design documents did not include a specific section on "information plans", we wish to state for the record that the Mission gives high priority to monitoring and evaluation. It is for this reason that, as noted on p. 14 of the report, our program and project agreements include numerous mechanisms that will generate the information required to allow the Mission to keep close track of implementation progress and to assure that funds are utilized for intended purposes.

Private Sector Reactivation Program

The report states that planning for one sub-component of this program was inadequate and that the program is not functioning as intended. The Mission disagrees on both counts.

The RIG's issue on adequate planning for the credit expansion sub-component appears to be that a formal "demand" study was not undertaken and, thus, the true "needs" of the private sector were not fully analyzed. We maintain that the design process provided sufficient information to conclude that the lack of medium to long term credit was a major constraint to private sector reactivation.

When the Program was being designed (April-June, 1990), considerable information was collected on the condition of both the banking system and the private sector which demonstrated that:

- Wholesale and retail businesses were in the process of rebuilding inventories that had been heavily looted following the events of December 20, 1989. (The American Chamber of Commerce estimated such losses at \$500 million).

- Manufacturing and industrial companies were replacing plant, equipment and inventory that was lost during the looting.
- Those manufacturing companies that had not been looted were in the process of carrying out much needed maintenance on their plant and equipment; something that had been postponed during the two years of crisis.
- Some \$1.2 billion in time deposits were still frozen in the banking system. The GOP was planning to unfreeze these accounts and the banks were allocating resources to a build up of their liquidity positions in anticipation of a bank run. The result was that essentially all deposits captured by the banking system were being used to increase their liquidity position and not for on-lending purposes.

As part of the design process, A.I.D. personnel conducted extensive interviews with bankers as well as businessmen which clearly identified the need to reactivate the banking system so it could serve its traditional role as lender to stimulate private sector growth. The interviews showed that the banks faced two problems: (1) an immediate concern about a possible run once accounts were unfrozen and (2) assuming that no run occurred, a lack of medium term funds to support working capital needs, investment in plant and equipment, maintenance and expansion.

The banks indicated that if a run did not occur, they had the short-term liquidity needed to meet short-term obligations. However, they were unwilling to use large amounts of short-term deposits to finance medium and long-term loans. This was because, before the crisis of 1987-1989, many banks had mismatched their portfolios with regard to the term structure of deposits and loans. They had used short-term funds to finance medium and long-term activities (such as plant and equipment financing) and, during the crisis, found themselves in the unenviable position of having to face massive withdrawals without being able to access their assets. This created severe cash flow problems causing banks to force customers to pre-pay loans and cut off credit to their best customers in order to conserve cash.

In response to this situation, the Mission proposed a Program to (1) provide immediate liquidity to Panamanian banks that experienced a liquidity problem due to a bank run and (2) support medium-term credit expansion by the banking system to the private sector through the purchase of interbank certificates of deposit.

When restrictions on time deposits were lifted on July 10, 1990, a bank run did not take place. It is not unreasonable to conclude that the A.I.D. Program itself, announced shortly after the unfreezing, served to enhance the confidence of depositors who in turn did not withdraw funds from the banking system on a massive scale. It also meant that all resources available under the

Program could be devoted to the credit expansion sub-component.

The Program moved rather slowly at first, but then showed a dramatic increase in usage. Figure 1 shows Program drawdowns on a monthly basis. Rather than attempt to tie drawdowns to a reduction in the interest rate or other minor changes (p. 13), the report should note that a number of factors, especially the local political situation, had an effect on investor confidence and, thus, willingness to contract long-term debt. These include heated discussions on the country's economic strategy during 1990, an attempted coup in December 1990 and a Cabinet shakeup in April 1991. These local political events track closely with the rate of drawdown of Program funds which shows little activity through January 1991, a spurt in activity in February and March 1991, limited activity in April and May and major movement in June and July.

The lessons learned during the crisis are reflected in how banks do business today. With the banking system currently at less than half the pre-crisis level of deposits (\$10.9 billion in June 1991 versus \$26.7 billion in June 1987), bankers are making a more determined effort to match the terms of their assets and liabilities. The Private Sector Reactivation Program is a source of funds which allows a bank to increase its medium term deposit base so that it can in turn increase its medium term loan portfolio. A recently completed independent evaluation of the Program shows that, as a group, the participating banks' increase in medium-term lending has been greater than their drawdown of Program funds. This provides clear evidence that the Program not only stimulated increased medium-term lending but also leveraged increased medium-term lending with the banks' own resources.

Hindsight thus proves that our initial analysis was accurate and that there was clearly a strong, pent-up demand for medium and long-term credit to support private sector reactivation. As of August 16, 1991, A.I.D. had disbursed the full \$107.9 million under the Program because of the heavy demand by the private sector for these funds. This is very close to the original 12 month time frame that was envisioned for disbursing Program funds. We note, too, that the DAEC concurred with the Mission's initial analysis and, in accordance with its authority, recommended that the AA/LAC approve the Program. This was done on July 16, 1990.

Regarding the issue on compliance with the terms of the Program Agreement, the Mission is satisfied that implementation of the Program complies with the Agreement. It appears that the basis for the RIG's position is a different interpretation of the statement in the Agreement that "Banks that plan to expand their medium and long term portfolio...may submit to the BNP (National Bank of Panama) a description of such incremental lending that they plan to make in the next thirty days." The RIG has interpreted this to mean that Program funds can only be disbursed after receipt

and concurrence with a bank's lending plan.

The Mission disagrees. The operative phrase in the Agreement is "may submit." Such a phrase does not establish a requirement. In fact, the Agreement goes on to state that "The purchase of [ICDs] will take place after the participating bank submits documentation...evidencing the actual increase in new medium and long-term lending." The GOP followed this to the letter by requiring that the banks make their disbursement on new loans prior to the disbursement of Program funds to the banks.

For many banks in Panama, there is a significant gap between the time it approves a loan and when funds are disbursed. The reason is that many loans are guaranteed by collateral which often includes property. In order to put a lien on a piece of property, banks (with the borrower's approval) must submit certain documents to the Public Registry. It can take up to four months to complete this process. Had funds been disbursed on the basis of loan approvals rather than disbursements, U.S.G. resources might have been tied up for an unacceptable length of time.

On this basis, the GOP proposed a more stringent criterion -- i.e., that banks show that they have already made their disbursements against new loans. The Mission found this to be in full accord with the terms of the Agreement and, more importantly, good cash management.

The RIG has also focused on a concern that Program activity be restricted to "new" loans. The purpose of the Program is to contribute to reactivation of the private sector. "New" is any activity which occurred subsequent to the signing of the Program Agreement since that is when funds became available to contribute to the reactivation process. This is also consistent with the objective of leveraging private funds by seeing that investments are made prior to the purchase of ICDs. Refinancing old loans, i.e., those approved prior to the date that Program funds became available, is not an eligible use of Program funds.

The National Banking Commission (CBN) is responsible for auditing the Participating Banks to insure that they comply with all rules and regulations established in the Agreement and the Operations Manual. The CBN has developed an audit plan and will report on their findings as they implement the plan. Any instances of ineligible activities, such as the first example provided in the report (p. 19), will be identified during this process, and the CBN will apply the appropriate sanctions to the respective bank. These can be as severe as prepaying all ICDs and not being allowed future access to the Program.

In summary the Mission believes there has been full compliance with the letter and spirit of the Program as described in the Agreement.

Tracking of Cash Transfer Dollars

The final major area where the Mission takes exception to the report is the discussion on the tracking of cash transfer dollars. As noted on p. 16 of the report, A.I.D.'s preference is to use cash transfers for import financing. The A.I.D. policy, however, does not limit cash transfers to this purpose; rather, it anticipates that situations will vary among countries which will call for different approaches depending on the situation encountered. In designing its cash transfer programs, USAID/Panama recognized that its proposals were breaking new ground. It was for this reason that RIG staff were invited to Panama in June, 1990, to review the design and provide comments at that very early date.

When the PAADs for the respective programs were reviewed by AID/W, the issue of the proposed design and the implications for tracking dollars was raised and discussed in detail. After hearing the arguments, and with clearance from PPC and GC, the AA/LAC -- the authority in AID/W empowered to act on the issue -- determined that the proposed design was appropriate given our objectives in Panama and consistent with existing Agency policy. Both PAADs were subsequently authorized by AID/W as proposed by the Mission.

USAID/Panama maintains, therefore, that for the purposes of this audit report RIG must limit its comments to the extent to which implementation of the two programs did or did not comply with what was approved by the AA/LAC. In that context, we believe we have complied and that the report cannot claim (p. 17) that "there is no specific A.I.D. criteria by which to measure compliance."

If the RIG is concerned that tracking cash transfer dollars only to their use for a macroeconomic purpose defeats the control measures for which separate accounts were established, it should bring that issue to the attention of A.I.D. management through a different channel than this audit report and suggest that A.I.D. consider modification of current policy on the use of cash transfer dollars. Until such a modification is made, however, we reiterate that the two programs were determined by the appropriate authorities to be consistent with A.I.D. policy and, therefore, this audit report should focus only on whether the Mission complied with what was approved under existing policy.

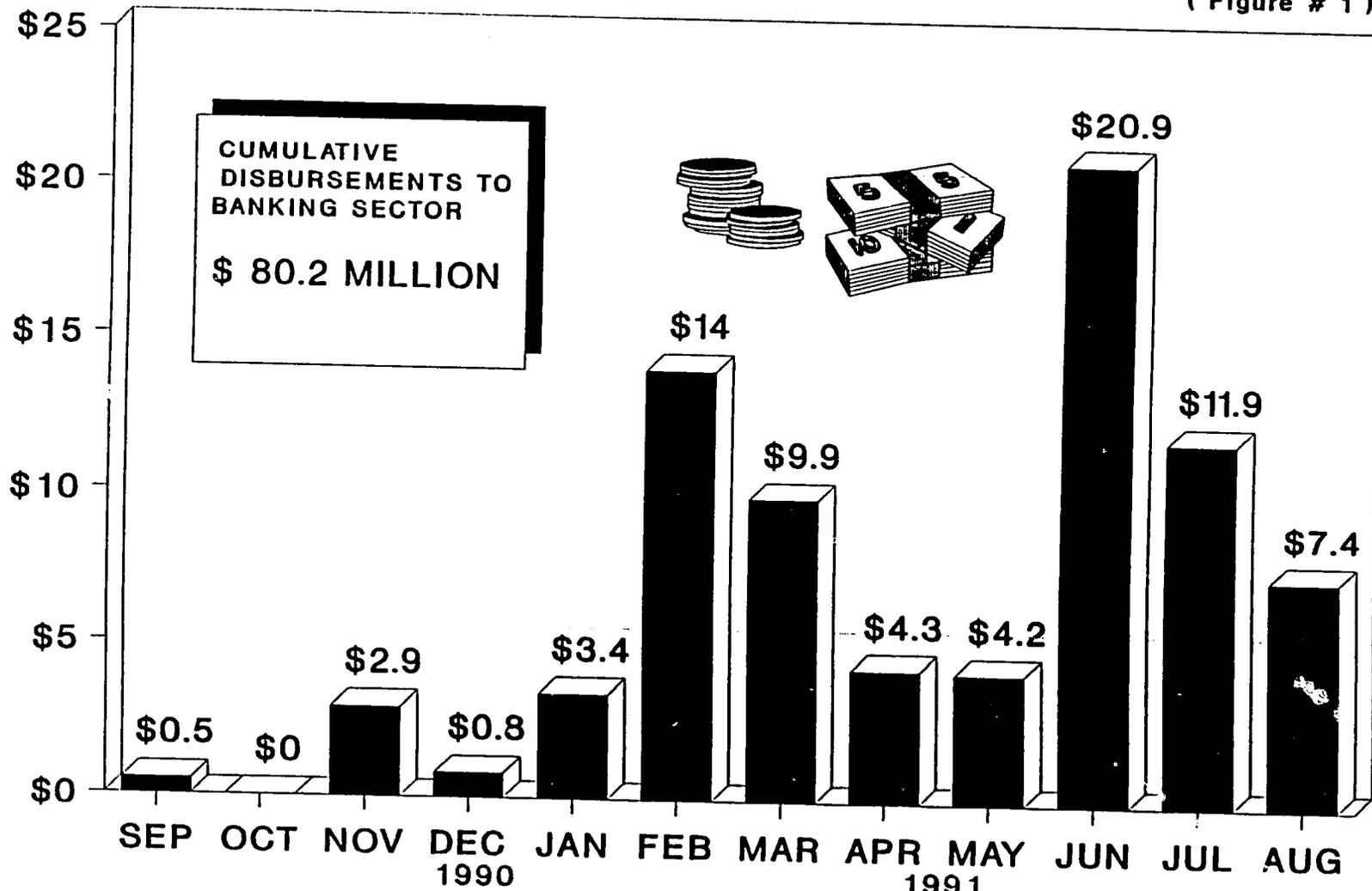
In conclusion, the Mission strongly believes that it has implemented all aspects of its program in a manner consistent with guidance provided by Congress and AID/W.

We understand that our comments will be attached in their entirety to the final audit report.

MONTHLY MOVEMENT OF FUNDS PRIVATE SECTOR REACTIVATION PROGRAM

USAID GRANT IN MILLIONS

(Figure # 1)



AUGUST 26, 1991

Previously Reported Issues

The following are apparent weaknesses which existed in the Assistance Program in Panama as of November 30, 1990, as disclosed in our Audit Report No. 1-525-91-005 dated February 8, 1991, and the resolution status of these weaknesses as of May 31, 1991.

Apparent Weakness Reported

- Under the first cash transfer, the Economic Recovery Program, A.I.D. funds amounting to \$113.85 million were transferred into a commingled account to support Panama's public sector investment budget and accordingly cannot be traced to their final expenditure. While the agreement specifies prohibitions on the uses of the funds, this arrangement does not permit A.I.D. to monitor their use.
- Under the second cash transfer, the Private Sector Reactivation Program, A.I.D. provides liquidity to Panama's banking system by purchasing interbank certificates of deposit (ICDs) for one half of the value of qualifying loans made by private banks. The ICDs are backed only by the good faith of the institutions.
- A \$240,000 subproject for Civic Education under the Democratic

Resolution Status

This remains a problem but is a function of program design and difficult to change at this time. See report section entitled "Cash Transfer Dollars Could Have Been Tracked in Greater Detail".

This remains a potential problem and is a function of program design. As of May 31, 1991, about \$40 million of program funds had been used to purchase ICDs from private banks. The Mission believed the GOP's normal supervision of its banking system minimized this risk. However, no reviews had been completed as of May 31, 1991. Mission officials stated that the reviews have been started. Consequently, an assessment needs to be made as to the adequacy of these reviews.

This problem has been resolved as the subproject is now progressing

Initiatives Project has the basic purpose of creating a new center within a Panamanian nonprofit organization so that center can pursue an ambitious agenda of activities. However the new center is basically an idea that needs to be developed into a functioning organization and has not yet developed the financial and accounting systems to account for and control A.I.D. funds.

- For the Immediate Recovery Project Amendment component providing \$1.9 million of food and shelter assistance to displaced families, most of the assistance goes to two local restaurants which catered food deliveries to four project feeding sites. The Mission orders meals from the restaurants but the deliveries are made in bulk. There is no contract specifying serving sizes and no procedures to verify that the bulk amount of food delivered equals the number of meals ordered.
- Under the Private Sector Scholarships Project, the implementing entity, COSPAE, has not yet proven its ability to contract and account for training activities to be conducted through U.S. organizations, and therefore it may not be able to adequately control and account for the funds. Matching contributions is another area of weakness since due to the Mission's two-year closing it has not monitored these contributions as called for by the agreement.

well. The subproject grantee has provided a subgrant to the Civic Crusade, and the Pro-Democracy Center has been established. Also an accounting system was incorporated to account for A.I.D. funds.

This remains a potential problem as the procedures have not changed. However, the number of people in the shelters has been greatly reduced and the Mission plans to discontinue catered food deliveries by June 30, 1991.

Although COSPAE made some progress during the reporting period, additional review is needed to evaluate whether further improvements are needed in accounting, procuring, contracting, organizing training programs, and generating training funds. The Mission is now monitoring COSPAE's contribution.

- Under the Improving Police Services Project, funds for project implementation were transferred from A.I.D. to the Department of State and from State to the Department of Justice (DOJ). Due to the urgency of the situation in Panama (which did not have a standing police force once the military regime was unseated) the funds were transferred without going through the analytical and review processes that would normally be called for on a project of this magnitude.
- The Mission project officers do not administratively approve expenses incurred in Panama by U.S. Private Voluntary Organizations (PVOs) under regional agreements.
- With regard to the Central American Peace Scholarship Project, the Mission does not know if the costs of Georgetown University have been audited. Although the project officer has been able to monitor costs and student progress through other reports, it appears that the Mission should reinstate administrative approval of vouchers and obtain copies of audits to determine if there has been any audit coverage of its contract.

After signing the Memorandum of Agreement with the Department of State, the LAC/Bureau requested that a Project Paper be prepared by the implementing entity, the Department of Justice's International Criminal Investigative Training Assistance Program (ICITAP). A description of the DOJ's proposed program was prepared but the program description has never been subjected to formal interagency review. We requested the DOJ Assistant Inspector General for Audit to review ICITAP's activities under the Project with regard to their compliance with DOJ's systems for planning, implementing, monitoring, evaluating, and reporting.

This problem has been resolved as the PVO's submit financial information in accordance with the uniform administrative requirements of Office of Management and Budget (OMB) Circular A-110.

This problem has been resolved as we found that the U.S. Department of Health and Human Services is performing financial audits of Georgetown University which meet Federal audit requirements. Also vouchers needing administrative approval by the project officer were sent during the audit period.

Appendix IV

Financial Status of the Panama Assistance Program
As of May 31, 1991 1/ 2/

Funded Under the Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act
(Unaudited)

Program/ Project Number	Title	Implementing Organizations (Primary-Sub)	Budgeted Amount (000s)	Obligated Amount (000s)	Accrued Expenditures (000s) 2/	Disbursed Amount (000s)
	CASH TRANSFERS:					
525-0303	ECONOMIC RECOVERY PROGRAM Repayment of GOP Debt Arrearages Support to GOP Public Investment Budget	MIPPE and BNP MIPPE and BNP	\$130,000 113,850	\$130,000 113,850	0 \$14,824 3/	0 \$29,850
525-0304	PRIVATE SECTOR REACTIVATION PROGRAM	CENA and BNP	107,900	107,900	40,000 4/	72,000
	SUBTOTAL CASH TRANSFERS		\$351,750	\$351,750	\$54,824	\$101,850
	DEVELOPMENT PROJECTS:					
525-0258	PRIVATE SECTOR SCHOLARSHIPS	COSPAE	500	0	0	0
525-0281	PANAJURU LOCAL SCHOLARSHIPS	PANAJURU	500	500	0	0
525-0300	EMERG. REHAB. OF CHORRILLO APARTMENTS	MIVI	2,500	2,500	2,500	2,500
525-0302	IMMEDIATE RECOVERY PROJECT AMENDMENT Replacement Housing					
525-0305	Food and Shelter to Displaced Persons IMPROVING POLICE SERVICES	MIVI and Caja de Ahorro Camara de Comercio Dept. of State	6,375 1,900 13,200	5,355 1,900 6,700 5/	3,015 1,682 4,600	2,698 1,608 6,700 5/
525-0306	FINANCIAL MANAGEMENT REFORM	- Dept. of Justice CG, MIPPE, and MHT	4,500	0	0	0
525-0307	DEMOCRATIC INITIATIVES:					
525-0307.01	Journalism Strengthening	Florida Intl. Univ.	500	500	75	0
525-0307.02	Civic Education	Am. Develop. Fnd. - Civic Crusade	240	240	35	0
525-0307.03	Aid to Electoral Tribunal	IIDH/CAPEL	660	660	616	616
525-0307.04	Legislative Development	Consortium for Leg. Dev.	700	0	0	0
525-0308	NATURAL RESOURCE MANAGEMENT	INRENARE & NATURA	10,000	0	0	0
525-0309	TRADE PROMOTION	local priv. sector org(s)	2,000	0	0	0
525-0310	PEACE CORPS - NATURAL RESOURCES	Peace Corps	100	100 5/	20	100 5/
525-0311	USIA-TRAINING	USIA	500	500 5/	75	500 5/
525-0312	IMPROVED ADMINISTRATION OF JUSTICE	Sup. Court, Public Minist. Bar Assoc. & Univ. of Pan	6,900	6,900	0	0
525-0313	ECONOMIC POLICY DEVELOPMENT	MIPPE	3,100	3,100	0	0
525-0314	TAX ADMINISTRATION IMPROVEMENT	IRS	1,600	1,600	0	0
525-1000	CENTRAL AMERICAN PEACE SCHOLARSHIP Participant Training Program (less ELT)					
598-0790	English Language Training (ELT) AIFLD LABOR DEVELOPMENT PROGRAM Unallocated Funds	Georgetown University To be determined AIFLD	5,450 550 500 1,730	5,450 0 500 0	0 0 500 0	0 0 0 0
	SUBTOTAL DEVELOPMENT PROJECTS		\$64,005	\$36,505	\$13,118	\$14,722

**Financial Status of the Panama Assistance Program
As of May 31, 1991 ^{1/} _{2/}**

**Funded Under the Fiscal Year 1990 Dire Emergency Supplemental Appropriations Act
(Unaudited)**

Program/ Project Number	Title	Implementing Organizations (Primary-Sub)	Budgeted Amount (000s)	Obligated Amount (000s)	Accrued Expenditures (000s) ^{2/}	Disbursed Amount (000s)
525-0000	USAID MISSION EXPENSES:					
	PROJECT DEVELOPMENT AND SUPPORT OPERATING EXPENSES	A.I.D. A.I.D.	975 3,270	689 1,533	257 1,220	188 1,011
	SUBTOTAL MISSION EXPENSES		\$4,245	\$2,222	\$1,477	\$1,199
	TOTAL FY 1990 DIRE SUPPLEMENTAL		\$420,000	\$390,477	\$89,419	\$117,771

- 1/ This report includes financial information obtained from USAID/Panama relating to several program activities managed through A.I.D./Washington. USAID/Panama does not maintain the official accounting records for these activities so this information may not be complete and accurate--particularly with regard to those projects being implemented through other U.S. Government entities.
- 2/ Accrued expenditure information in this table is based on USAID/Panama's estimations which have not been verified. Therefore this table may not reflect the exact expenditures under the Assistance Program.
- 3/ GOP withdrawals from Special Priority Investment Fund account at the National Bank of Panama (BNP).
- 4/ Interbank Certificates of Deposit purchased by BNP from private Panamanian banks as of May 31, 1991.
- 5/ Budget transfers to other U.S. Government entities. For purposes of this table funds are considered to be fully obligated and disbursed at the time of transfer. The actual status may be different.

Analysis of Compliance with Selected Policy/Procedural
Requirements Associated with the Panama Assistance Program

POLICY/PROCEDURAL REQUIREMENTS	YES	PARTIAL	NO	COMMENTS
OBJECTIVE No. 2				
Prepare Country Development Strategy Statement (CDSS). Handbook 3, Chapter 1.			x	The new Mission in Panama, with A.I.D./ Washington/LAC Bureau approval, started the Assistance Program without a CDSS due to the need to begin implementation to support the new democratic Government of Panama. The Mission developed a CDSS during the audit period which was submitted to the LAC Bureau for review and approval in May 1991.
Prepare Action Plan. A.I.D./Washington LAC/DPP Memorandum dated October 31, 1990.			x	The above comment is applicable and an Action Plan for FY 1992 and 1993 was prepared and submitted to A.I.D./ Washington for approval in May 1991.
Program/project was properly authorized. Handbook 3, Chapter 5; Handbook 4, Chapter 2.	x			
Project agreements are to be preceded by a preliminary analysis and summary justification. Handbook 3 Chapter 2.		x		Assistance Program in Panama was preceded by a Supplemental Package Discussion Paper which covered most of the programs, projects or activities funded under the Act. This document did not meet A.I.D. Handbook standards for a preliminary design document. However, Project Papers exceeding this minimum requirement were later prepared for certain projects.
Unless excepted, agreements are to be preceded by detailed analysis and full-scale development documents. Handbook 3, Chapter 3 and Handbook 4, Chapter 3.		x		The two cash transfer agreements were preceded by the required documents (PAADs) However one subprogram of the Private Sector Reactivation Program was not fully analyzed. Detailed analysis documents

POLICY/PROCEDURAL REQUIREMENTS	YES	PARTIAL	NO	COMMENTS
Congressional notifications sent prior to obligating funds. FAA section 634A.	x			(Project Papers) were required on certain projects and in two of three such cases Project Papers meeting Handbook standards were prepared.
Objective No. 2 - Subtotal	6	2	2	
OBJECTIVE No. 3				
Prepare plans relating to monitoring, evaluating and auditing. Handbooks 3, 4 and 13. (Specific requirements for the different types of assistance vary.)		x		Of 11 agreements within the scope of our review that had been signed, each had some degree of planning for monitoring, 8 evaluation plans, and 5 had requirements for financial audits contracted by the implementing entity. Audit coverage was increased to 10 agreements by including recipient audits that are planned outside the terms of the agreements and a planned Mission-funded financial audit of Assistance Program activities that can be verified to records in Panama.
Issue a Mission Order to formally establish a monitoring and evaluation system. Supplement to Handbook 3 Chapter 12.			x	
Prepare Project Implementation Status Report. Handbook 3, Chapter 11.	x			
Prepare Information Plans. A.I.D. Evaluation Handbook (Supplement to Chapter 12 of Handbook 3.)			x	No information plans were prepared. However, certain aspects of information plans were sometimes covered as part of other plans e.g. implementation, monitoring and evaluation plans, or were evident from the narrative of the final design document or agreement.
Cash transfer dollars to be maintained in a separate account. State 325792.	x			

POLICY/PROCEDURAL REQUIREMENTS		YES	PARTIAL	NO	COMMENTS
Cash transfer dollars are to be trackable to final acceptable end-use. State 325792.			x		Debt repayment will be tracked to the specific transactions. The remaining dollars under both cash transfers will be tracked only to the macroeconomic level.
Objective No. 3 - Subtotal	6	2	2	2	
OBJECTIVE No. 4					A.I.D./Washington delayed transmittal of vouchers for administrative approval.
Budget allowances are to be received prior to obligation. Controllers Guidebook, Chapter 3.		x			
Mission project accounting should conform to the A.I.D. Project Accounting System. Controllers Guidebook Chapter 13.		x			
Voucher payment systems for approvals, fund availability, and examination and processing are in the line with A.I.D. procedures. Controllers Guidebook Chapter 5.			x		
Cash advances are not in excess of recipient needs. Controllers Guidebook Chapter 16.		x			
Prior to making a cash transfer payment the Mission cables A.I.D./Washington to certify compliance with conditions precedent. State 194322.		x			
INTERNAL CONTROL REPORT					
Prepare Mission General Assessment. A.I.D. Payment Verification Policy #1.		x			
Objective No. 4 - Subtotal	6	5	1	0	
Total	18	9	5	4	