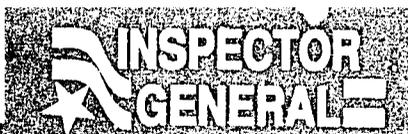


Regional Inspector General for Audit
Tegucigalpa, Honduras

Audit of
USAID/Costa Rica's
Grants and Cooperative Agreements

Audit Report No. 1-515-93-003
November 30, 1992



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AMERICAN EMBASSY
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November 30, 1992

MEMORANDUM

TO: D/USAID/Costa Rica, Ronald F. Venezia

FROM: RIG/A/T, Lou Mundy 

SUBJECT: Audit of USAID/Costa Rica's Grants and Cooperative Agreements

The Office of the Regional Inspector General for Audit/Tegucigalpa has completed the audit of grants and cooperative agreements at USAID/Costa Rica. The final report is being transmitted to you for your action.

In preparing this report we reviewed your comments on the draft report. A summation of your comments has been included in the Management Comments section of the Executive Summary. Your written comments are included in the report as Appendix II.

Based on your written comments, we consider Recommendation Nos. 1.1, 1.2, 2, 3.1, 3.2, 4.1, and 4.2 closed upon issuance of this report and Recommendation No. 5 resolved. Please respond to the report within 30 days indicating final actions taken in regard to the resolved recommendation.

I appreciate the cooperation that you and your staff provided the auditors during this assignment.

**Regional Inspector General for Audit
Tegucigalpa, Honduras**

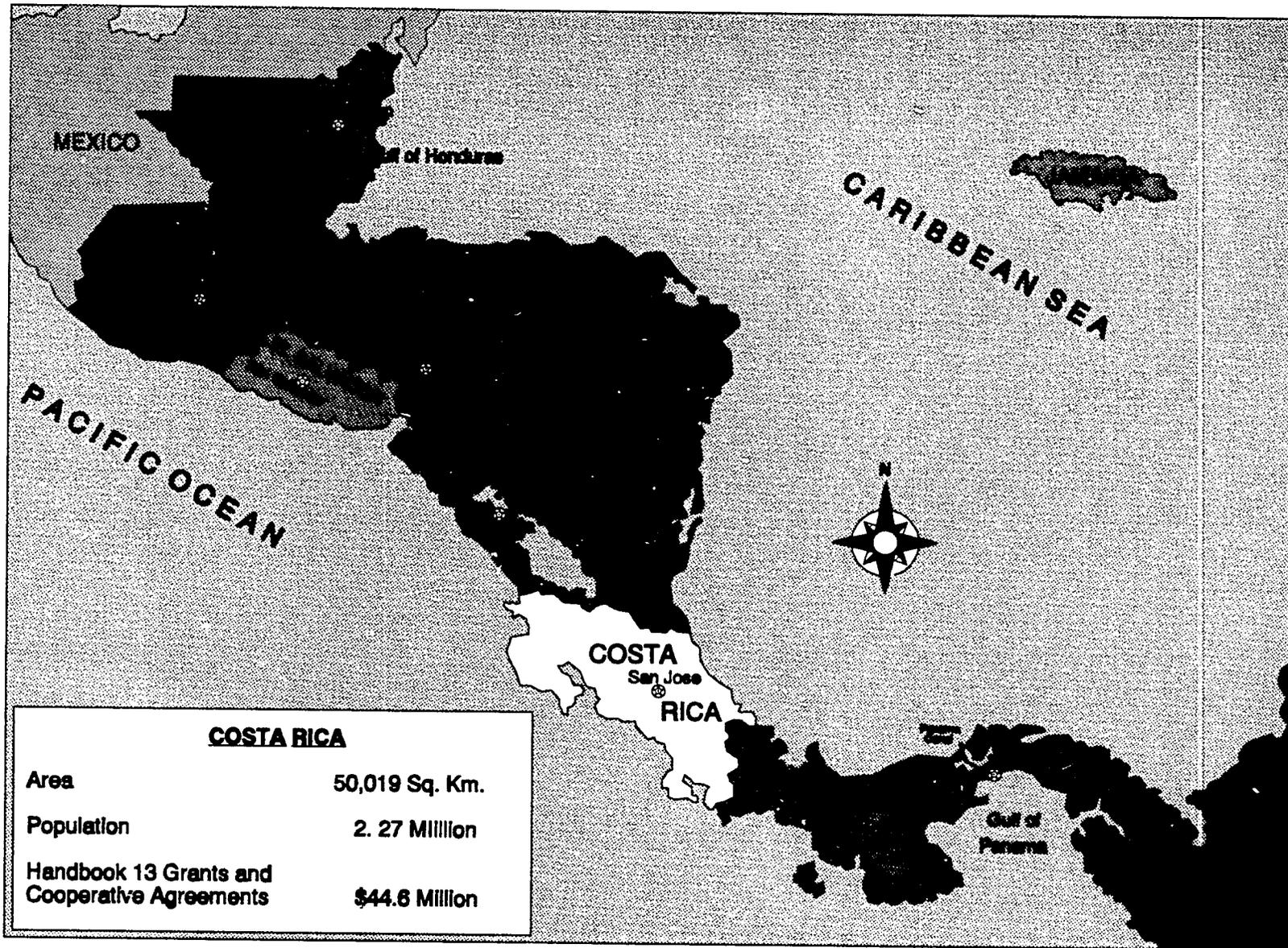
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EXECUTIVE SUMMARY

Background

The Federal Managers' Financial Integrity Act of 1982 requires A.I.D. to prepare a yearly report to Congress and the President of its management controls. In turn, A.I.D. requires each mission or office, such as the Office of the USAID/Costa Rica to submit a yearly assessment of its management controls in order to prepare the required report. These management controls, also called internal controls, are to provide reasonable assurance that obligations and costs are proper, funds and assets are safeguarded, and revenues and expenditures are properly accounted.

The Office of the Regional Inspector General for Audit/Tegucigalpa audited USAID/Costa Rica's processes for providing assistance to nonprofit organizations under the guidance of A.I.D. Handbook 13, *Grants and Cooperative Agreements*. As of March 31, 1992, USAID/Costa Rica was managing a portfolio of 19 grants valued at \$ 44.6 million (See Appendix III). The audit period covered grants awarded from June 1986 to September 1991 and we tested the management system in place at the time of the audit.

Audit Objectives

We audited selected systems of internal controls at USAID/Costa Rica concerning its processes for providing assistance to nonprofit organizations under the guidance of A.I.D. Handbook 13. Our field work was conducted from March 16, 1992 through May 14, 1992 and was designed to answer the following objectives:

1. Did USAID/Costa Rica establish and follow procedures for reviewing and authorizing solicited and unsolicited proposals and negotiating with nonprofit organizations the award of grants as required by A.I.D. Handbook 1, Supplement B and Handbook 13, Chapter 2?
2. Did USAID/Costa Rica establish and follow procedures for registering and maintaining current registration of private voluntary organization as required by A.I.D. Handbook 3, Appendix 4C?

3. Did USAID/Costa Rica establish and follow policies and procedures in providing, liquidating, and accounting for advances to nonprofit organizations as required by A.I.D. Handbook 19, Chapter 1, Appendix 1B?
4. Did USAID/Costa Rica establish and implement policies and procedures for monitoring, reporting, and evaluating implementation of grants or cooperative agreements by nonprofit organizations as required in A.I.D. Handbook 13, Chapters 1 and 4 and Handbook 3, Supplement to Chapter 12?
5. Did USAID/Costa Rica establish and implement policies and procedures to ensure that grantees performed annual independent audits as required by A.I.D. Handbook 13, Appendix 4D (2)?
6. Did USAID/Costa Rica establish and follow policies and procedures in the closeout, suspension, or termination of grants or cooperative agreements as required by A.I.D. Handbook 13, Chapter 1?

Summary of Audit

Although the Director, USAID/Costa Rica provided us with certain essential written representations concerning management's responsibilities and the full and accurate disclosure of recorded information, he did not provide written representations concerning: 1) whether all information relevant to the audit objectives was provided, 2) irregularities within or involving the audited activity, 3) noncompliance with A.I.D. policies and procedures and on violations of laws and regulations, and 4) events occurring subsequent to the period under audit. Also, other USAID/Costa Rica officials directly responsible for the audited activities did not provide written representations to the Director, USAID/Costa Rica confirming essential information. As a result, our answers to the audit objectives are qualified to the extent of the effect of not having such representations. Finally, because USAID/Costa Rica officials did not provide a written representation concerning their knowledge of noncompliance or possible violations of laws and regulations for the audited activities, we are disclaiming an opinion in this regard (see Report on Compliance, page 25). Per the Director's request the representation letter provided by USAID/Costa Rica is presented in Appendix II.

Except for the effects, if any, of not receiving acceptable representations, as discussed above, USAID/Costa Rica established and followed policies and procedures in accordance with Agency criteria to ensure that: (1) proposals were adequately reviewed and authorized and grants were properly negotiated, (2) private voluntary organizations were registered, (3) advances

of funds to nonprofit organizations were adequately provided, liquidated and accounted, and (4) grants were independently audited annually. However, the audit also showed that: (1) the Mission's system for monitoring, reporting, and evaluating nonprofit organizations' implementing of A.I.D. grants could be improved and (2) the Mission did not fully establish and follow A.I.D. policies and procedures for the closeout, suspension, or termination of grants and cooperative agreements. As a result, USAID/Costa Rica lacked assurances that: cost-sharing contributions were reported and verified; grantee progress reports timely identified, documented, and reported problems to the Mission; and grants and cooperative agreements were properly closed out.

Audit Findings

The Mission's System for Awarding Grants Could Be Strengthened

Although USAID/Costa Rica established guidelines for awarding grants to nonprofit organizations, there was confusion as to the responsibility for managing grant activities and the procedures for preaward evaluation needed clarification. We attributed this situation to an oversight on the part of Mission officials as a consequence of added responsibilities assigned to its available staff due to reductions in personnel. As a result, technical reviews of proposed grants were not always performed or properly documented as required. Although we did not identify any negative effect currently resulting from this condition, potential problems could be minimized by strengthening the review and authorization process for grant proposals. (See page 4.)

Established Guidelines For Site Visits Need To Be Followed

Agency and Mission procedures require site visits to be made and documented. Although project officers stated that they had made frequent visits to project sites, the audit found that they did not document visit results. Documenting these visits would help ensure that implementation problems are being identified, documented, and brought to the attention of cognizant officials for proper resolution. (See page 9.)

Guidelines Are Needed for Cost-Sharing Contributions and Grantee Reporting

A.I.D. guidance states that unless there is strong justification for doing otherwise, cost-sharing contributions are required from nonprofit organizations and must be documented. Grant recipients are also required to submit performance reports. The audit found that USAID/Costa Rica had not established a system for monitoring, verifying, and documenting cost-sharing contributions (see page 10) or for ensuring that consistent, comprehensive, and timely performance reports were received (see page 13). As a result, there were no assurances that grantee contributions reported in the Mission's semi-annual reports were correct or that project progress reported by grantees was adequate in relation to planned accomplishments.

Closeout Procedures Need To Be Strengthened

A.I.D. guidance prescribes uniform closeout procedures for grants. Although USAID/Costa Rica established closeout procedures it did not include all pertinent requirements. Consequently, the Mission closed out some projects with less than full compliance with Agency requirements. We do note however, that some of these projects were from 1985 and not all documentation might have been available. (See page 16).

Summary of Recommendations

We made five recommendations to improve the systems covered by the audit objectives. The recommendations were to:

- amend current mission orders to designate the officer and office responsible for awarding grants and issue internal control procedures for preaward reviews of prospective grantees.
- implement its guidelines requiring project officers to prepare and distribute site visit reports.
- establish written policies and procedures for monitoring, verifying, documenting, and reporting cost-sharing contributions.
- establish internal controls to ensure that grantees comply with reporting requirements of A.I.D Handbook 13.

- amend its Mission Order on closeout of grants and cooperative agreements to include the appropriate requirements from A.I.D. Handbook 13 and Contract Information Bulletin No. 90-12.

Management Comments and Our Evaluation

The draft audit report was reviewed and commented on by USAID/Costa Rica. Management agreed with the five report recommendations and has taken steps to close and resolve the recommendations. Four recommendations were closed upon issuance of this report and the fifth recommendation has been resolved.

Office of the Inspector General

Office of the Inspector General
November 30, 1992

INTRODUCTION

Background

The Federal Managers' Financial Integrity Act of 1982 (FMFIA) requires A.I.D. to prepare a yearly report to Congress and the President of its management controls. In turn A.I.D. requires each mission or office, such as USAID/Costa Rica, to submit a yearly assessment of its management controls in order to prepare the required report. These management controls, also called internal controls, are to provide reasonable assurance that obligations and costs are proper, funds and assets are safeguarded, and revenues and expenditures are properly accounted.

As of March 31, 1992, USAID/Costa Rica's portfolio included 19 grants, valued at \$44.6 million, awarded to nonprofit organizations¹ under A.I.D. Handbook 13 policies and procedures. Obligations and expenditures as of March 31, 1992, for these grants were \$44.6 million and \$28.6 million, respectively.

The management of USAID/Costa Rica is responsible for establishing various systems of internal control to manage its portfolio in accordance with the FMFIA and Office of Management and Budget (OMB) guidance. Our audit focused on the major systems used to manage grants to nonprofit organizations. We selected these systems because grants comprise a large part of the USAID/Costa Rica portfolio and prior Office of Inspector General audits have frequently disclosed problems with these systems at other missions.

Audit Objectives

As a part of its annual audit plan the Office of the Regional Inspector General for Audit in Tegucigalpa, Honduras audited USAID/Costa Rica's systems of internal controls for managing A.I.D. Handbook 13 grants to nonprofit organizations to answer the following objectives:

¹ Nonprofit organization is defined as any organization which: (1) is operated primarily for scientific, educational, service, charitable, or similar purposes in the public interest, (2) is not organized primarily for profit, and (3) uses its net proceeds to maintain, improve, and/or expand its operations.

1. Did USAID/Costa Rica establish and follow procedures for reviewing and authorizing solicited and unsolicited proposals and negotiating with nonprofit organizations the award of grants as required by A.I.D. Handbook 1, Supplement B and Handbook 13, Chapter 2?
2. Did USAID/Costa Rica establish and follow procedures for registering and maintaining current registration of private voluntary organizations as required by A.I.D. Handbook 3, Appendix 4C?
3. Did USAID/Costa Rica establish and follow policies and procedures in providing, liquidating, and accounting for advances to nonprofit organizations as required by A.I.D. Handbook 19, Chapter 1, Appendix 1B?
4. Did USAID/Costa Rica establish and implement policies and procedures for monitoring, reporting, and evaluating implementation of grants or cooperative agreements by nonprofit organizations as required in A.I.D. Handbook 13, Chapters 1 and 4 and Handbook 3, Supplement to Chapter 12?
5. Did USAID/Costa Rica establish and implement policies and procedures to ensure that grantees performed annual independent audits as required by A.I.D. Handbook 13, Appendix 4D (2)?
6. Did USAID/Costa Rica establish and follow policies and procedures in the closeout, suspension, or termination of grants or cooperative agreements as required by A.I.D. Handbook 13, Chapter 1?

In answering these audit objectives, we tested whether USAID/Costa Rica followed applicable internal control procedures and complied with certain provisions of laws and regulations. Our tests were sufficient to provide reasonable, but not absolute, assurance of detecting abuse or illegal acts that could significantly affect the audit objectives. Because of limited time and resources, we did not continue testing when we found that, for the items tested, USAID/Costa Rica established and followed Agency policies and procedures and complied with legal and regulatory requirements. When we found problems we performed work to determine that USAID/Costa Rica had not established or followed a policy and/or procedure, identify the cause and effect of the problem noted, and make recommendations to correct the condition and cause of the problem.

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

REPORT OF AUDIT FINDINGS

The Director, USAID/Costa Rica provided us with certain essential written representations concerning management's responsibilities and the full and accurate disclosure of recorded information; however, he did not provide written representations concerning: 1) whether all information relevant to the audit objectives was provided, 2) irregularities within or involving the audited activity, 3) noncompliance with A.I.D. policies and procedures and on violations of laws and regulations, and 4) events occurring subsequent to the period under audit. Also, other USAID/Costa Rica officials directly responsible for the audited activities did not provide written representations to the Director, USAID/Costa Rica confirming essential information. As a result, our answers to the audit objectives are qualified to the extent of the effect of not having such representations. Finally, because USAID/Costa Rica officials did not provide a written representation concerning their knowledge of noncompliance or possible violations of laws and regulations for the audited activities, we are disclaiming an opinion in this regard (see Report on Compliance, page 25). Per the Director's request the representation letter provided by USAID/Costa Rica is presented in Appendix II.

1. Did USAID/Costa Rica establish and follow procedures for reviewing and authorizing solicited and unsolicited proposals and negotiating with nonprofit organizations the award of grants as required by A.I.D. Handbook 1, Supplement B and Handbook 13, Chapter 2?

Except for the effects, if any, of not receiving acceptable representations, as discussed above, USAID/Costa Rica established and followed procedures for reviewing and authorizing solicited and unsolicited proposals and in negotiating with nonprofit organizations the award of grants as required by A.I.D. Handbook 1, Supplement B and Handbook 13, Chapter 2. However, we believe that internal controls for awarding grants to nonprofit organizations could be strengthened by issuing the mission order covering preaward evaluations which has been in draft since 1989 and by clarifying and designating a Mission officer responsible for managing grant activities.

In three different mission orders concerning A.I.D.-funded grants, USAID/Costa Rica established: (1) guidelines for selecting, reviewing, approving and monitoring grants, (2) the roles and functions of mission offices, and (3) the requirement that a project implementation order/technical (PIO/T) be used to facilitate the negotiation and execution of grants. To complement the above guidelines, a Controller Bulletin was also issued which contained a checklist to facilitate the review of grants and cooperative agreements.

We sampled seven grants² to test the Mission's process for awarding grants to nonprofit organizations and found that, with one exception, USAID/Costa Rica followed its established policies and procedures. For example, the Mission reviewed the applicant's proposals; included the required standard provisions in grant agreements; and with one exception, prepared written justifications for the noncompetitive award of grants and PIO/Ts for program description and negotiation of awards.

However, we noted two weaknesses in the grant award process that, when corrected, could help strengthen the Mission's internal controls for awarding grants to nonprofit organizations. These areas are discussed in the following report section.

The Mission's System for Awarding Grants Could Be Strengthened

A.I.D. Handbook 13 and USAID/Costa Rica's mission orders establish guidelines for awarding grants to nonprofit organizations. However, the existing guidelines need clarification of the responsibility for managing grant activities and on the internal control procedures for preaward evaluations. The Mission has a draft mission order which clarifies the procedures for preaward evaluations but it has not been finalized. Operational personnel stated that there was confusion as to which office was responsible for reviewing and awarding grants to nonprofit organizations. Also, technical analysis and reviews of proposed grants were not always properly documented in accordance with Handbook 13 requirements. Although we did not identify any significant negative effect as a result of these two conditions on current operations, potential problems could be minimized by amending existing guidance to clarify the responsibilities for reviewing and awarding grants to nonprofit organizations, and finalizing the draft mission order for preaward

² We judgmentally selected seven of the 19 grants awarded by USAID/Costa Rica under A.I.D. Handbook 13. The seven grants selected were valued at \$31.1 million or 70 percent of the \$44.6 million awarded by the Mission for the entire portfolio.

evaluations. In our opinion this will help strengthen the internal control process for awarding grants to nonprofit organizations.

Recommendation No. 1: We recommend that USAID/Costa Rica:

- 1.1 amend current mission orders to designate the officer and office responsible for reviewing and awarding grants to nonprofit organizations; and**
- 1.2 issue in final the draft mission order which covers internal control procedures for preaward evaluations of prospective grantees.**

A.I.D. Handbook 13, Chapters 2 (Selection of Grant Recipients) and 4 (Specific Support Grants) describe the requirements for reviewing and awarding grants to nonprofit organizations and the need for determining a prospective recipient's capacity to perform technically and financially. Although USAID/Costa Rica established guidance for implementing these requirements, we noted two areas in which their controls could be strengthened.

First, the current guidance for reviewing and awarding grants to nonprofit organizations could be clarified. Mission Order Nos. 565 and 140 assigned responsibilities for handling nonprofit organization activities to two different offices--the Project Development Office and the General Development Office. Also, the Mission officer responsible for the review and approval of grants and the registration of nonprofit organizations had not been designated due to an oversight. Also with respect to technical analysis of proposals, we reviewed documentation to determine if these analysis were done as required by Section 4F of Handbook 13. We found that in two of the seven grants sampled, there was no supporting evidence that technical analysis was performed as required.

Second, although being followed, the Mission's internal control procedures for preaward evaluations of prospective recipients were contained in a draft mission order written in 1989 but not finalized. These procedures are to help ensure that grantees are qualified to administer A.I.D. funds by reviewing their technical and managerial capabilities before grants are awarded. The draft mission order requires that the Controller's Financial Analysis Section perform preaward reviews of a grantee's managerial and financial capabilities, and the appropriate technical office perform reviews of the technical aspects related to the grant proposals. Mission management assigned a low priority to the finalization of the draft mission order because an increased workload to available operational personnel necessitated fulfillment of responsibilities based on priorities.

Although we did not identify any significant negative effect as a result of these two conditions on current operations, potential problems could be minimized by amending existing guidance to clarify the responsibilities for reviewing and awarding grants to nonprofit organizations, and finalizing the draft mission order for preaward evaluations. In our opinion this will help strengthen the internal control process for awarding grants to nonprofit organizations.

Management Comments and Our Evaluation

USAID/Costa Rica concurred with both parts of Recommendation No. 1. It revised/issued two Mission Orders to designate the officer and office responsible for reviewing and awarding grants to nonprofit organizations. It also issued a new Mission Order which establishes internal controls procedures for preaward evaluations of prospective grantees.

Based on the above Mission Orders, Recommendation No. 1.1 and No. 1.2 are closed upon report issuance.

2. Did USAID/Costa Rica establish and follow procedures for registering and maintaining current registration of private voluntary organizations as required by A.I.D. Handbook 3, Appendix 4C?

Except for the effects, if any, of not receiving acceptable representations, as discussed on page 3, USAID/Costa Rica established and followed procedures for registering and maintaining registration of private voluntary organizations (PVOs) in accordance with Handbook 3, Appendix 4C (Registration of Agencies for Voluntary Foreign Aid).

USAID/Costa Rica issued a Controller Bulletin which described the registration procedures to be followed for U.S. and local PVOs. Agency guidance regarding registration and annual reevaluation of registered local PVOs was also disseminated within Mission offices. Two of the seven grants we tested³ were local PVOs, and we found that USAID/Costa Rica followed the established process for provisional registration of local PVOs. Final registration of these PVOs with A.I.D.'s Office of Private and Voluntary Cooperation was also properly done. Two U.S. PVOs were directly registered in A.I.D./Washington. According to A.I.D. guidance the remaining three grantees (an educational institution, an international institution and one for-profit institution) did not require registration.

³ See footnote 2 on page 4.

3. Did USAID/Costa Rica establish and follow policies and procedures in providing, liquidating, and accounting for advances to nonprofit organizations as required by A.I.D. Handbook 19, Chapter 1, Appendix 1B?

Except for the effects, if any, of not receiving acceptable representations, as discussed on page 3, USAID/Costa Rica established and followed policies and procedures in providing, liquidating, and accounting for advances to nonprofit organizations as required by A.I.D. Handbook 19, Chapter 1, Appendix 1B (Cash Management).

As part of the Mission's internal control procedures, USAID/Costa Rica issued a mission order which contained policies, procedures, and monitoring responsibilities for advances as stated in Handbook 19, conducted periodic tests of advances, and prepared monthly aging reports on advances.

In another mission order, USAID/Costa Rica detailed three types of advances: an initial cash advance, 30-day advance and a maximum of up to a 90-day advance. Guidance was provided describing when each method was applicable and its requirements. For the grants tested, the audit found that five grantees received advances up to 90 days and that all advances were properly justified in writing.

The Controller's office conducted periodic tests of outstanding advances. For example, as part of the 1991 Internal Control Assessment, the Mission tested advances for four of the twelve government and nonprofit organizations receiving advances. This test indicated full compliance with A.I.D. regulations. The test also identified that cash advances, in some instances, exceeded immediate cash needs, but in processing a subsequent request for advance, the Mission reduced the amount to a more acceptable level.

The Mission also prepares a monthly aging report on project advances which shows outstanding advances at various intervals. If the report shows a project with a long outstanding advance, the Controller notifies the project officer who is responsible for taking corrective action. Each request for an advance includes the project officer's approval of the advance voucher, a statement of outstanding advances, a certification of cash needs, a cash advance status report, and a certification of expenses incurred and accumulated for the period.

4. Did USAID/Costa Rica establish and implement policies and procedures for monitoring, reporting, and evaluating implementation of grants or cooperative agreements by nonprofit organizations as required in A.I.D. Handbook 13, Chapters 1 and 4 and Handbook 3, Supplement to Chapter 12?

USAID/Costa Rica: (1) had established, but had not implemented, policies and procedures for monitoring through site visit reports, (2) had not established policies and procedures for monitoring grantee cost-sharing contributions and periodic progress reporting, and (3) except for the effects, if any, of not receiving acceptable representations, as discussed on page 3, had established and implemented policies and procedures for evaluating implementation of grants or cooperative agreements by nonprofit organizations as required in A.I.D. Handbook 13 (Grants), Chapters 1 (Introduction) and 4 (Specific Support Grants) and Handbook 3, Supplement to Chapter 12 (Evaluation Handbook).

To test the Mission's monitoring system we reviewed two aspects of the monitoring process: site visits and cost-sharing contributions. We found that USAID/Costa Rica had issued two mission orders explaining policies and procedures for performing site visits, including the frequency of such visits and the preparation and distribution of site visit reports. Although project officers stated that they made frequent visits to project sites, they were not documented as required by Agency and Mission guidance. Regarding cost-sharing contributions, the Mission had not established a system to monitor, verify, report, and document contributions. With respect to reporting, the Mission had not established a system to ensure that periodic progress reports from grantees complied with the requirements of Handbook 13, Section 1N which reflects the requirements of OMB Circular A-110, Attachment H.

Our review of the Mission's system for evaluating projects disclosed that USAID/Costa Rica issued a mission order and disseminated and adopted LAC Bureau guidance on evaluations. Of the seven projects we sampled, six included evaluation requirements for the grants and cooperative agreements in accordance with A.I.D. policy. Also, as of May 1992, five evaluations had been conducted, and all were made in accordance with the evaluation requirements. The Mission's system identified one evaluation which was not performed in accordance with the approved scope of work, and corrective action was taken.

The following report sections discuss the areas where USAID/Costa Rica can improve their internal controls for monitoring and reporting of grants and cooperative agreements.

Established Guidelines For Site Visits Need To Be Followed

A.I.D. Handbook 13, Chapter 1 and the Project Officers' Guidebook establish policies and procedures for site visits. In addition, Mission guidelines also outline procedures for preparing site visit reports. Our sample of seven grants disclosed that project officers were not documenting the results of their site visits. According to project officers, site visit reports are not the best mechanism to communicate problems to management as this imposed a greater workload and they did not have the time. However, if site visits are not documented USAID/Costa Rica management does not have assurance that implementation problems are being properly identified for resolution.

Recommendation No. 2: We recommend that USAID/Costa Rica implement its guidelines requiring project officers to prepare and distribute site visit reports.

A.I.D. Handbook 13, Chapter 1, Section 1N7 (Monitoring and Reporting Program Performance) requires that project officers perform site visits, as frequently as practicable, to review program accomplishments and management control systems and to provide technical assistance as may be required. The Project Officers' Guidebook also prescribes policies and procedures for site visits. The Guidebook states that periodic visits by the project officer to the work site is one of the more significant aspects of the oversight of a grant. An appraisal of performance based on a comparison of the findings of a written site visit report against implementation plans should provide a basis for isolating problems and identifying follow-up actions that need to be taken. In addition, site visits are fundamental for the project officer's administrative approval of a nonprofit organization voucher.

To implement Agency guidance, USAID/Costa Rica issued Mission Order No. 570 dated March 30, 1988, which details the Mission's policies and procedures for performing site inspections, including the frequency of such visits and the preparation and distribution of site visit reports. In its 1991 Internal Control Assessment, the Mission asserted that office chiefs are briefed on site visits and, if a serious issue is identified, a memorandum may be drafted to record the issue and action decisions. It also says that Mission Order No. 570 which covers site visits will be altered to bring it into conformity with Mission needs.

We reviewed the files for seven grants to determine whether site visits were made, the frequency of visits, whether meaningful reports were prepared, and if appropriate follow-up actions were taken on identified problems. Although project officers stated that they made frequent visits to project sites, we found that, except for one project, project officers were not documenting the results of their site visits. They could not provide evidence of systematic visits which would satisfy the requirements of Handbook 13 and Mission guidelines. Project officers told us they were not documenting the results of these visits because of their heavy workload.

However, we believe documenting these visits would help ensure that implementation problems are identified and brought to the attention of management for resolution. Consequently, USAID/Costa Rica should ensure implementation of its established guidelines by conducting periodic management reviews of this area.

Management Comments and Our Evaluation

USAID/Costa Rica concurred with Recommendation No. 2 and issued a Mission Order which requires project officers to prepare and distribute site visit reports. It also requires the Mission Project Development Office to develop a site visit report filing and tracking system to ensure compliance with Mission site visit reporting guidelines.

Based on the actions taken by USAID/Costa Rica, Recommendation No. 2 is closed upon report issuance.

Guidelines for Monitoring and Verifying Grantee Cost-Sharing Contributions Need to Be Established

Agency guidance specifies that missions should require cost-sharing contributions from nonprofit organizations unless there is strong justification for doing otherwise. In addition, recent guidelines require missions to provide "auditable evidence" with respect to reporting and documenting financial contributions. USAID/Costa Rica had not established written guidelines for monitoring, verifying, documenting, and reporting cost-sharing contributions. Guidelines had not been established because Mission personnel assumed that including the contribution clause in the agreements was sufficient. As a result, there was no basis for knowing to what extent grantees complied with cost-sharing requirements.

Recommendation No. 3: We recommend that USAID/Costa Rica:

- 3.1 establish written policies and procedures for monitoring, verifying, documenting, and reporting cost-sharing contributions; and**

3.2 report this condition as a weakness in the next internal control assessment if not fully resolved.

A.I.D. Handbook 13 (Grants), Chapter 4 (Specific Support Grants), Section 4B.1.(e) requires that when funding a grant, 25 percent of the project cost should come from non-U.S. Government sources. An A.I.D./Washington world-wide cable dated October 23, 1987 (STATE 331065) also states that a 25 percent non-U.S. Government contribution is required for mission-funded PVO activities supported through grants and cooperative agreements. This guidance further states that the required contribution may be waived or reduced, but missions should require the full contribution unless there is strong justification for doing otherwise.

Another A.I.D./Washington world-wide cable dated April 27, 1991 (STATE 138349) added that there should be mission standards to provide "auditable evidence" with respect to reporting and documenting financial contributions to projects. This cable also requires that the adequacy of the host government contributions should be reviewed during Project Implementation Reviews and the reliability of the reported data tested during site visits and evaluations. This cable was not disseminated within the Mission until March 1992.

In its 1991 Internal Control Assessment, USAID/Costa Rica disclosed that it monitors and assures that the specified counterpart contribution is provided by including the requirement in agreements. It also disclosed that contributions from nonprofit organizations are verified by the Controller's Financial Analysis Section while reviewing a PVO's registration documentation and supporting analysis, including their audited financial statements. However, this verification is done before a grant is awarded to ensure that cost-sharing contributions from nonprofit organizations have been considered.

Since management assumed that including a clause on cost-sharing contributions in grant agreements was sufficient, it had not established written guidelines for monitoring, verifying, documenting, and reporting cost-sharing contributions.

Our review of seven grant agreements⁴ and related grant files and discussions with project officials showed that:

- Only two of the seven grants or cooperative agreements required cost-sharing contribution from grantees. The required contribution for one of these two agreements was not being made and was waived three

⁴ See footnote 2 on page 4.

years after the grant was awarded. The other grantee had not reported contributions as of our review.

- Cost-sharing contributions for the five remaining grants were not required. However, for three of these five grants, contributions were planned to be provided by the beneficiary institutions or by the Government of Costa Rica under a bilateral grant agreement. Although cost-sharing contributions from beneficiary institutions were disclosed in the Mission's semiannual reports, project officers did not have auditable records of these contributions. Therefore, they were not sure if the reported amounts for contributions were correct.
- Record keeping requirements necessary to document grantee contributions were not explained to grantees in any of the five grants.

As a result of not establishing internal controls, there is no basis for establishing to what extent cost-sharing contributions have been made by grantees. Consequently, USAID/Costa Rica needs to establish written policies and procedures for monitoring, verifying, documenting, and reporting cost-sharing contributions.

During the course of this audit, Mission officials recognized this problem and designated the Controller's Financial Analysis Section responsible for ensuring that grant agreements include a clause requiring PVOs to report their cost-sharing contribution annually. Also, as part of the recipient contracted audit program, the scope of work for these audits now includes a requirement for the external auditors to review compliance with cost-sharing provisions.

Management Comments and Our Evaluation

USAID/Costa Rica concurred with both parts of Recommendation No.3. It issued a new Mission Order which establishes written policies and procedures for monitoring, verifying, documenting, and reporting cost-sharing contributions. In addition, the Mission informed RIG/A/T that it has modified the standard scope-of-work under the Recipient Contracted Audit Program to include the preparation of an opinion on Fund Accountability Statements of cost-sharing contributions.

Based on the actions taken by USAID/Costa Rica, Recommendation No. 3.1 and No. 3.2 are closed upon report issuance.

Guidelines For Grantee Reporting Requirements Need To Be Established

A.I.D. Handbook 13 (Grants) requires grant recipients to submit performance reports which compare actual accomplishments with established goals. USAID/Costa Rica had not established guidelines for grantee reporting to ensure that consistent, comprehensive, and timely progress reports were received. Guidelines were not established because Mission officials believed that reporting from grantees was adequate. As a result, reporting requirements in grant agreements were inconsistent and most reports only described the activities which occurred during the reporting period. These reports could have been improved by requiring grantees to compare actual versus planned accomplishments.

Recommendation No. 4: We recommend that USAID/Costa Rica:

- 4.1 establish internal controls to ensure that grantees comply with reporting requirements in A.I.D. Handbook 13, Section 1N. These requirements, as a minimum, should cover areas such as (a) frequency of reports, (b) the need to report progress achieved against quantitative indicators and approved work plans, (c) identification of problem areas affecting project implementation, and (d) work to be undertaken during the next reporting period; and**
- 4.2 report this condition as a weakness in the next internal control assessment if not fully resolved.**

One of the principal methods missions have to provide oversight of grant activities is periodic progress reports. A.I.D. Handbook 13 (Grants), Section 1N (Monitoring and Reporting Program Performance) reflects the criteria stated in OMB Circular A-110, Attachment H in setting forth the requirements for grant recipients to report program performance. This section stipulates:

...Recipients shall monitor their performance under grants and cooperative agreements and, where appropriate, ensure that time schedules are being met, projected work units by time periods are being accomplished, and other performance goals are being achieved.... Recipients then, shall submit a performance report (technical report) for each grant or cooperative agreement that briefly presents the following information for each program, function, or activity involved:

- a. *A comparison of actual accomplishments with the goals established for the period.*
- b. *Reasons why established goals were not met.*
- c. *Other pertinent information including, when appropriate, analysis and explanation of cost overruns or high unit costs.*

The Mission had not established and implemented guidelines for grantee reporting to ensure compliance with Agency guidance because Mission officials believed that reporting from grantees was adequate.

Our review of seven grant agreements disclosed that reporting provisions were inconsistent. Only one agreement contained the reporting clause as required by Handbook 13, Section 1N. For six agreements, the reporting clause varied, was incomplete, and in four cases did not require comparison of actual accomplishments with planned targets. For example, the reporting clause of one agreement only required: *"quarterly reports will be submitted in Spanish and evaluations reports will be submitted in English and Spanish, to the A.I.D. Project Officer."*

Also, most reports submitted by grantees were of a descriptive nature and only provided information concerning activities that took place during the reporting period. These reports could have been improved by requiring grantees to compare actual versus established goals or objectives.

In summary, USAID/Costa Rica should document internal controls to ensure that nonprofit organizations report progress in accordance with Agency guidelines. This will provide needed assurance that projects are being implemented in accordance with grant agreements, goals and targets are being met, and problems are being surfaced and resolved.

Management Comments and Our Evaluation

USAID/Costa Rica concurred with both parts of Recommendation No. 4. It issued a new Mission Order to establish internal controls to ensure that grantees comply with reporting requirements of A.I.D. Handbook 13, Section 1N. It also informed RIG/A/T that as part of the Semiannual Review process, the Mission Project Development Office will track grantee compliance with the reporting requirements.

Based on the above action, Recommendation No. 4.1 and No. 4.2 are closed upon report issuance.

5. Did USAID/Costa Rica establish and implement policies and procedures to ensure that grantees performed annual independent audits as required by A.I.D. Handbook 13, Appendix 4D (2)?

Except for the effects, if any, of not receiving acceptable representations, as discussed on page 3, USAID/Costa Rica established and implemented policies and procedures to ensure that grantees performed annual independent audits as required by A.I.D. Handbook 13, Appendix 4D (2) (Mandatory Standard Provisions for Non-U.S. Nongovernmental Grantees).

Our review of the Mission's system for ensuring that independent audits are performed revealed that USAID/Costa Rica: (1) issued a comprehensive mission order on Procedures for Handling Audits, (2) designated an audit follow-up officer, (3) established and has implemented since September 1991 an Audit Tracking System, (4) determined its audit universe of 23 grantees, (5) requested IG's Office of Financial Audits in Washington, D.C. to include in its audit universe yearly audits of U.S. PVOs operating in Costa Rica under A.I.D. funded projects, and (6) issued periodic reports on the status of RIG/A/T recommendations.

Furthermore, our review of seven grant agreements revealed that USAID/Costa Rica had taken actions to amend the agreements as necessary to include the revised standard audit provisions and funds were budgeted to pay for audits. A.I.D. funds provided to two grantees had already been audited in accordance with generally accepted auditing standards. Audits for the remaining five grants have been scheduled.

Consequently, we concluded that USAID/Costa Rica established sufficient internal controls to ensure that audits are performed when required in accordance with Handbook 13, Appendix 4D (2).

6. Did USAID/Costa Rica establish and follow policies and procedures in the close out, suspension, or termination of grants or cooperative agreements as required by A.I.D. Handbook 13, Chapter 1?

USAID/Costa Rica had not established and followed A.I.D. policies and procedures for the closeout, suspension, or termination of grants and cooperative agreements as required by A.I.D. Handbook 13, Chapter 1.

In a mission order USAID/Costa Rica established internal controls for closeout of grants and cooperative agreements based on requirements

contained in Handbook 3, Chapter 14 (Project Completion and Post Project Considerations). However, the closeout procedures described in Handbook 13, Chapter 1, Section 1Q (Closeout Procedures) as well as A.I.D. guidance contained in a Contract Information Bulletin (CIB) No. 90-12 for closeout of grants was not included in the Mission's procedures. Apparently, because the Mission did not regularly closeout projects, these guidelines were overlooked and not established as part of the Mission's procedures.

Internal control procedures for closeout of grants and cooperative agreements need to be strengthened by incorporating into current Mission guidelines the requirements of Handbook 13 and CIB No. 90-12 as discussed in the following report section.

Closeout Procedures Need To Be Strengthened

A.I.D. Handbook 13 and CIB No. 90-12 prescribe uniform closeout procedures for A.I.D. grants. Although USAID/Costa Rica established internal control procedures for closeout of projects based on Handbook 3, it did not include the additional procedures prescribed in Handbook 13 and CIB No. 90-12. This happened because officials responsible for the closeout process, overlooked Handbook 13 and were not aware of guidelines contained in CIB No. 90-12. As a result, Mission guidelines were incomplete and 10 projects were closed out with less than full compliance to agency requirements.

Recommendation No. 5: We recommend that USAID/Costa Rica amend its mission order on closeout of grants and cooperative agreements to incorporate the appropriate requirements from A.I.D. Handbook 13 and Contract information Bulletin No. 90-12.

The closeout of a grant agreement involves determining whether all applicable administrative actions and work required by the agreement have been completed by A.I.D. and the recipient. A.I.D. Handbook 13, Chapter 1, Section 1Q (which implements closeout procedures contained in OMB Circular No. A-110, Attachment K), prescribes uniform closeout procedures for A.I.D. grants and other agreements with recipients. Additional guidelines in CIB No. 87-5 of January 1987 which was superseded by CIB No. 90-12 of June 1990 expanded Handbook 13 closeout procedures for grants and cooperative agreements.

The Mission did not include specific procedures prescribed in Handbook 13 and CIB No. 90-12. In March 1988, USAID/Costa Rica established Mission Order No. 575 which prescribed the Mission's internal control procedures on project closeout based on Handbook 3, Chapter 14. These procedures, which refer to activities that need to be completed in preparation for project

closeout, did not specify if they were applicable to grants and cooperative agreements.

We believe that because it has not been a regular practice for the Mission to close out projects, Handbook 13 guidelines were overlooked and current procedures had not been revised. Additional guidelines contained in CIB No. 90-12 although received, were not circulated within the Mission offices, and personnel responsible for the closeout process were not aware of such guidelines. On May 8, 1992, as a result of our audit inquiries, a Mission Notice disseminated CIB No. 90-12.

In its 1991 Internal Control Assessment, USAID/Costa Rica reported that closeout procedures for grants and cooperative agreements were not being consistently followed. It stated that terminated and/or completed projects were not properly closed out in previous fiscal years and established September 1992 as the target date for their resolution. The Mission has taken a more active role and, since January 1992, ten projects (9 of which were Handbook 13 grants) which had expired as far back as 1985 have been closed out. But established agency guidelines for closeout of grants and cooperative agreements were not always followed because of the age of the projects and closeout procedures were incomplete.

As of May 11, 1992, the Mission had begun the closeout process for two other projects with 15 others pending closeout. We reviewed seven grants closed out by the Mission and found that four had been closed out as required by Mission Order No. 575. However, the other three grants had been closed out with only a memorandum to the files. No additional information was prepared for these closeouts because the projects had been expired for such a long period.

In summary, USAID/Costa Rica's guidelines were incomplete and as a result projects/grants could continue to be closed out with less than full compliance to Agency requirements. The requirements of Handbook 13 and CIB No. 90-12 should be incorporated into the Mission's closeout procedures to ensure close outs of grants and cooperative agreements are performed as required.

Management Comments and Our Evaluation

USAID/Costa Rica concurred with Recommendation No. 5 and was in the process of amending its current Mission Order to incorporate the appropriate requirements from A.I.D. Handbook 13 and Contract Information Bulletin No. 90-12.

Recommendation No. 5 is resolved and can be closed when RIG/A/T receives and reviews for completeness a copy of the amended mission order.

REPORT ON INTERNAL CONTROLS

This section provides a summary of our assessment of USAID/Costa Rica's internal controls for the audit objectives.

Scope of Our Internal Control Assessment

We conducted our audit in accordance with generally accepted government auditing standards which require that we:

- assess the applicable internal controls when necessary to satisfy the audit objectives, and
- 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 objectives and not to provide assurance on the auditee's overall internal control structure.

For the purposes of this report, we classified significant internal control policies and procedures applicable to each audit objective by categories. For each category, we obtained an understanding of the design of relevant policies and procedures and determined whether they had been placed in operation--and we assessed control risk. When assessing control risk, we found that the USAID Office had not documented its internal controls applicable to the areas covered by our audit objectives. We therefore conducted more extensive testing, whenever possible, to achieve our purpose of assessing applicable internal controls. We have reported the internal control categories as well as any significant weaknesses under the applicable audit objective in the "Conclusions for the Audit Objective" section of this report.

General Background on Internal Controls

The management of A.I.D., including USAID/Costa Rica, is responsible for establishing and maintaining adequate internal controls. Recognizing the

need to re-emphasize the importance of internal controls in the Federal Government, Congress enacted the Federal Managers' Financial Integrity Act (FMFIA) in September 1982. The FMFIA, which amends the Accounting and Auditing Act of 1950, makes the heads of executive agencies and other managers as delegated legally responsible for establishing and maintaining adequate internal controls. Also, the General Accounting Office has issued "Standards for Internal Controls in the Federal Government" to be used by agencies in establishing and maintaining such controls.

In response to the FMFIA, the Office of Management and Budget has issued guidelines for the "Evaluation and Improvement of Reporting on Internal Control Systems in the Federal Government". According to these guidelines, management is required to assess the expected benefits versus the related costs of internal control policies and procedures. The objectives of internal control policies and procedures for federal foreign assistance programs 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. Moreover, predicting whether a system will work in the future is risky because changes in conditions may require additional procedures or the effectiveness of the design and operation of policies and procedures may deteriorate.

Conclusions for Audit Objectives

Audit Objective One

The first audit objective concerns the requirement for USAID/Costa Rica to establish and follow procedures for reviewing and authorizing solicited and unsolicited proposals and in awarding grants to nonprofit organizations. In planning and performing this objective we reviewed the Mission's internal controls relating to managing grant activities. These internal controls were cited in A.I.D. Handbook 13 and internal policy guidance established by the Mission. We classified USAID/Costa Rica's internal controls into a category called selection of grant recipients.

We reviewed the Mission's internal controls relating to the review and award of grants and our tests showed that the Mission's internal controls were logically and consistently applied. Therefore, we limited our tests to achieve our objective of determining whether USAID/Costa Rica ensured that proposals were properly reviewed and authorized and that grants were

negotiated as required by Agency policy. These tests consisted of reviewing grant proposals and agreements.

However, considered significant in terms of answering the audit objective, our tests did disclose two areas in which USAID/Costa Rica's internal controls for awarding grants to nonprofit organizations could be strengthened. These areas and the related recommendation are discussed on pages 4-6.

Audit Objective Two

The second audit objective relates to the requirement that PVOs must be currently registered with the Agency in order to receive A.I.D. funds. In planning and performing this objective we considered the applicable policies and procedures cited in A.I.D. Handbook 3, Chapter 4C. We classified USAID/Costa Rica's internal controls into a category called the registration process.

We reviewed the Mission's internal controls relating to the registration of PVOs and our tests showed that USAID/Costa Rica controls were logically and consistently applied. Therefore, we limited our tests to determine whether the PVOs were properly registered and maintained their registration status.

Audit Objective Three

The third objective concerns advances of funds to grantees. In planning and performing this objective we reviewed the internal controls cited in A.I.D. Handbook 19, Chapter 1B and mission orders. For purposes of this report, we classified the relevant policies and procedures into a category called the payment process.

We reviewed the Mission's internal controls relating to advances of funds to grantees and our tests showed that the Mission's internal controls were logically and consistently applied. Therefore, we limited our tests to determining whether advances were properly provided, liquidated, and accounted.

Audit Objective Four

This objective relates to the management of grants and cooperative agreements and consists of three parts. The first part relates to monitoring the implementation of grants and cooperative agreements through site visits and the monitoring of grantee cost-sharing contributions. The second part concerns the requirement that grantees prepare periodic progress reports on their programs and the third part involves the requisite for

evaluating grants. In planning and performing this objective we considered Sections 110 and 621 A(b) of the Foreign Assistance Act, OMB Circular A-110 and the applicable internal control policies and procedures cited in A.I.D. Handbooks 3 and 13. We classified the relevant policies and procedures into categories called the monitoring, reporting and evaluating processes.

First, we reviewed the Mission's controls relating to monitoring grants and cooperative agreements through the performance of site visits and the monitoring of cost-sharing contributions. Our assessment showed that for site visits, although not considered a significant internal control weakness, the internal controls were logical but not consistently applied because project officers did not document the results of their visits. This problem area and related recommendation is discussed on pages 9-10. Regarding the monitoring of cost-sharing contributions, our assessment showed that the Mission's internal controls were not properly designed or implemented because written guidelines were not established for monitoring, verifying, documenting, and reporting grantee contributions. Therefore we could not rely on them in designing an audit approach. However, we conducted more extensive testing to achieve our objective of determining whether USAID/Costa Rica could properly monitor the cost-sharing contributions. These alternative procedures consisted of reviewing seven selected grants to determine whether grantee contributions were made. We concluded that USAID/Costa Rica's internal controls did not provide assurance that cost-sharing contributions were properly made.

Second, we reviewed the Mission's controls relating to ensuring that grantee's prepare periodic progress reports. Our assessment showed that the controls were not logically or consistently applied; therefore, we could not rely on them in designing our audit approach. However, we conducted more extensive testing to achieve our objective of determining whether USAID/Costa Rica could properly monitor the progress of grant programs. These alternative procedures consisted of reviewing seven randomly selected grants to determine whether recipients were submitting progress reports as required. We concluded that USAID/Costa Rica's internal controls did not provide assurances that grantees prepared adequate progress reports.

Finally, we reviewed the Mission's controls relating to the evaluation of grants and our tests showed that USAID/Costa Rica's controls were logically and consistently applied. Therefore we limited our tests to a review of the evaluations performed under six projects.

It should be noted that the significant weaknesses pertaining to cost-sharing contributions and grantee progress reports were not reported by USAID/Costa Rica in its 1991 internal control assessment.

Audit Objective Five

This objective examined USAID/Costa Rica's policies and procedures to ensure that grantees performed annual independent audits. In planning and performing this objective, we reviewed the applicable internal control policies and procedures cited in A.I.D. Handbook 13, Appendix 4D. We classified these policies and procedures into a category called the audit monitoring process.

We reviewed the Mission's internal controls relating to the audit monitoring process and our tests showed that the Mission's internal controls were logically and consistently applied. Therefore, we limited our tests to determining if the Mission established an audit tracking system, identified its audit universe, and ensured that audits were carried out as planned.

Audit Objective Six

Our last audit objective concerned the Mission's system for closeout, suspension, or termination of grants. In planning and performing this objective, we reviewed the applicable internal control policies and procedures cited in A.I.D. Handbook 13, Chapter 1, OMB Circular A-110, and CIB No. 90-12. We classified these policies and procedures into a category called the closeout process.

We reviewed the Mission's internal controls relating to the closeout process and our tests showed that the Mission's internal controls were not logically or consistently applied; therefore, we could not rely on them in designing our audit approach. However, we conducted more extensive testing to achieve our objective of determining whether USAID/Costa Rica ensured that grants were properly closed out. These alternative procedures consisted of reviewing nine grants that were closed out in the last six months. We concluded that the Mission had not fully established a system that provided sufficient assurances that grants are adequately closed out.

It should be noted that this significant weakness in the Mission's controls was reported by USAID/Costa Rica in its 1991 internal control assessment.

REPORT ON COMPLIANCE

This section summarizes our conclusions on USAID/Costa Rica's compliance with applicable laws and regulations.

Scope of Our Compliance Assessment

We conducted our audit in accordance with generally accepted government auditing standards which 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 USAID/Costa Rica's compliance with provisions of FAA Section 110 (Cost-Sharing and Funding Limits) related to ensuring that at least 25 percent of the costs of the project may be provided from sources other than the U.S. Government; OMB Circular A-110 (Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Nonprofit Organizations), Attachments D through I and K; OMB A-133 (Audit of Institutions of Higher Education and Other Nonprofit Institutions); CIB Nos. 87-25 (Evaluations Scopes of Work), and 87-5 and 90-12 (Closing Out Contacts, Grants and Cooperative Agreements); and grant agreements as they could affect our audit objectives. However, our objective was not to provide an opinion on USAID/Costa Rica's overall compliance with such provisions.

Although the Director, USAID/Costa Rica provided us with certain essential written representations, he did not provide written representation concerning his knowledge of any noncompliance or possible violations of laws and regulations for the activities audited. Also, other USAID/Costa Rica officials directly responsible for the activities audited did not provide

written representations to the Director, USAID/Costa Rica confirming essential information.

The limited representations on compliance and lack of written representations from officials directly responsible for the activities audited constitute a limitation on the scope of the audit and are sufficient to preclude us from providing an unqualified opinion on compliance with applicable laws and regulations. Therefore, we are disclaiming an opinion.

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 an organization's 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 applicable laws, regulations, and contractual obligations is the overall responsibility of USAID/Costa Rica's management.

Conclusions on Compliance

As noted in the Scope of Our Compliance Assessment section of this report, we have disclaimed an opinion on USAID/Costa Rica's compliance with laws and regulations. However, our tests showed that it was not in compliance with Section 110 of the FAA. Since USAID/Costa Rica has not established internal controls for monitoring, verifying, documenting, and reporting the contributions there was no basis for determining if at least 25 percent of the cost of the grant-funded projects was provided as planned in agreements for four of the seven grants reviewed. (See page 10.)

**SCOPE AND
METHODOLOGY**

Scope

We audited selected systems of internal controls at USAID/Costa Rica concerning its processes for providing assistance to nonprofit organizations under the guidance of A.I.D. Handbook 13. We identified an audit universe consisting of 19 grants awarded under this guidance during the period from June 1986 to September 1991. For testing purposes, we judgmentally selected seven of the 19 grants awarded by USAID/Costa Rica under A.I.D. Handbook 13. The seven grants selected were valued at \$31.1 million or 70 percent of the \$44.6 million awarded by the Mission for the entire portfolio. We conducted the audit from March 16 to May 14, 1992, at the offices of USAID/Costa Rica in San Jose, Costa Rica. The audit entailed reviewing Mission files and records, reviewing those policies and procedures necessary to determine whether USAID/Costa Rica established and implemented policies and procedures to ensure that audit objectives could be answered, and interviewing USAID/Costa Rica officials. For each audit objective, we discussed our audit results with cognizant Mission officials. We visited two grantee recipients to interview officials and verify information. We also verified information with a third grantee, through a telephone communication. Our audit work was conducted in accordance with generally accepted government auditing standards, except as discussed below with regard to the extent of representations made by USAID/Costa Rica management officials.

Government auditing standards state that auditors should, when they deem it useful, obtain written representations from the officials of the audited entity. The Office of the Inspector General has determined that representation letters are necessary to support potentially positive findings. We requested USAID/Costa Rica management to provide written representation with regard to the activities audited under this assignment. In response to our request the Director, USAID/Costa Rica provided us with certain essential written representations concerning his: 1) overall responsibility, as Director, for the internal control system, compliance with applicable laws, regulations, and legally binding requirements, and fairness and accuracy of accounting and management information; 2) request to

appropriate member of the USAID/Costa Rica staff to make available all records in their possession for purposes of the audit, 3) belief, based on representations made to him by his staff, that the records are accurate and complete and give a fair representation of the status of the control systems covered by the audit, and 4) knowledge of no other facts which would alter the conclusions reached in the draft audit report. Per the Director's request the representation letter provided by USAID/Costa Rica is presented in Appendix II.

Although the Director provided us with the above representations, he did not provide written representations concerning: 1) whether all information relevant to the audit objectives was provided, 2) knowledge of any irregularities within or involving the audited activity, 3) knowledge of any noncompliance with A.I.D. policies and procedures or violations of laws and regulations, and 4) knowledge of any events occurring subsequent to the period under audit which may have an effect on the representations made. Also, other USAID/Costa Rica officials directly responsible for the audited activities did not provide written representations to the Director, USAID/Costa Rica confirming essential information. As a result, our answers to the audit objectives are qualified to the extent of the effect of not having such representations. Finally, because USAID/Costa Rica officials did not provide a written representation concerning their knowledge of noncompliance or possible violations of laws and regulations for the audited activities, we have disclaimed an opinion in our Report on Compliance.

To achieve the assignment's objectives we extensively relied on computer-processed data contained in MACS reports. Except for determining the status of advances, we did not establish the reliability of this data because it was not critical for answering our audit objectives.

USAID/Costa Rica's portfolio of Handbook 13 grants was valued at \$ 44.6 million of which \$28.6 million was expended. Our sample selected was valued at \$31.1 million of which \$18.8 million was expended. We did not specifically verify and audit these amounts, rather our audit focused on selected systems for controlling grant activities.

Methodology

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

Audit Objective One

To accomplish the first audit objective, we obtained and reviewed A.I.D. Handbook 1, Supplement B and Handbook 13, Chapter 2 as well as

mission orders to determine the criteria for reviewing and authorizing proposals and awarding grants. Additionally, we reviewed policy papers on private voluntary organizations and population assistance to determine their applicability. We interviewed operating personnel to determine if they adhered to the established criteria. We identified a universe of 19 grants awarded to nonprofit organizations. To answer the audit objectives, we selected from this universe a sample of 7 grants. Subsequently, we reviewed the files and obtained the supporting documentation for each of the 7 grants and compared against the criteria to determine if USAID/Costa Rica established and followed procedures for reviewing and authorizing solicited and unsolicited proposals and in awarding the grants.

Audit Objective Two

To achieve the second audit objective, we obtained and reviewed criteria cited in A.I.D. Handbook 3, Appendix 4C and Section 621 of the FAA. We reviewed 7 grant files from a universe of 19 and obtained pertinent documentation regarding registration of private voluntary organizations. We interviewed operating personnel to determine USAID/Costa Rica policies and procedures and compared them to the requirements of the previously stated criteria.

Audit Objective Three

To answer the third objective, we obtained and reviewed criteria stated in A.I.D. Handbook 19, Appendix 1B, and the Controller's Guidebook. We also reviewed USAID/Costa Rica's internal controls on advances described in Mission Orders. We held discussions with USAID/Costa Rica officials to determine their policies and procedures for negotiating and liquidating advances and compared them to the requirements in the previously cited criteria.

We obtained a MACS report on advances at USAID/Costa Rica which listed those advances which were past the required settlement date. For the 7 grants tested we verified the accuracy of this report by tracing the amounts to the supporting documentation. We discussed our analysis with USAID/Costa Rica officials and were told that for one overdue outstanding advance they will initiate corrective actions.

Audit Objective Four

For the fourth audit objective, we obtained and reviewed FAA Sections 110 and 621, OMB Circular A-110, and the applicable internal control policies and procedures cited in A.I.D. Handbooks 3 and 13 and the Project Officers' Guidebook as they relate to performing site visits, reporting cost-sharing contributions, grantee progress reporting, and evaluation of grants. We

interviewed USAID/Costa Rica officials to determine their policies and procedures with respect to these four areas. From our sample of grants we reviewed grant files to identify if site visit reports were filed. We also obtained information and reviewed progress reports submitted by grantees to determine if they conformed to the requirements of OMB Circular A-110, Attachment H, cost-sharing contributions disclosed by the Mission in its semiannual reports, and evaluations conducted on the grants.

We interviewed operating personnel to determine USAID/Costa Rica policies and procedures regarding the above four areas and compared them to the requirements of the previously stated criteria.

Audit Objective Five

To accomplish the fifth objective, we obtained and reviewed criteria cited in OMB Circular A-133, A.I.D. Handbooks 3 and 13 and internal guidance established in mission orders to determine if USAID/Costa Rica established policies and procedures to ensure that grantees performed annual independent audits. The Mission identified and we verified a universe of grants under the Recipient Contracted Audit Program and the written procedures for an Audit Tracking System.

We interviewed operating personnel to determine the procedures to ensure that grantees performed the required annual audits and compared them to the requirements. Subsequently, from our sample of grants we reviewed grant agreements to determine whether required audit and budget provisions were included. We reviewed the files for these grants to determine whether USAID/Costa Rica received copies of the audit reports. For those audit reports on file, we reviewed them to determine whether the audits were performed in accordance with government auditing standards.

Audit Objective Six

To achieve the sixth objective, we obtained and reviewed criteria cited in A.I.D. Handbooks 3 and 13, contract information bulletins, and mission orders, to determine if USAID/Costa Rica established and implemented policies and procedures regarding closeout of grants. We interviewed operating personnel to verify if established policies and procedures were followed. USAID/Costa Rica prepared a list of projects and grants which had expired and needed to be closed and a list of nine grants that had been closed since January 1992. We verified provided information, obtained and reviewed documentation supporting the closeout process for these nine grants, and compared against the above cited guidance.

MANAGEMENT COMMENTS



AGENCY FOR INTERNATIONAL DEVELOPMENT
UNITED STATES A.I.D. MISSION TO COSTA RICA

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MEMORANDUM
FAS-92/C-511

DATE: October 19, 1992
TO: Lou Mundy, RIG/AT, USAID/Tegucigalpa
FROM: Ronald F. Venezia, Director, USAID/Costa Rica 
SUBJECT: DRAFT AUDIT REPORT OF USAID/COSTA RICA'S GRANTS AND COOPERATIVE AGREEMENTS

The Mission has reviewed the subject draft audit report. We do not disagree with any information, comments, or recommendations presented in the draft report.

The Mission agrees with the five recommendations presented in the subject draft report and has taken steps to resolve or close each of them. Specific comments are presented below:

RECOMMENDATION NO.1: We recommend that USAID/Costa Rica:

- 1.1. "amend current mission orders to designate the officer and office responsible for reviewing and awarding grants to nonprofit organizations"

USAID/Costa Rica agrees with the recommendation and has revised/issued two Mission Orders (Nos. 565-A and 592; copies attached) to designate the officer and office responsible for reviewing and awarding grants to nonprofit organizations. These steps fully implement this recommendation. USAID requests that this recommendation be closed based on the issuance of the above Mission Orders.

- 1.2. "issue in final the draft mission order which covers internal control procedures for preaward evaluations of prospective grantees".

USAID/Costa Rica agrees with the recommendation and has issued Mission Order No. 1150 (copy attached), which establishes internal control procedures for preaward evaluations of prospective grantees. The issuance of the Mission Order fully implements this recommendation. USAID requests that this recommendation be closed based on actions taken.

RECOMMENDATION NO.2: We recommend that USAID/Costa Rica:

- 2.0. "implement its guidelines requiring project officers to prepare and distribute site visit reports".**

USAID/Costa Rica agrees with the recommendation and has issued Mission Order No. 570-A (copy attached) to fully implement this recommendation. In addition, the Project Development Office will develop site visit report filing and tracking systems to ensure compliance with Mission site visit reporting guidelines. USAID requests that this recommendation be closed based on the issuance of the above Mission Order.

RECOMMENDATION NO.3: We recommend that USAID/Costa Rica:

- 3.1. "establish written policies and procedures for monitoring, verifying, documenting, and reporting cost-sharing contributions"**

USAID/Costa Rica agrees with the recommendation and has issued Mission Order No. 574 (copy attached) to establish written policies and procedures for monitoring, verifying, documenting, and reporting cost-sharing contributions. In addition, the Mission has modified the standard audit scope-of-work under the Recipient Contracted Audit Program to include the preparation of and opinion on Fund Accountability Statements of cost-sharing contributions. The Project Development Office, when appropriate, will amend existing HB13 agreements to include special cost-sharing contributions reporting provisions. These steps fully implement this recommendation. USAID requests that this recommendation be closed based on actions taken.

- 3.2. "report this condition as a weakness in the next internal control assessment if not fully resolved".**

USAID/Costa Rica agrees with the recommendation and as stated above considers this condition to be fully resolved. Therefore, this condition will not be reported as a weakness in the next Mission internal control assessment. USAID requests that this recommendation be closed based on actions taken.

RECOMMENDATION NO.4: We recommend that USAID/Costa Rica:

- 4.1. "establish internal controls to ensure that grantees comply with reporting requirements in Handbook 13, Section 1N. These requirements, as a minimum, should cover areas such as (a) frequency of reports, (b) the need to report progress achieved against quantitative indicators and approved work plans, (c) identification of problem areas affecting project implementation, and (d) work to be undertaken during the next reporting period"**

USAID/Costa Rica agrees with the recommendation and has issued Mission Order No. 562 (copy attached) to establish internal controls to ensure that grantees comply with reporting requirements in Handbook 13, Section 1N. These requirements, as a minimum, cover areas such as (a) frequency of reports, (b) the need to report progress achieved against quantitative indicators and approved work plans, (c) identification of problem areas affecting project implementation, and (d) work to be undertaken during the next reporting period. In addition, as part of the Semiannual Review (SAR) process, the Project Development Office will track grantee compliance with the reporting requirements in Handbook 13, Section 1N. This tracking will ensure compliance with Mission reporting guidelines. These steps fully implement this recommendation. USAID requests that this recommendation be closed based on actions taken.

- 4.2. **"report this condition as a weakness in the next internal control assessment if not fully resolved".**

USAID/Costa Rica agrees with the recommendation and as stated above considers this condition to be fully resolved. Therefore, this condition will not be reported as a weakness in the next Mission internal control assessment. USAID requests that this recommendation be closed based on actions taken.

RECOMMENDATION NO.5: We recommend that USAID/Costa Rica:

- 5.0. **"amend its mission order on closeout of grants and cooperative agreements to incorporate the appropriate requirements from Handbook 13 and Contract Information Bulletin No. 90-12".**

USAID/Costa Rica agrees with the recommendation and is in the process of amending its Mission Order No. 575 on project closeout procedures to incorporate the appropriate requirements from Handbook 13 and Contract Information Bulletin No. 90-12. The Mission will provide a copy of the amended Mission Order to the Regional Inspector General as soon as it is issued. As of now, USAID requests that this recommendation be classified as resolved. USAID expects the recommendation to be closed upon issuance of the amended Mission Order.



AGENCY FOR INTERNATIONAL DEVELOPMENT

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May 14, 1992

Mr. Lou Mundy
RIG/A/Tegucigalpa
Agency for international Development

Dear Mr. Mundy

In connection with your audit of Grants and Cooperative Agreements at USAID/Costa Rica covering procedures in place for grants awarded from June 1986 to September 1991, I confirm the following representations made to your staff during the audit.

1. For the eight categories of control systems covered by the audit

1. Selection of Grant Recipients
2. Registration Process
3. Payment Process
4. Management of Grants and Cooperative Agreements
 - a) Monitoring Process
 - b) Reporting Process
 - c) Evaluating Process
5. Audit Monitoring process
6. Closeout Process

I, as Mission Director for the period August 1990 to September 1991, had overall responsibility for

- the internal control system
- compliance with applicable laws, regulations and legally binding requirements and
- the fairness and accuracy of the accounting and management information

2. I further confirm that I have asked appropriate members of my staff to make available to your staff all records in our possession for the purposes of this audit. Based on the representations made by those individuals to me, I believe that those records are accurate and complete, and that they give a fair representation as to the status of the the eight categories of control systems covered by the audit. After review of your draft audit report and consultation with my staff, I know of no other facts (other than those expressed in the Mission's comments given in response to the draft report) which, to the best of my knowledge and belief, would materially alter the conclusions reached in the draft report.

I request that this Representation Letter be considered a part of the official Mission comments on the draft report, and be published along therewith as an annex to the report.

Sincerely,


Mission Director/USAID/Costa Rica

**USAID/Costa Rica's Portfolio of
Handbook 13 Grants and Cooperative Agreements
as of March 31, 1992¹**

Grants/Projects Managed by	Project Number	Project Name	Grant Funding
Rural Development Office	596-0129 ²	Regional Higher Education	\$12,310,582
	515-0243	Forest Management	7,500,000
	515-0237	Non-Traditional Exports	3,500,000
	515-0248	Cooperating Management Strengthening	1,000,000
	515-0255	Forest Conservation Management	1,000,000
	515-0249	Caribbean Conservation Corp.	550,000
	936-5542	Program Science and Technical Cooperation	296,000
	515-0235 ³	Northern Zone Consolidation	270,000
	515-0235 ³	Northern Zone Consolidation	137,000
	515-0235 ³	Northern Zone Consolidation	8,644

¹ Unaudited figures provided by the Controller's Office based on MACS records

² Shaded projects valued at \$31.1 million selected to test the Mission's system

³ Same project but grants awarded to three different implementing agencies

Grants/Projects Managed by	Project Number	Project Name	Grant Funding
General Development Office	515-0232	Private Agencies Collaborating Together	4,900,000
	515-0242	Central American Peace Scholarship	2,667,077
	515-0168	Family Planning Self Reliance	2,200,000
	515-0252	Support to PVOs (ACORDE)	2,000,000
	515-0258	Cooperative Housing Foundation	1,600,000
	515-0253	Drug Awareness	500,000
Project Development Office	940-0002	Ecological Tourism	50,000
Private Sector Office	515-0257	International Executive Service Corporation	1,300,000
Regional Administration of Justice Office	515-0244	Justice Sector Improvement	2,833,329
Total			\$44,622,632

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FA/MCS	1
FA/FM/FPS	2
IG	2
AIG/A	1
D/AIG/A	1
IG/A/PPO	3
IG/LC	1
IG/RM	12
IG/I	1
IG/A/PSA	1
IG/A/FA	1
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