

Regional Inspector General for Audit  
San Jose, Costa Rica

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**Audit of USAID/Honduras's  
Controls Over the Honduran Government's  
Counterpart Contributions**

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Audit Report No. 1-522-94-005  
March 22, 1994





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March 22, 1994

**MEMORANDUM**

TO: USAID/Honduras Director, Marshall Brown  
FROM: RIG/A/San Jose, *Coinage N. Gothard*  
SUBJECT: Audit of USAID/Honduras's Controls Over the Honduran Government's Counterpart Contributions

Enclosed are five copies of the subject report. Our audit work and written representations made by USAID/Honduras confirmed that controls over the Honduran Government's counterpart contributions were adequate in many areas. For example, the Mission successfully followed USAID policies and procedures by issuing a Mission Order requiring that counterpart contribution reporting be included in project agreements and establishing monitoring responsibilities for counterpart contributions.

USAID/Honduras's controls, however, could be strengthened by: (1) ensuring that counterpart contribution reports are received as required, (2) Project Implementation Reviews better documenting counterpart contribution problems, and (3) project officers testing the reliability of counterpart contribution reports before certifying the reports.

We made three recommendations to improve controls over the Honduran Government's counterpart contributions. Your comments to these recommendations and the draft report were fully considered in finalizing this report. Based on these comments, Recommendation Nos. 1 and 3 are resolved and Recommendation No. 2 is closed upon report issuance. Your comments to the draft report are summarized after each finding and are presented in their entirety in Appendix II.

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

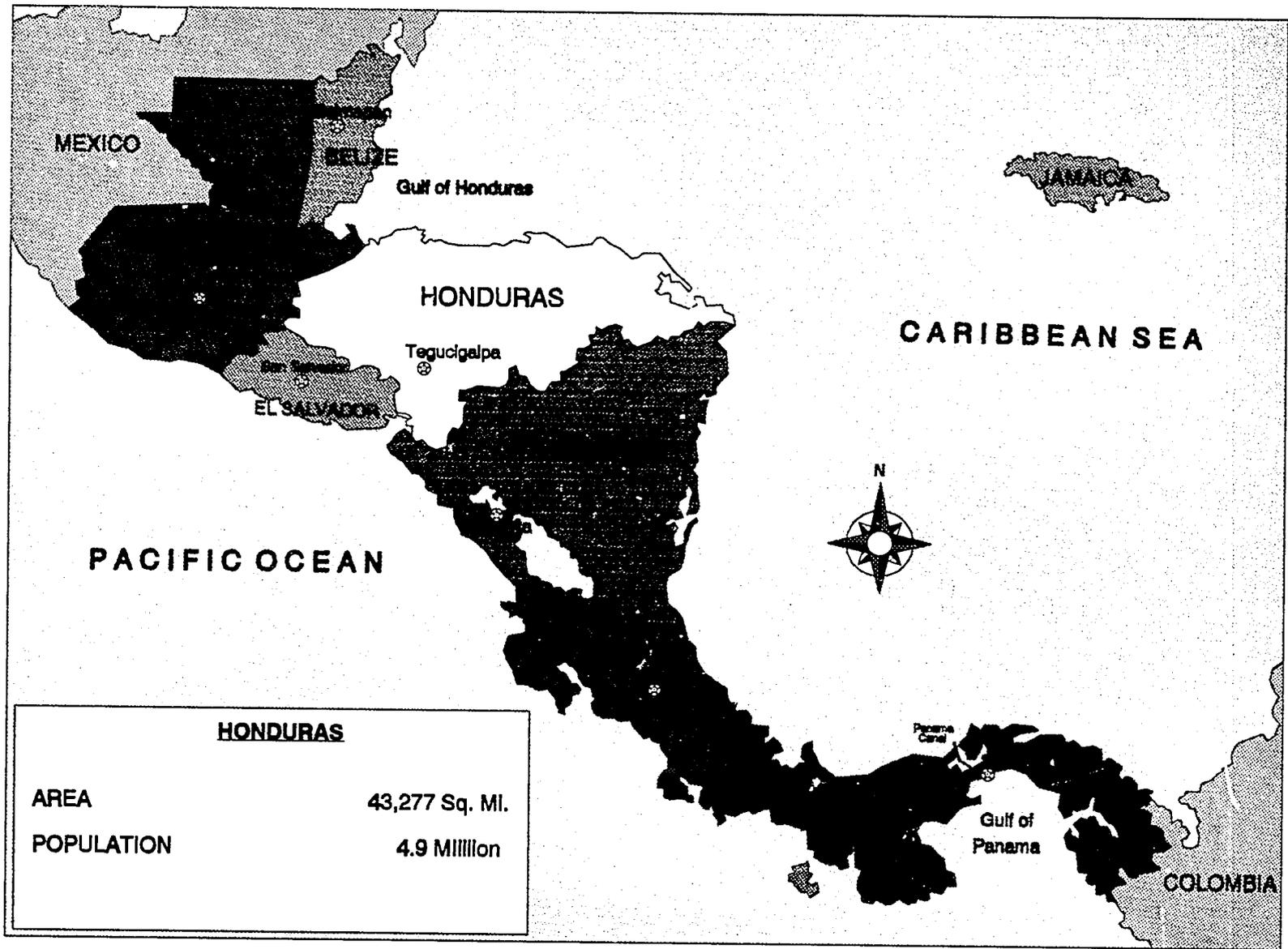
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## EXECUTIVE SUMMARY

To ensure that foreign governments have a vested interest in the success of USAID-financed activities, Congress enacted Section 110 of the Foreign Assistance Act of 1961 to require assurances that these governments will generally finance at least 25 percent of each USAID-financed activity. Audits made between 1982 and 1987, however, disclosed significant problems with USAID's willingness or ability to hold foreign governments accountable for their financial commitments. Since 1987 USAID has established additional procedures to correct these problems, the most recent procedures being established in 1991. To comply with these procedures, USAID/Honduras was responsible for ensuring that the Honduran Government provided agreed-upon contributions to 16 active projects. As of March 31, 1993, USAID had authorized \$310 million for these 16 active projects, and the Honduran Government had agreed to provide \$236 million (see pages 1 and 2).

USAID/Honduras followed USAID's 1991 cable guidance to ensure that systems are in place to obtain information on host government contributions and that such information is recorded in official records/files of the Mission. However, these systems were not yet fully implemented and improvements are needed in the following areas:

- USAID/Honduras has not required the Government of Honduras to report on its contributions to 6 of the 16 active projects (although the Government did, in fact, report for 2 of these projects) and has not enforced the reporting requirements which have been established for another 5 projects. As a result, USAID/Honduras did not have an accurate accounting on how much of the required \$151 million in counterpart contribution for 9 projects had been contributed to the Government of Honduras (see page 6).
- USAID/Honduras Project Implementation Reviews for the 16 active projects did not identify all problems related to counterpart contributions. As a result, USAID/Honduras did not take action to correct counterpart contribution reporting problems identified in our audit, such as: incomplete, untimely, or no counterpart contribution reporting (see page 9).

- USAID/Honduras did not certify the reasonableness of any reports received from the Government of Honduras nor perform tests on the reliability of reported contributions for the active projects which reported on time. As a result, USAID/Honduras did not have assurance that the counterpart contribution reported by the Government of Honduras was accurate (see page 12).
- Although USAID/Honduras defined the basis for valuing the Government of Honduras's contributions in agreements, USAID/Honduras used incorrect exchange rates when valuing the reported local currency contributions for 3 of 6 projects sampled. In addition, USAID policy and procedures for valuing counterpart contributions are not completely clear and, therefore, the valuation of the required contributions may not have been proper (see page 14).

This report contains three recommendations to: better enforce reporting requirements for host government contributions (see page 7), document the adequacy of host government contributions during Project Implementation Reviews (see page 9), and establish additional controls to ensure the reliability of reports on these contributions (see page 11).

In commenting on a draft of this report, USAID/Honduras acknowledged that further progress was needed to implement controls over host country contributions.

*Office of the Inspector General*

Office of the Inspector General  
March 22, 1994

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# INTRODUCTION

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## Background

Similar to the principles of cost sharing and matching contributions in Federal domestic aid programs, contributions by foreign governments are usually required to ensure that these governments have a vested interest in the success of USAID-financed activities. To ensure this vested interest, Section 110 of the Foreign Assistance Act of 1961 provides that:

*No assistance shall be furnished by the United States Government to a country under sections 103 through 106 of this Act until the country provides assurances to the President, and the President is satisfied that such country will provide at least 25 per centum of the costs of the entire program, project or activity with respect to which such assistance is to be furnished, except that such costs borne by such country may be provided on an 'in-kind' basis.*

While this section of the Act applies only to bilateral, government-to-government activities funded with development assistance appropriations, and the Development Fund for Africa (Section 496d), USAID has administratively extended this requirement to activities funded with the Economic Support Fund.

Audits made by the Office of the Inspector General and the General Accounting Office have found recurrent problems with host country contributions. One example of these problems is USAID Missions did not attach importance to proper accounting for host government contributions.

In a 1987 memorandum to the Assistant Administrator of the Office of Program and Policy Coordination, the Inspector General also noted that, in 146 project audits covering the years 1982 to 1987, the recommendation for managers to require host governments to provide and account for their contributions was made 59 times. However, project design, implementation, monitoring, and reporting problems related to host-country contributions persisted. The Inspector General further pointed out that the problems were worldwide in USAID's programs, affecting all bureaus, and that the Agency needed to issue additional guidance in several areas.

Since 1987, USAID has responded to these problems with additional policies and procedures to, among other things, (1) require the preparation of pro forma host country contribution budgets early in the project design process, and (2) provide specific details about the application, definition, and calculations of host country contributions. Also, in 1991, USAID established additional procedures (Department of State Cable number 138349, dated April 27, 1991) requiring Missions to:

- ***ensure that systems are in place to obtain information on host government contributions and that such information is recorded in the official records/files of the Mission;***
- ***include in agreements or Project Implementation Letters, a requirement for the host government to report at least annually on their contribution;***
- ***review the adequacy of host government contributions during project implementation reviews and test the reliability of the reports by Mission site visit reviews and evaluations; and***
- ***adhere to USAID. Handbook 3, Chapter 2, Appendix 2G and Handbook 1, Part VII, 2.41 for computing the value of in-kind contributions and rate of exchange to be used for calculating host government contributions.***

USAID/Honduras had 16 active projects which required host country contributions as of March 31, 1993. USAID authorized \$310 million for these 16 projects, and the Government of Honduras agreed to provide \$236 million, or 43 percent of the total project costs of \$546 million. USAID obligations and expenditures as of March 31, 1993 for the 16 projects were \$243 million and \$177 million, respectively. The amount of Government of Honduras's contributions was reported as \$192 million; however, this amount has not been verified.

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## Audit Objectives

As part of a world-wide audit lead by RIG/A/Singapore, the Office of the Regional Inspector General for Audit/San Jose audited USAID/Honduras's controls over the Government of Honduras's counterpart contributions to answer the following audit objectives:

- Did USAID/Honduras follow USAID's 1991 cable guidance to ensure that systems are in place to obtain information on host government contributions and that such information is recorded in the official records/files of the Mission?

- Did USAID/Honduras follow USAID's 1991 cable guidance to include in agreements or Project Implementation Letters a requirement for the host government to report at least annually on its contribution?
- Did USAID/Honduras follow USAID's 1991 cable guidance to (1) review the adequacy of the host government contribution during project implementation reviews and (2) test the reliability of the reports by Mission site visit reviews and evaluations?
- Did USAID/Honduras follow USAID's 1991 cable guidance to adhere to A.I.D. Handbook 3, Chapter 2, Appendix 2G and Handbook 1, Part VII, 2.41 for computing the value of in-kind contributions and rate of exchange to be used in calculating host government contributions?

In answering these audit objectives, we tested whether USAID/Honduras followed applicable internal controls and complied with certain legal requirements. We also included steps to detect abuse or illegal acts which could affect the audit objectives. As part of our audit, we requested USAID/Honduras's management to provide (upon receipt of the formal draft audit report) written representations which we consider essential to answering the audit objectives and assessing internal controls and compliance.

For problem areas, we did additional work to:

- identify the cause and effect of the problem; and
- make recommendations to correct the problem and the cause.

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

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## REPORT OF AUDIT FINDINGS

### **Did USAID/Honduras Follow USAID's 1991 Cable Guidance to Ensure That Systems Are in Place to Obtain Information on Host Government Contributions and That Such Information is Recorded in the Official Records/Files of the Mission?**

Although USAID/Honduras followed USAID's 1991 cable guidance to ensure that systems are in place to obtain information on host government contributions and that such information is recorded in the official records/files of the Mission, these systems were not yet fully implemented.

In July 1992, USAID/Honduras established procedures which assigned various Mission offices and individuals responsibilities for carrying out specific tasks to obtain and record information on the Honduran Government's contributions to the projects. Among other things, these Mission procedures required that:

- New and on-going projects include a requirement for the Government of Honduras to report quarterly on its contributions to USAID projects and the reports be received by the USAID/Honduras no later than 30 days after the end of each calendar quarter;
- Project Officers after obtaining the Government of Honduras's reports on contributions, sign the reports indicating the reasonableness of the information reported and test the reliability of counterpart performance by periodic site visits, informal reviews, and evaluation;
- Compliance with counterpart contribution requirements will be either reviewed through formal USAID/Honduras Controller office reviews or audited through recipient or non-Federal audit programs; and
- The Office of Development Finance ensure that USAID/Honduras's program is in compliance with Section 110 of the Foreign Assistance Act of 1961, as amended, and ensure that official project files contain contribution reports certified by the project officer.

Mission personnel, however, had not yet fully implemented these procedures. For example, formal reporting requirements were not established for 6 of the 16 active projects and reporting requirements which

were established were not enforced for another 5 projects (see page 6 for a discussion of this problem). Another example is that, although the Mission reviewed the adequacy of contributions during project implementation reviews, the reviews did not identify all counterpart contribution problems (see page 9 for a discussion of this problem). Also, reported counterpart contributions were not tested for its reliability nor were the reports certified for reasonableness (see page 11 for a discussion of this problem). And, for 3 of the 6 projects tested, USAID/Honduras did not adhere to established procedures for computing the value of in-kind contributions and the rate of exchange used in calculating the Government of Honduras's contributions (see page 15 for a discussion of this problem). Since these problems areas are discussed in other sections of this report, separate recommendations are not being repeated here.

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### **Did USAID/Honduras Follow USAID's 1991 Cable Guidance to Include in Agreements or Project Implementation Letters a Requirement for the Host Government to Report at Least Annually on its Contribution?**

USAID/Honduras did not fully follow USAID's 1991 cable guidance to include in agreements or Project Implementation Letters a requirement for the Honduran Government to report at least annually on its contributions.

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... USAID/Honduras did not establish reporting requirements for six projects and did not enforce the reporting requirements that were established for another five projects.

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For 10 of 16 active projects which required host country contributions, USAID/Honduras established, in Project Implementation Letters (PILs) or agreement amendments, requirements for the Government of Honduras to report quarterly on its contributions to the projects and provided sample reporting formats. However, USAID/Honduras did not establish reporting requirements for the remaining six projects and did not enforce the reporting requirements that were established for another five projects.

### **The Government of Honduras Did Not Always Report Its Contributions**

Contrary to USAID procedures, USAID/Honduras did not require the Government of Honduras to report on its contributions to 6 of the 16 projects active at the time of our audit; however, the Government of Honduras did, in fact, report on its contributions to 2 of these 6 projects. For another 5 active projects, USAID/Honduras did not enforce the

reporting requirements which were established. Although USAID/Honduras designed new procedures to establish and enforce the reporting requirements, prompt implementation was not emphasized. USAID/Honduras stated that the 1991 cable guidance did not establish a deadline for adding the reporting requirements and they decided to wait until the projects became due for incremental funding. As a result, the Mission did not have an accurate accounting on how much of the required \$151 million in counterpart contributions for 9 projects (4 not reporting and 5 reporting late) had been contributed by the Government of Honduras as of March 31, 1993.

Recommendation No. 1: We recommend that USAID/Honduras establish the reporting requirements for host-government contributions to the six projects lacking requirements and enforce the timely reporting of counterpart contributions.

One of the new USAID procedures established in 1991 was intended to strengthen host country accountability for its financial commitments by ensuring that the host country reports the status of its contributions for every USAID-financed activity which required contributions. According to the 1991 cable:

*Missions should include in agreements or PILs a requirement for host governments to report annually (more frequently if appropriate) on their contribution (cash and in-kind) to the AID financed program/project/activity. (USAIDs may design their own report format.) Where such requirements do not exist, an ideal time for adding this language would be when the project is amended to provide incremental funding, or when issuing the annual budget PIL if such procedures are utilized.*

In accordance with this USAID cable, USAID/Honduras established new procedures in July 1992 which required new and on-going projects to include in Project Agreements or Project Implementation Letters a requirement for the Government of Honduras to report quarterly on its contributions.

USAID/Honduras personnel did not fully implement these new USAID and Mission procedures when they did not require counterpart contribution reporting for 6 of the 16 projects active at the time of our audit; however, the Government of Honduras did, in fact, report on its contributions to 2

of these 6 projects<sup>1</sup>. USAID/Honduras stated that the 1991 cable guidance did not establish a deadline for adding the reporting requirements and they decided to wait until the projects became due for incremental funding. Also, counterpart reporting requirements were not enforced for 5 of the 10 active projects for which the Government of Honduras was required to report on counterpart contributions. Specifically, Mission procedures, as delineated in the July 1992 Mission Order, state that:

*... the Grantee shall provide USAID with quarterly reports on the provision of counterpart contributions which shall be submitted no later than 30 days after the end of each calendar quarter.*

An example of the lack of enforcement for counterpart contribution reporting occurred when the Government of Honduras provided the required reports late—four in May 1993 and one in June 1993. This problem was due to USAID/Honduras officials not emphasizing the enforcement of the reporting requirements which had been established for the five projects. As a result, USAID/Honduras did not have an accurate accounting on how much of the required \$151 million in counterpart contributions for 9 projects (4 not reporting and 5 reporting late) had been contributed by the Government of Honduras as of March 31, 1993.

In conclusion, USAID/Honduras needs to ensure that its established procedures for requiring and obtaining reports on the Honduran Government's contributions are fully implemented and establish the reporting requirements for the projects lacking requirements.

#### Management Comments and Our Evaluation

USAID/Honduras agreed with the recommendation. Host-government contribution reporting requirements were established for three of the six projects needing reporting requirements while two other projects were scheduled to have reporting requirements added by March 31, 1994 and the remaining project had reached its Project Assistance Completion Date. USAID/Honduras commented that since the 1991 cable guidance did not set a deadline for establishing host-government counterpart reporting requirements it was USAID/Honduras' strategy to include this requirement in Project Agreement Amendments as the projects came due for incremental funding. USAID/Honduras also noted that USAID guidance only requires annual reports--not quarterly--but they elected to be more strict in order to assure the timely receipt of information to meet management needs.

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<sup>1</sup> USAID/Honduras obtained counterpart contribution reports in August 1993 for the other four projects lacking reporting requirements.

USAID/Honduras said they would request recommendation closure after all of the Project Implementation Letters adding host-government contribution reporting requirements had been issued.

Based on USAID/Honduras's comments, Recommendation No.1 is resolved and will be closed when USAID/Honduras provides evidence that host-government contribution reporting requirements have been added to the active projects identified during the audit as lacking requirements or evidence that the project has reached its Project Assistance Completion Date.

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### **Did USAID/Honduras Follow USAID's 1991 Cable Guidance to (1) Review the Adequacy of the Host-Government Contributions During Project Implementation Reviews and (2) Test the Reliability of the Reports by Mission Site Visit Reviews and Evaluations?**

USAID/Honduras did not fully follow USAID's 1991 cable guidance to (1) review the adequacy of the host-government contributions during project implementation reviews or (2) test the reliability of the reports by Mission site visit reviews and evaluations.

As discussed below, USAID/Honduras needs to better review the adequacy of the Government of Honduras's contributions during Project Implementation Reviews and test for the reliability of counterpart contribution reporting.

#### **The Adequacy of Honduran Government Contributions Was Not Properly Reviewed**

Although USAID/Honduras reviewed the adequacy of counterpart contributions during Project Implementation Reviews as required by the 1991 cable guidance, these reviews did not identify all contribution problems such as incomplete, untimely, or no counterpart contributions reporting. Moreover, USAID/Honduras did not document reviews that were made. This situation occurred because of the Mission 's failure to adequately emphasize the importance of counterpart contributions during Project Implementation Reviews. As a result, USAID/Honduras did not take action to correct the counterpart contribution reporting problems identified, such as incomplete, untimely, or no counterpart contribution reporting.

**Recommendation No. 2:** We recommend that USAID/Honduras during Project Implementation Reviews (1) base reviews of counterpart

contributions on counterpart reports as of the current reporting period, (2) report all deficiencies related to counterpart contributions including untimely and inadequate reporting, and (3) fully document the discussions on counterpart contributions.

USAID's 1991 cable guidance requires Missions to review the adequacy of host country contributions during Project Implementation Reviews (PIRs) to ensure that project objectives are met. Although USAID/Honduras stated it reviewed the adequacy of counterpart contributions during these implementation reviews, our audit identified that the reviews did not discuss all counterpart contribution problems.

In the March 31, 1993 Semi-Annual Reports (SARs), only one project reported counterpart contributions as a problem. Our review of the documentation pertaining to the Mission's reviews found that the problems that we had identified, such as late reporting and reporting based on estimates, were not discussed. The following examples illustrate the problems we found:

- Reports on counterpart contributions from the implementing entities were received late. For example, four projects—the Small Business II, the Privatization of State-Owned Enterprises, the Honduran Agricultural Research Foundation, and the Shelter Sector Program projects—did not provide counterpart contribution reports covering March 31, 1993 until August 1993, three months after the April 30 deadline. Moreover, another five projects submitted counterpart contribution reports beyond that deadline date, i.e., these reports were submitted between May 10 and June 8, 1993.
- Estimated counterpart contributions were reported as actual. For example, the Project Officer for the Public Sector Policy Analysis and Implementation Project said he estimated the counterpart contributions reported in the March 31, 1991 SAR based on his knowledge of host government participation and a rough estimate of contributions made. He said the project had never received any counterpart contribution reports and he had nothing in writing to document his analysis of contributions.

Although Mission officials said that problems with the Government of Honduras's contributions were reviewed and discussed during Project Implementation Reviews, little documentation existed to show that the above mentioned problems had been reviewed or how these problems would be addressed.

Since the determination of the adequacy of counterpart contributions is dependent on adequate accounting and reporting of counterpart

contributions, we consider the untimely submission of these reports as a major problem area. Accordingly, we would expect that when counterpart contribution reports were not received by Project Officers that this problem be documented in the issues section of the SARs. As previously noted, the Mission's March 31, 1993 SAR only discussed one project with a counterpart contribution problem, nothing was mentioned about the lack of reporting as a problem.

It is clear that the Mission has taken steps to better monitor, report, and review counterpart contributions—as seen by the issuance of its July 1, 1992 Mission Order and its July 16, 1993 revised Mission Order. Nevertheless, project implementation reviews were not adequately documented and did not in all cases report deficiencies associated with counterpart contributions. USAID/Honduras's lack of emphasis on counterpart contributions during Project Implementation Reviews resulted in USAID/Honduras not taking action to correct counterpart contribution reporting problems.

#### Reports on Honduran Government Contributions Were Unreliable

Contrary to USAID procedures, USAID/Honduras did not certify the reasonableness of any report on Government of Honduras's contributions nor did it perform tests on the reliability of the counterpart contribution reports. This situation was due to insufficient management oversight and lack of procedures for testing the reliability of reported counterpart contributions during site visits. As a result, USAID/Honduras did not have assurance that the counterpart contributions reported by the Government of Honduras were accurate.

Recommendation No. 3: We recommend that USAID/Honduras establish procedures for ensuring that Project Officers certify the reasonableness of reports on the Government of Honduras's contributions only after the test for reliability of reported counterpart has been conducted and documented.

To ensure that host country contributions reported data are reliable, USAID procedures require Project Officers to review and certify the reasonableness of the reports and that the reliability of reports be tested by site visits and evaluations. The 1991 cable said:

*The adequacy of the HG contribution should be reviewed during Project Implementation Reviews (PIRs) and the reliability of the reports tested by Mission site visit reviews and evaluations. If HG centralized systems are not maintained, as a minimum, the Project Officer/Manager should obtain the HG 'cost sharing' report and, after*

*signing the report indicating the report's reasonableness in relation to project activity, staffing progress, etc., file the report in the official Mission project/program files.*

Consistent with these requirements, USAID/Honduras established guidelines and procedures in July 1992 to be followed for counterpart contribution reporting. These procedures require Project Officers to certify the reasonableness of reports on counterpart contributions in relation to project activity, staffing, progress, etc. A dated and signed statement by the Project Officer on the report itself would be acceptable for the purpose of certification. The Project Officer was also expected to send the report to be filed in the Office of Development Finance's (ODF) official project files and test the reliability of counterpart contributions performance by periodic site visits, informal reviews and evaluations. The ODF's backstop officer is responsible for reviewing the official project files to see that they contain contribution reports certified by the Project Officer.

Contrary to these procedures, USAID/Honduras did not certify the reasonableness of any report on Honduran Government contributions for the March 31, 1993 reporting period, and did not verify the reliability of the reports. These issues are discussed below.

Certification of Contribution Reports - Project Officers did not certify the reasonableness of any of the reports on the Honduran Government's contributions to the 16 USAID bilateral projects. At the audit cut-off date (March 31, 1993), we did not find any certified counterpart report filed in the official files in ODF. According to Project Officers this was not done because ODF never provided the Project Officers with any guidance on how the reports should be certified and never requested the project officers to submit the reports. In July 1993, USAID/Honduras in its revised Mission Order for Counterpart Contribution Reporting and Monitoring provided the standard language for Project Officer certification. In August 1993, USAID/Honduras provided the auditors certified counterpart contribution reports for the 16 active projects covering the March 31, 1993 period.

Verification of Contribution Reports - USAID/Honduras did not test the reliability of counterpart contribution performance by periodic site visits, informal reviews, and evaluations as required by its guidelines. We selected 6 of the 16 active projects in our audit universe to test verification of counterpart contributions reported by the Government of Honduras. Site visits with the purpose of verifying counterpart contributions were not done in all cases. For example, for 4 of the 6 projects tested, counterpart contributions were not discussed in site visit reports.

The 1991 cable and Mission Order require USAID/Honduras to verify reported counterpart contributions through site visits to the implementing entity. Since counterpart reports are required quarterly from the implementing entities and Project Officers must certify the reasonableness of these reports, the verification of these reports should be done through site visits on a quarterly basis. The degree of testing should be based on previous analysis of the administrative and accounting capabilities of the implementing entity as well as experience in reporting data to USAID/Honduras.

The 1991 cable also stated that the reliability of the counterpart contribution reports would be tested through Mission evaluations. Our review found that although 4 of the 6 projects had been evaluated, none of the evaluations addressed counterpart contributions.

In addition, Mission procedures state that compliance with counterpart contribution requirements will be either reviewed through formal Controller office reviews or audited through recipient or non-Federal audit programs. For the six projects tested, five had Controller office reviews with only one discussing counterpart contributions. Three audits were also conducted with only one discussing counterpart contributions.

There is clearly a need for USAID/Honduras to establish procedures spelling out the type of review and documentation necessary for adequate counterpart contributions verification. Mission's management should increase its supervision over the implementation of the procedures to ensure Project Officers fulfill their required duties, especially as it concerns site visit reviews and certification of counterpart contribution reports.

### Management Comments and Our Evaluation

USAID/Honduras generally agreed with Recommendations Nos. 2 and 3. Concerning Recommendation No. 2.1, USAID/Honduras used current data in the reviews of counterpart contributions during the Semi-Annual Review conducted for the period ending September 1993. Regarding Recommendation No 2.2 USAID/Honduras commented that according to Bureau for Latin America and the Caribbean's guidance for Semi-Annual Reviews USAID, missions should discuss only those major problems requiring the attention of senior mission management. In their judgement the projects reviewed during the March 31 and September 30, 1993 Semi-Annual Reviews did not include major counterpart reporting problems. They emphasized that all projects had reported on host-country contributions for the period ending September 1993. USAID/Honduras noted however, that they are committed to report any serious deficiencies related to counterpart contributions in the Semi-Annual Reviews. Regarding

Recommendation No. 2.3, USAID/Honduras commented that a Mission Order had been amended requiring the preparation of a memorandum documenting any major problems related to counterpart contributions discussed during the Semi-Annual Reviews.

Concerning Recommendation No. 3, USAID/Honduras officials believe the Recipient Contracted Audit Program is the mechanism to use for testing financial data and have confirmed that the scopes of work for these audits include a requirement to audit host-country contributions. Project officers, on the other hand, are reviewing and certifying host-country counterpart reports as reasonable based on their personal knowledge of project implementation and services provided similar to that of a project officer's administrative approval of payment vouchers. USAID/Honduras considers both procedures responsive to the audit recommendation and will request closure when the Recipient Contracted Audit Program audit plan has been established with the Government of Honduras Controller General.

Based on USAID/Honduras's comments Recommendation No. 2 is closed upon the issuance of this report while Recommendation No. 3 is resolved and will be closed when a copy of the Recipient Contracted Audit Program audit plan is provided to RIG/A/San Jose.

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### **Did USAID/Honduras Follow USAID's 1991 Cable Guidance to Adhere to USAID Handbook 3, Chapter 2, Appendix 2G and Handbook 1, Part VII, 2.41 for Computing the Value of In-Kind Contributions and Rate of Exchange To Be Used in Calculating Host Government Contributions?**

USAID/Honduras properly followed USAID's 1991 cable guidance to adhere to USAID Handbook 3, Chapter 2, Appendix 2G. However, USAID/Honduras did not follow Handbook 1, Part VII, Section 2.41 for computing the value of in-kind contributions and the rate of exchange to be used in calculating host government contributions.

USAID/Honduras followed Handbook 3, Chapter 2, Appendix 2G for the one project agreement signed after issuance of the 1991 procedures by:

- Calculating the level of Honduran Government contributions based upon the total cost of the projects;
- Identifying the project operating and/or capital costs to be provided by the Honduran Government; and

- Excluding contributions by other donors in the calculation of Honduran Government contributions as a percentage of total project costs.

However, USAID/Honduras did not consistently use appropriate exchange rates to calculate the value of the Government of Honduras's contributions.

#### **Agency Instructions for Valuing Host Government Contributions Were Not Clear**

Contrary to established procedures, USAID/Honduras did not consistently use the appropriate exchange rates when valuing the reported local currency contributions for 3 of 6 projects we sampled. This problem occurred because USAID's policy and procedures in this area are not very clear. As a result, the Mission's valuation of the contributions in its records and reports may not have been proper.

In an attempt to clarify, reaffirm, and extend USAID exchange rate policy, USAID issued in 1987 the Department of State cable number 1860822 (subsequently incorporated into USAID Handbook 1 as Part VII). This cable defined the Agency's new policy governing the appropriate exchange rate at which USAID, among other things, accounts for host government contributions to projects. Basically, the policy requires that the host country's real resource contribution be converted into dollars calculated at the highest exchange rate current at the time of the project agreement in order to determine the percentage contribution and the dollar equivalent. This basis of calculation ensures that the agreed-upon level of contributions (percentage and dollar equivalent) is not affected by fluctuations in exchange rates. Accordingly, Section 2.41 of this policy requires that:

*The value of the real resource contribution provided by a host country for a project or program generally should be obtained by first pricing the host country's real resource contribution in local currency. This figure then is converted into dollars at the HR [highest rate per U.S. dollar not unlawful that is available to anyone in a recipient country (sec.2.22)] current at the time of the project agreement so that A.I.D. and host country contributions can be expressed in one common monetary unit and so that the real resource contribution by the host country can be expressed in percentage and dollar-equivalent terms. Thus, at the signing of an assistance agreement, the host country's real resource contribution is to be expressed both in terms of absolute dollars and a percentage of the total project based on the domestic and foreign prices and the exchange rate existing at that date. This forms the basis for determining host country's absolute real resource contribution and percentage share of the total project throughout its*

*life, and insulates the host country's contribution from the effect of any exchange rate fluctuations which may occur.*

In addition, Section 2.42 states:

*... In no case, unless authorized by waiver ... , is the host country contribution, after recalculation of the entire project budget at the new exchange rate, to be an amount less than 25 percent of total project costs. Automatic downward adjustment in host country/recipient percentage contribution due to devaluation, inflation, and similar financial or economic events is not acceptable.*

The additional 1991 USAID procedures, governing host country contributions, reminded Missions of these policy requirements:

*Missions should follow guidelines in referenced Handbook [3] and Handbook 1, Part VII, 2.41 for computing value of in-kind contributions and rate of exchange to be used in calculating the HG contributions.*

In July 1992, in accordance with the above USAID policies and procedures, USAID/Honduras issued a Mission Order which required Mission staff to comply with Handbook 1, Part VII, 2.41. The Mission Order said:

*The value of the real resource contribution provided by the host country should be calculated by first pricing the contribution in local currency and then converting it into dollars at the highest rate not unlawful at the time the Project Agreement is signed.*

However, USAID/Honduras did not follow these procedures to calculate counterpart contributions using the exchange rate at the time the project agreement was signed, they instead used several exchange rates. For example, the Agreement to the Small Farmer Organization Strengthening project signed September 26, 1985 was amended on July 13, 1992 and stated:

*...The resources provided by the Borrower/Grantee for the Project will be not less than the lempira equivalent of \$22,465,530. The counterpart contribution shall be calculated as follows: \$19,804,000 shall be calculated at the exchange rate in effect on the date of the original Project Agreement, \$1:L2, equal to L39,608,000; the \$2,000,000 of additional counterpart financing required by amendment No. 7 shall be calculated at the exchange rate of \$1:L5.3, equal to L10,600,000, and the additional counterpart funds of \$661,530 required by this amendment shall be calculated at the current exchange rate of \$1:L5.4, equal to L3,572,262.*

Although USAID/Honduras used several exchange rates for the Small Farmer Organization Strengthening project, they did not consistently use this process for all projects. For example, the Forestry Development Project Agreement was signed December 29, 1987 when the exchange rate was 2 lempiras equaled 1 dollar, the same exchange rate that was in effect when the Small Farmer project was originally signed. This rate of L2 equal \$1 was used in the calculation of counterpart contributions reported in the March 31, 1993 Semi-annual Report (SAR) for the Forestry Development project; whereas, the rate of L5.3 equal \$1 was used for the Small Farmer project.

The exchange rate used greatly affects the amount of counterpart contributions actually reported. For example, the Forestry Development project reported L836,318 as counterpart contributions for the first quarter of 1993 and this was reported in the March 31, 1993 SAR as \$418,159 using an exchange rate of L2 equals \$1. If a more current exchange rate was used, such as L6 equal \$1, which was the rate at the end of March 1993, the amount reported would have been \$139,386 or 33 percent of what was actually reported. Considering that approximately \$4.8 million in counterpart contribution has yet to be provided to the Forestry Development project, the decision as to what is the appropriate exchange rate is essential.

The 1991 cable guidance also noted that when agreements called for contributions in excess of 25 percent, the Mission must ensure that the agreed total of host government contribution is provided so that project and program objectives are met. The Government of Honduras in the above example was to provide approximately 37 percent or \$11.7 million of the original \$31.7 million total Forestry project costs.

Using the less than current exchange rate of L2 equal \$1, the Government of Honduras could meet the originally planned contribution and still fall below the required percentage of total project cost in real dollar terms. For example, if the Government of Honduras provides the remaining \$4.8 million in counterpart contributions at the L2 equal \$1 rate, approximately L9.6 million would be provided. However, if the current exchange rate of L6 equal \$1 is used then the L9.6 million would only be valued at \$1.6 million rather than the required \$4.8 million or a shortfall of \$3.2 million. Accordingly, instead of providing the required \$11.7 million or 37 percent of total project costs, the Government of Honduras would provide only \$8.5 million or 27 percent of total project costs.

Although USAID guidance and Mission procedures state that the Government of Honduras's contributions would be calculated by using the exchange rate at the signing of the agreement, we found that this procedure

was not being done for 3 of 6 projects tested. USAID/Honduras is not consistently calculating contributions and needs to address the situation.

A closer look at the provisions of Handbook 1, Part VII shows that they are somewhat ambiguous and, depending on the intent of the guidance, Section 2.41 could be interpreted in one of two ways: either the exchange rate stated in the project agreement should be used throughout the life of the project or, the dollar value of the real resource contribution should be obtained no matter what happens to the exchange rate. The later interpretation coincides with Section 2.22 which requires the accounting for contributions to be made at the highest rate per U.S. dollar. Because the intent of the Agency guidance is unclear, we are not making a recommendation to the Mission at this time but will address this issue to the attention of USAID/Washington in the final capping report on the worldwide audits of host government contributions.

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## SCOPE AND METHODOLOGY

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### Scope

We audited USAID/Honduras's controls over the Government of Honduras's counterpart contributions in accordance with generally accepted government auditing standards. The audit was made from April 21, 1993 through August 26, 1993. We did field work at the Tegucigalpa offices of USAID/Honduras and at six Honduran implementing entity offices in Honduras. Our audit was confined to test and answer the Mission's implementation of four control requirements identified in USAID's 1991 cable (Number 138349) on host government contributions.

USAID/Honduras had 16 active bilateral Handbook 3 projects requiring counterpart contributions as of March 31, 1993. The Mission also had three expired projects which ended May 1991 or later. The total project funding was \$310 million. As of March 31, 1993, the obligations and expenditures for the 16 projects were \$243 million and \$177 million respectively.

According to the Mission's report on Host Country Contributions as of March 31, 1993, the Honduran Government's contributions for the 16 projects totalled \$192 million; however, this amount has not been verified.

In addition to the methodology described in the following section for each audit objective, we have requested a letter from USAID/Honduras's management (upon receipt of the formal draft report) providing written representations which we consider essential for answering our audit objectives and for assessing internal controls and compliance.

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### Methodology

The methodology for each audit objective is described below.

### Audit Objective One

The first objective was to determine whether USAID/Honduras followed USAID's 1991 cable guidance to ensure that systems are in place to obtain information on host government contributions and that such information is recorded in the official records/files of the Mission. To accomplish this objective, we evaluated the Mission's controls with respect to the policies and procedures set forth in USAID's 1991 cable guidance.

We interviewed USAID/Honduras Office Directors and Division Chiefs, the Controller, and Project Officers to establish their perspectives on (1) their roles and responsibilities for establishing and maintaining the systems for obtaining and recording the information, (2) who is responsible for ensuring compliance with the applicable standard defined in the cable, and (3) whether the Mission is fully complying with this standard. We obtained a copy of the Mission Order and any other existing documentation to further identify the system in place and to verify the validity of the testimonial evidence obtained from Mission personnel. Also, we incorporated the results of objectives two, three and four to determine whether the Mission fully implemented the procedures established through the Mission Order.

### Audit Objective Two

The second objective was to determine whether USAID/Honduras followed USAID's 1991 cable guidance to include in agreements or Project Implementation Letters, a requirement for the host government to report at least annually on its contribution. To accomplish this objective, we evaluated the Mission's controls with respect to the policies and procedures set forth in USAID's 1991 cable guidance.

We obtained from the project files, a copy of all Project Agreements and Project Implementation Letters for all 16 projects, and other correspondence identifying host country contribution reporting requirements. We reviewed these agreements and Project Implementation Letters to determine the inclusion of the reporting requirements. For the six projects lacking any reporting requirement, we followed up with the respective Project Officers and financial analysts to verify that reporting requirements had, in fact, not been established and obtained reasons for this. We verified that the Mission enforced the established reporting requirements by obtaining copies of all host country contribution reports on file. We also verified that Project Assistance Completion Reports included a summary statement on contributions made by the host country and other donors which includes comparison of planned versus actual contributions.

Audit Objective Three

The third objective was to determine whether USAID/Honduras followed USAID's 1991 cable guidance to (1) review the adequacy of the host government contribution during project implementation reviews and (2) test the reliability of the reports by Mission site visit reviews and evaluations. To accomplish this objective, we evaluated the Mission's controls with respect to the policies and procedures set forth in USAID's 1991 cable guidance.

We obtained copies of all the projects' host country contribution reports and then (1) determined if reports contained certifications by Project Officers verifying the reliability of reported information as required, and (2) traced the reported host country contributions to the Mission's semiannual status reports.

We judgmentally selected six projects and visited the respective implementing entities to verify that these agencies have documented/auditable evidence in support of the amounts disclosed in the contribution reports provided to USAID. For these six projects, we ascertained the validity of reported contributions. This was done through discussions with Project Officers and reviews of supporting documentation on file at the Mission and at the implementing agency offices.

The host country contributions reports for all projects were obtained and analyzed to determine if reports were submitted on time and if the reports were in the format as specified in the respective Project Implementation Letter or official correspondence.

To determine if reported contributions were verified during field trips or during visits to the Ministerial Offices of the Honduran Government, we held discussions with Project Officers. We also reviewed the field trip reports where these were prepared. Four Project Evaluations were reviewed to determine if the reports addressed the reliability of the Honduran Government's reports on host country contributions. We also held discussions with financial analysts from the Controller's office to determine their level of counterpart review.

Finally, we obtained and reviewed Project Implementation Review reports, USAID/Honduras's semiannual reports prepared for March 31, 1993 to determine if the reports contain evidence that the Mission had reviewed the adequacy of the Honduran Government's contribution and had determined that this contribution was adequate or not.

Audit Objective Four

The fourth objective was to determine whether USAID/Honduras followed USAID's 1991 cable guidance to adhere to USAID Handbook 3, Chapter 2, Appendix 2G and Handbook 1, Part VII, 2.41 for computing the value of in-kind contributions and rate of exchange to be used in calculating host government contributions. To accomplish this objective, we evaluated the Mission's controls with respect to the policies and procedures set forth in USAID's 1991 cable guidance and Handbooks 1 and 3.

We obtained and examined the one Project Agreement issued since April, 1991 and evaluated the execution of that agreement against Handbook 1, Part VII and Handbook 3, Appendix 2G criteria. We interviewed Project Officers to determine the exchange rates used for calculating contributions.

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USAID/HONDURAS  
MEMORANDUM



DATE : February 28, 1994

TO : Coinage Gothard, RIG/A/SJ

FROM : Marshall Brown, MD *Smalun*

APPENDIX II  
Page 1 of 7

SUBJECT : Draft Audit Report of USAID/Honduras Controls Over the Honduran Government's Counterpart Contributions.

The Mission has reviewed the draft audit report and has found it both helpful and informative. In fact, we have been actively implementing improvements in the management of host country contributions issues, several of which are responsive to the recommendations contained in the report. Our response is organized in two sections. The first section specifically addresses the report recommendations; the second section contains comments about the body of the report.

**RECOMMENDATION NO. 1**

We recommend that USAID/Honduras establish the reporting requirements for host-government contributions to the six projects lacking requirements and enforce the timely reporting of counterpart contributions.

**Mission Comments:**

The Mission agrees with this recommendation. The Mission has been in the process of formalizing this requirement through inclusion of appropriate project specific language in incremental funding ProAgs and budget PILs. Of the six projects mentioned in the recommendation, three now include the reporting requirement. One of the three remaining projects has reached its PACD. PILs to establish the reporting requirement for the two other projects will be issued by March 31, 1994. Once all the appropriate PILs have been issued, they will be furnished to RIG/A/SJ and recommendation closure will be requested.

Also, it should be noted that the Mission, regardless of formal PIL issuance, is assuring timely receipt of host country counterpart contribution reports (see comment on recommendation 2.1 below). Furthermore, the 1991 cable guidance cited in the report (p. 7) did not set a deadline by which missions were to establish reporting requirements. Absent such a deadline, USAID/Honduras' strategy for implementing the recommendation was to include this requirement in ProAg Amendments as projects came due for incremental funding. We did this not because we did not take the requirement seriously, but rather because we wished to emphasize to the GOH the importance we attached to it; it has been our experience that the GOH takes funded ProAg Amendments more seriously than it does PILs or unfunded amendments. Please revise the audit observation (p. 7) to reflect our attitude towards receiving host country contribution data as serious.

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As stated in the report, the cable guidance only requires that host governments report *annually* on their contributions, whereas USAID has elected to be stricter by requiring *quarterly* reports. The GOH would be in compliance with Agency policy even if it only submitted one counterpart contribution report per project per year. Our strategy to require more frequent reporting is to assure timely receipt, both in terms of USAID policy and in terms of Mission management information needs. It should be noted, in fact that all of the six referenced projects did, and are meeting the annual reporting policy standard.

## RECOMMENDATION NO. 2

We recommend that USAID/Honduras during Project Implementation Reviews (I) base reviews of counterpart contributions on counterpart reports as of the current reporting period, (2) report all deficiencies related to counterpart contributions including untimely and inadequate reporting; and (3) fully document the discussions on counterpart contributions.

### Mission Comments:

#### Recommendation No. 2.1

The Mission agrees with this recommendation. As of the last semi-annual review (SAR), for the period ending September 1993, the reviews of counterpart contributions were done using current data. Enclosed, please find copies of all counterpart reports used in the last SAR, including reports for those projects awaiting inclusion of the formal reporting requirement in a PIL. Therefore, the Mission hereby requests closure of the recommendation upon issuance of the audit report.

#### Recommendation No. 2.2

The guidance for Project Implementation Reviews or what is now formalized in the LAC Bureau as "Semi-Annual Reviews", (SARs), states that in a section titled "Problems and Delays", USAID missions should discuss only those major problems requiring the attention of senior mission management to resolve, or of which senior management should be aware. In view of this guidance, our response to this recommendation is that we are reporting, and will continue to report, on all *serious* contribution reporting problems. We should not, however, report on less than serious problems. For example, in our judgment the projects reviewed for the SAR cycles ending March 31 and September 30, 1993 included no major counterpart reporting problems requiring senior management attention; therefore, we did not list any such problems in the text of the SARs. Again, please note that all projects reported on host country contributions for the period ending September 1993. The Mission hereby commits to report any serious deficiencies related to counterpart contributions as part of SARs submissions, in the "Problems and Delays" section. Therefore, the Mission hereby requests closure of the recommendation upon issuance of the audit report.

### Recommendation No. 2.3

The Mission agrees with the recommendation. The Office of Development Finance prepares and distributes to all involved Offices a memorandum summarizing decisions reached at each SAR meeting. If there are any major problems related to counterpart contributions disclosed during SAR reviews, they will be documented in this manner. In addition, we have amended the Mission Order (see copy attached) to document how we will report on problems related to counterpart contributions. Therefore, the Mission hereby requests closure of the recommendation upon issuance of the audit report.

### RECOMMENDATION NO. 3

**We recommend that USAID/Honduras establish procedures for ensuring that Project Officers certify the reasonableness of reports on the Government of Honduras' contributions only after the test for reliability of reported counterpart has been conducted and documented.**

#### Mission Comments:

The Mission agrees with the general thrust of this recommendation, with a linkage to the Recipient Contracted Audit Program (RCAP) for testing financial data. The project officers are now certifying the report based on their direct knowledge of the project activities. See copies of the certifications enclosed. We plan to have the project officers continue to provide their review and certification of host country counterpart reports as reasonable based on their personal knowledge of project implementation, and goods and services provided. Further, we have confirmed that our RCAP scopes of work include a requirement to audit host country contributions. We believe that both procedures are responsive to the audit recommendation's concern. Moreover, this process parallels the project officers' administrative approval of payment vouchers of appropriated funds, subject to post audit. Therefore we will request closure of this recommendation once an RCAP audit plan has been established with the GOH Controller General.

#### OTHER ISSUES:

#### Computing the Rate of Exchange

We believe that in this section (pp. 15-19), the auditors have misunderstood, and thus drawn inaccurate conclusions about the way in which USAID calculates the exchange rate to be used in calculating the value of the GOH contribution. In fact, the process we follow may be summarized simply: *we calculate that value using the approved exchange rate on the date the GOH incurred its obligation.*<sup>1</sup>

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<sup>1</sup> The procedures for calculating the approved rate are set forth (most recently) in PIL No. 2 for the Structural Adjustment II Program (522-0396), dated January 24, 1994 (see copy attached). With some modifications, the system outlined in this PIL has been in force since January 1993.

Thus, in the first case cited by the report (p. 17), the Small Farmer Organization Strengthening Project (SFOS, 522-0252), the exchange rates used were the "highest not unlawful" in Honduras on the date the GOH incurred its obligations to provide a given tranche of funding: L 2:1 on the date of the original ProAg (September 26, 1985); L 5.3:1 on the date of Amendment No. 7 to that ProAg (May 31, 1991); and L 5.4:1 on the date of Amendment No. 8 (July 13, 1992). Amendments No. 7 and 8 to SFOS both *increased* the required Life of Project (LOP) contribution expected of the GOH. The exchange rate used to calculate the value of the *original* LOP GOH contribution (i.e., that obligated by the original SFOS ProAg) was not changed by these subsequent amendments. In the second case cited by the report (p. 17), the Forestry Development Project (FDP, 522-0246), the exchange rate used was the "highest not unlawful" on the date of the original ProAg (L 2:1 as of December 29, 1987). Because subsequent amendments required no *additional* LOP contribution from the GOH to FDP, there was no need to use any other exchange rate. When we amend FDP later this year to, among other things, require an additional, lempira-denominated counterpart contribution from the GOH, we will calculate the dollar value of that additional contribution using the approved exchange rate on the date we sign the amendment.

A final point on this subject: The report's statement (p. 17) that USAID did not calculate the value of the GOH's real resource contribution to SFOS by first pricing it in local currency and then converting it into dollars is inaccurate. The host country contribution to *all* our projects is calculated in this manner. We work with the GOH to estimate the value of the needed contribution in lempiras, then calculate the dollar value of those lempiras as described in PIL No. 2 for the Structural Adjustment II Program (522-0396).

### Suggested Corrections

The report contains several factual errors and inappropriate statements that we request be modified in the final version. These include the following:

- ◆ On p. 1, the report states that "*A.I.D. has administratively extended [the 25 percent host country contribution] requirement to activities funded by the Economic Support Fund.*" We believe this is inaccurate. Many USAID Missions (e.g. Nicaragua) have ESF-funded projects to which this requirement is not applied.
- ◆ On p. 6, the report states that "*Contrary to A.I.D. procedures, USAID/Honduras did not require the [GOH] to report on its contributions to 6 of the 16 projects active at the time of our audit...*" This is incorrect. Prior to the issuance of Mission Order 590 on July 1, 1992, we tracked GOH contributions through the annual local currency programming exercise. We knew precisely how many lempiras, whether generated from Title I, Title III, or ESF disbursements, were being released to the various projects by the Ministry of Finance and Public Credit (MFPC). In other words, we tracked contributions in advance at the *programming* level rather than after the fact at the *recipient reporting* level, as established by the Mission Order.

- ◆ On p. 9, we question on what objective basis the auditors can determine that *"This problem was due to USAID/Honduras officials not giving priority to enforcing the reporting requirements which had been established for the five projects."* In fact, as explained above, we did give priority to the requirements by phasing them in through funded ProAg Amendments. Moreover, for those projects for which requirements had been established but that were not submitting reports prior to the deadline, DF, the technical office, and CONT personnel all actively encouraged the cognizant Project Implementing Units (PIUs) to improve the timeliness of their reports.
- ◆ Also on p. 9, we take issue with the suggestion that *"USAID/Honduras needs to increase the supervisory oversight of Project Officers to ensure that the well-designed Mission procedures for requiring and obtaining reports on [GOH] contributions are fully implemented."* We question the objective basis on which the auditors could have determined that there was insufficient supervision; moreover, as we have stressed above, all levels of the Mission were and are actively involved in putting these reporting procedures into practice.
- ◆ On p. 13, the report states that Project Officers told the auditors they were not certifying counterpart contribution reports *"because ODF never provided the Project Officers with any guidance on how the reports should be certified and never requested the project officers to submit the reports."* This statement mixes apples and oranges, and is untrue in any case. DF did provide the Project Officers with a format for reports, and did request that Project Officers provide these reports. The format was set forth in Attachment B to Mission Order 590 of July 1, 1992, which was made available throughout the Mission. That Mission Order also required a certification – a dated and signed statement on the report itself. Because the Mission did not provide a specific format for such certification, project officers were unclear of this requirement. For this reason, our revised Mission Order issued July 16, 1993 (see attached copy) included a standard format to be used by project officers for certifying the reports.



# AGENCY FOR INTERNATIONAL DEVELOPMENT

USAID/HONDURAS

APPENDIX II  
Page 6 of 7

February 28, 1994

Mr. Coinage Gothard  
RIG/A/SJ  
San José, Costa Rica

Dear Mr. Gothard:

This letter is submitted in connection with your draft audit of USAID/Honduras' Controls Over the Honduran Government's Counterpart Contributions as of March 31, 1993.

I have been assigned as Director of USAID/Honduras only since October of 1991. Therefore, my personal knowledge of many of the details of the matters under audit is necessarily limited. While I speak on my own behalf and not on behalf of other USAID/Honduras employees, I have asked appropriate members of my staff to make available to you all records in our possession for the purposes of this audit. They have represented to me that they are aware that USAID/Honduras management is relying on their knowledge and the knowledge of their staffs as the basis for the representations herein. They also have represented to me that they have read this letter and concur with the representation herein.

Based thereon and as of the date of this letter, I confirm to the best of my knowledge and belief as a layman and not as a lawyer, the following representations which were made to you during the course of the audit.

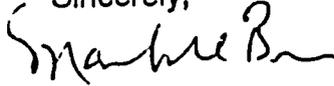
1. For the Honduran Government's Counterpart Contributions, USAID/Honduras is responsible for:
  - ▶ establishing procedures within the Mission to implement an internal control system of this Mission,
  - ▶ establishing procedures within the Mission to insure compliance with applicable U.S. laws and regulations, and
  - ▶ the fairness and accuracy of the accounting and management information maintained by the Mission.

Among other techniques, we rely extensively on the audit reports of contracted private independent audit firms, USAID's Office of the Inspector General and GAO as an element of internal control, to determine compliance with applicable laws, policies and regulations, and to ensure the accuracy of accounting and management information.

- 2 -

2. USAID/Honduras has allowed RIG auditors access to all financial and management information associated with the Honduran Government's Counterpart Contributions which are maintained by this Mission.
3. USAID/Honduras has not deliberately withheld from RIG auditors information concerning:
  - ▶ material irregularities involving management or employees who have roles in the internal control structure,
  - ▶ material irregularities involving any other organizations that could affect the Honduran Government's Counterpart Contributions, or
  - ▶ communications from any other organization concerning material noncompliance with or deficiencies in the Honduran Government's Counterpart Contributions.
4. There are no material instances where financial or management information of USAID/Honduras relating to the matters under audit has not been properly and accurately recorded and reported, except as noted in the audit report.
5. Except as noted in the audit report, there have been no instances of noncompliance with USAID required policies and procedures for the Honduran Government's Counterpart Contributions.
6. USAID/Honduras has not deliberately withheld any material information concerning violations or possible violations of U.S. laws or regulations pertinent to the matters being audited.
7. USAID/Honduras has complied with its obligations under all contractual agreements insofar as such compliance would materially affect the Honduran Government's Counterpart Contributions.
8. No events have occurred subsequent to the period under audit that would affect the above representations.

I request that this representation letter be made a part of the official Mission comments on the report and be published as an annex thereto.

Sincerely,  
  
Marshall D. Brown  
Mission Director

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