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GAO

Report to the Chairman, Subcommittee on Western Hemisphere Affairs, Committee on Foreign Affairs House of Representatives

December 1986

CENTRAL AMERICA

Problems in Controlling Funds for the Nicaraguan Democratic Resistance

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GAO/NSIAD-87-35

GAO

United States
General Accounting Office
Washington, D.C. 20548

National Security and
International Affairs Division

B-225024

December 5, 1986

The Honorable Michael D. Barnes
Chairman, Subcommittee on Western
Hemisphere Affairs
Committee on Foreign Affairs
House of Representatives

Dear Mr. Chairman:

This report responds to your October 15, 1985, request that we monitor compliance with the legislation that made $27 million available for humanitarian assistance to the Nicaraguan democratic resistance. A key provision of that law requires the President to establish appropriate procedures to ensure that program funds are not used for other than humanitarian purposes.

The assistance program was administered by the State Department's Nicaraguan Humanitarian Assistance Office (NHAO). The NHAO control procedures we reviewed were not sufficient to ensure that the funds were used as intended by law. According to NHAO, the governments of certain Central American countries did not permit NHAO to set up operations in the region as it originally intended. Instead of its own controls, NHAO said it relied primarily on intelligence reports to provide information on purchases and deliveries. According to NHAO officials, the intelligence reports were initially sporadic, but became increasingly frequent and detailed. We were denied access to these reports, and thus cannot comment on their comprehensiveness or adequacy.

We recognize the constraints on NHAO's control over expenditures and deliveries in the region, given its inability to operate openly there. The State Department maintains that intelligence reports show that the goods and services purchased under this program have reached the intended beneficiaries, but the Department did not provide us evidence to support this assertion. As far as we could determine, most transactions could not be fully tracked or verified. In response to allegations, NHAO investigated some transactions and confirmed two cases of misuse of funds. Due to the absence of verifiable controls and our inability to do audit work in the region, we cannot say whether these cases are indicative of a significant problem or isolated cases as the State Department maintains. These matters are summarized below and discussed in detail in appendix I.

NHAO Could Not Verify Most Receipts

As of September 4, 1986, NHAO had disbursed $26.8 million. NHAO authorized these payments based on invoices, receipts, and other documentation, indicating that goods and services had been provided by U.S. and regional suppliers. According to the receipts, about 64 percent ($17.0 million) was spent on goods and services purchased in the region; $9.8 million was paid to U.S. suppliers. The receipts indicated that the bulk of the funds (about $24 million) went for food, pharmaceuticals, transportation, and clothing.

NHAO exercised considerable control over funds expended in the United States by reviewing invoices, in many instances verifying the legitimacy of suppliers, checking reasonableness of prices, and at times verifying the delivery of purchased supplies at transshipment warehouses in the United States. We were generally satisfied with the controls over NHAO expenditures in the United States; however, it was a much different story for the funds spent in the region. NHAO could not set up operations there as it originally intended because of sensitive political situations in certain countries in the region. Thus it could not exercise sufficient financial and programmatic controls beyond U.S. borders. For example, NHAO could not routinely assess the validity of the receipts, was unable to check out many suppliers, and had difficulty establishing reasonableness of prices. NHAO also had no control over the use of excess funds generated through currency transactions. Moreover, it generally could not verify that the goods and services, wherever purchased, were not diverted.

In response to press allegations and intelligence reports, NHAO visited the region in June 1986 and found that it had paid about $80,000 based on false receipts. Some funds were used to purchase ammunition and grenades. NHAO has recovered about $25,000, and has taken action to offset the remaining funds against subsequent purchases. As you know, the Federal Bureau of Investigation is examining these and other allegations.

Payments Made to U.S. Bank Accounts

Efforts to track program funds paid to regional suppliers were further complicated because payments were not always made directly to them. Instead, about $6 million was paid to U.S. bank accounts of several brokers authorized by the regional suppliers to act as their agents. NHAO did not require the account owners to demonstrate that payments were made from those accounts to the suppliers of record. In fact, NHAO has

stated that payments into the U.S. bank accounts completed the transaction between NHAO and the suppliers, and that it had no authority to trace funds further.

Our examination of the bank account records, which were subpoenaed by your Subcommittee, raised a number of questions about the disposition of funds in the accounts. For example, we were able to trace only a small amount of funds to specific regional suppliers, and large payments were made to the armed forces of one country. As discussed in appendix I, the Department provided explanations for the account activity but did not furnish sufficient documentary support for most of the explanations.

Agency Comments

In commenting on our draft report, the Department of State took exception to our position that NHAO did not establish adequate control procedures as required by law. The Department believes that the Congress intended only that the controls be appropriate under the extraordinary circumstances of the program, and it does not believe that it is either reasonable or appropriate to apply conventional government auditing standards to the operations of NHAO. According to the Department, aid to an insurgency—by definition an unconventional operation—must of necessity operate under less than ideal auditing controls.

While we recognize the constraints on NHAO in managing and controlling program expenditures, we do not find evidence that the Congress intended that control procedures be disregarded because of these constraints. On the contrary, the legislative history of the statute indicates that the requirements for controlling the use of the funds were adopted in response to concerns that the unconventional circumstances of the program would lead to a lack of accountability. The procedures that we reviewed did not meet those concerns.

The Department made other comments, which were used as appropriate to make revisions to the report. The Department's comments are included in full as appendix II to this report.

Objectives, Scope, and Methodology

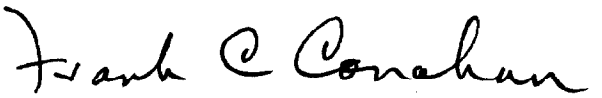
This review was conducted to monitor the expenditure of the $27 million in assistance to determine if only humanitarian assistance was provided and if the assistance was reaching the intended beneficiaries. We performed our review at the NHAO office in Rosslyn, Virginia, at warehouses in the United States, and at United Nicaraguan Opposition (UNO)

offices in Miami, Florida. We examined receipts and invoices submitted to NHAO by suppliers of goods and services, inspected goods awaiting shipment from the United States to Central America, and discussed program operations with NHAO and UNO officials. We also reviewed U.S. bank records for those accounts receiving payments for goods and services purchased in the region. We reported on the preliminary results of our work in testimony before your Subcommittee on three occasions (March 5, May 8, and June 11, 1986).

Because State would not permit us to travel to the region, we were not able to trace disbursements or delivery of goods outside the United States. State Department officials stated that audit work in the region would hamper implementation of the assistance program and that they would not approve our travel to Central America for this purpose. Our work in the United States was conducted in accordance with generally accepted government auditing standards.

We are sending copies of this report to the Chairmen, House Committee on Foreign Affairs, Senate Committee on Foreign Relations, the House and Senate Appropriations Committees, and House Government Operations and Senate Governmental Affairs Committees; the Secretary of State; and other interested parties.

Sincerely yours,



Frank C. Conahan
Assistant Comptroller General

Humanitarian Aid to the Nicaraguan Resistance

The International Security and Development Cooperation Act of 1985, which authorized $27 million for humanitarian assistance to the Nicaraguan democratic resistance, stipulated that:

"The President shall establish appropriate procedures to ensure that any humanitarian assistance provided by the United States Government to the Nicaraguan democratic resistance is used only for the intended purpose and is not diverted (through barter, exchange, or any other means) for acquisition of weapons, weapons systems, ammunition, or other equipment, vehicles, or material which can be used to inflict serious bodily harm or death.

"As used in this subsection, the term 'humanitarian assistance' means the provision of food, clothing, medicine, and other humanitarian assistance, and it does not include the provision of weapons, weapons systems, ammunition, or other equipment, vehicles, or material which can be used to inflict serious bodily harm or death."

On August 29, 1985, the President established the Nicaraguan Humanitarian Assistance Office (NHAO) within the Department of State to administer the assistance program and to establish appropriate controls over the expenditures as required by law. NHAO devised a system under which goods and services were purchased through suppliers in both the United States and Central America. Initially, NHAO planned to maintain offices in the United States and Central America to manage the program, but according to NHAO officials, the governments in the Central American countries involved did not permit the establishment of such offices in their countries. As a result, NHAO could not establish management controls outside the United States.

NHAO officials recognized the problems which might result from the absence of management controls in the region and took steps to obtain information about program activities outside the United States. This included obtaining reports on program activities from intelligence sources in the region, as well as NHAO officials conducting several inspection trips to Central America.

NHAO Could Not Verify Most Receipts

Because NHAO had limited oversight capability for purchases in the region, it made many payments to suppliers in the region based on receipts that it could not verify. According to receipts and invoices submitted to NHAO by the United Nicaraguan Opposition (UNO)—an umbrella organization representing the various resistance forces—the following goods and services were purchased.

Table I.1: Summary of NHAO Disbursements for Goods and Services
(As of September 4, 1986)

Type	In region	In U.S.	Total
Food and Consumables	$10,965,085	$0	**$10,965,085**
Medical/Pharmaceuticals	1,453,680	4,028,124	**5,481,804**
Clothing	1,205,700	2,279,194	**3,484,894**
Equipment	769,527	1,816,688	**2,586,215**
Transportation	2,417,692	1,371,389	**3,789,081**
Administrative Costs (includes Human Rights Program)	206,157	278,676	**484,833**
Total	**$17,017,841**	**$9,774,071**	**$26,791,912**
Percent	64	36	**100**

Source: Compilation of NHAO/State Department documents.

As can be seen from table I.1, a substantial portion (64 percent) of the goods was purchased in the Central American region. NHAO officials attributed this situation to the difficulties encountered in delivering U.S.-purchased items to the resistance forces. NHAO had assumed that except for food and other consumables, most goods would be purchased from U.S. suppliers, not only because NHAO's control would be greater but also because the quality of certain U.S. goods was higher and U.S. prices would be lower. However, due to the diplomatic sensitivities of the countries involved, deliveries of goods purchased in the United States (mostly pharmaceuticals, boots, and field gear) were delayed and the goods were temporarily stored in U.S. warehouses, principally in New Orleans. This caused more money to be spent in the region for items such as uniforms, boots, and pharmaceuticals than might otherwise have been the case.

Verification of U.S. Purchases

For purchases from U.S. suppliers, we are satisfied with the considerable controls that NHAO exercised over disposition of the funds. NHAO established procedures for administering procurements and making payments, which allowed it to control and oversee the types of goods and services being purchased and the prices paid. It relied principally on the UNO to determine the types and quantities of goods and services to be purchased.

UNO submitted pro forma invoices prepared by proposed U.S. suppliers identifying the goods or services to be purchased and the amount to be paid. NHAO reviewed these invoices to determine if the items or services were consistent with program objectives and that the stated price appeared to be reasonable. In many cases, NHAO obtained Dunn and Bradstreet reports on proposed suppliers to ensure that the companies

were legitimate. Furthermore, NHAO said that it often checked with other suppliers of similar items and with DOD procurement officials to verify the reasonableness of prices quoted. If the review was satisfactory, NHAO provided the supplier a letter of commitment for the funds to be paid upon receipt of the goods by UNO. When UNO sent NHAO confirmation of delivery of the goods, NHAO issued payment vouchers, and the Treasury sent checks directly to the suppliers. NHAO also inspected some of the supplies stored in U.S. warehouses awaiting shipment to the region to ensure that approved items had been delivered.

Inability to Verify Non-U.S. Purchases

For purchases in Central America, NHAO issued payment for goods and services only after receiving a delivery receipt from the supplier, submitted through UNO, stating the type and quantity of goods purchased and the amount of payment due. The documents submitted to NHAO included statements by UNO officials that the goods or services indicated on the receipts had been received. NHAO reviewed these receipts to ensure that the items on the receipts were allowable under the law and, if so, authorized payment to the account in the United States designated by the supplier organization. However, from its offices in Rosslyn, Virginia, NHAO could not assess the validity of the regional receipts, was unable to check out many suppliers, and had difficulty establishing reasonableness of prices. In response to press allegations and intelligence reports, NHAO visited the region in June 1986 and found two instances where false receipts had been submitted for payment.

In one instance, NHAO authorized payment of $25,870 in January 1986 based on receipts for food, clothing, and sundries. NHAO found that no goods had been furnished by the alleged supplier. When questioned about this transaction, UNO officials explained that the funds were used to purchase supplies of uniforms, ammunition, and grenades. NHAO has recovered the entire sum, which it will authorize to purchase approved goods.

In another case, NHAO authorized payment of $56,745, purportedly for clothing. In following up on press allegations, NHAO found during its investigation that an official of one of the resistance groups had submitted the false receipt to obtain advance funds. NHAO took action to offset this payment against subsequent UNO purchases.

Limited Ability to Verify Delivery and Use of Items

NHAO was limited in being able to verify the final delivery of items and their end-use in the region, whether purchased in or out of the United States. NHAO officials said that the lack of a regional office forced them to rely on intelligence reports and several inspection trips by NHAO officials. According to NHAO, the intelligence reports were initially sporadic and did not cover all transactions or verify quantities of specific deliveries, but they improved over time. Trip reports by one staff member, who visited the region in February, April, and June 1986, state that he was able to examine UNO's accounting procedures, visit some facilities and warehouses, meet with some suppliers, and personally observe the presence of various NHAO supplied goods.

The State Department maintains that the intelligence reports show that goods purchased under this program have been delivered to the resistance. According to Department officials, State could not provide the intelligence reports to us because they had been prepared by another agency, which subsequently denied us access.

Payments Made to U.S. Bank Accounts

NHAO adopted a policy of making payments to designated U.S. bank accounts instead of to suppliers' accounts in the region because of political sensitivities in the region and potential security problems for suppliers. Payments were made either to the U.S. bank accounts of the suppliers or to individuals having management positions in the supplier organization, or to the U.S. accounts of brokers designated by the suppliers to receive payment. Payments to broker accounts totalled about $6 million of the $17 million spent for purchases in the region.

Use of Funds Generated Through Currency Exchanges

According to the State Department, NHAO used the in-country official exchange rate in computing payments to regional suppliers based on U.S. Treasury Department regulations and advice of Treasury officials. Treasury regulations require that currency exchange transactions for official expenditures be computed at the prevailing rate which, according to State officials, was equal to the in-country official rate. However, since these payments were made in U.S. dollars to U.S. bank accounts, it is not clear whether the use of the in-country official exchange rate was required by law.

After funds were deposited in U.S. bank accounts, currency was exchanged at rates higher than the in-country official exchange rate—up to 31 percent higher. For example, a State Department analysis of one broker account to which NHAO had paid about $3 million showed

that the broker had acquired excess funds by exchanging the dollars for foreign currency at higher than the in-country official rate. These excess funds totalled about $940,000 as computed at the official rate (or about $717,000 computed at the higher rate). According to NHAO officials, the excess funds were paid to UNO, which used the funds to purchase humanitarian assistance. UNO officials provided NHAO with receipts for non-lethal equipment and regional air transportation services that they said were purchased with the funds. However, NHAO did not verify these transactions.

Similarly, funds in another U.S. account were also traded for foreign currencies at higher than the official rate. According to the State Department these transactions netted this account about 5 percent above the official exchange rate, or about $61,000. NHAO did not verify how the additional funds were used.

Questions Raised on Disposition of Funds

NHAO did not trace funds paid from the broker accounts and did not require that brokers demonstrate payments to the suppliers of record. According to NHAO officials, payments into the U.S. bank accounts complete the transaction between NHAO and the suppliers, and NHAO has no authority to trace funds further.

NHAO furnished us evidence to show that some suppliers were paid. There were statements from 20 of the 55 suppliers verifying payments of about $8.4 million out of the total $17 million reported as spent on goods and services purchased in the region. However, these statements showed that four suppliers received a total of about $600,000 less than the amount on NHAO vouchers and that one supplier received $107,000 more than the amount shown on NHAO vouchers. The value of such statements as a control is questionable since NHAO officials could not explain these discrepancies during the time of our review. They did reexamine the statements following receipt of our draft report and informed us that the differences were due to poor bookkeeping by the suppliers, disparities in time frames, and misinterpretations of what the statements were intended to include. These explanations cannot be verified.

Our examination of the bank records raised questions about the disposition of funds in these accounts. For example, we were able to identify payments of only a small amount of funds to specific regional suppliers, and we found that payments had been made to the armed forces of one country. The Department of State provided explanations for the account

activity, but did not furnish supporting evidence for most of the explanations.

Regarding payments to the Central American region, we found that the brokers seldom disbursed funds from these bank accounts to the regional suppliers that they represented. For example, of the total amount of about $3 million deposited to one broker account as of May 10, 1986, only $150,000 could be traced to Central America, none of which was paid to suppliers shown on the invoices and receipts received by NHAO. Instead, most of the funds were transferred from the account to other bank accounts in the United States and other countries. Thus, from the broker's bank records, we could not determine whether the funds reached the intended suppliers in the region.

According to State Department officials, a broker may not immediately disburse funds from his account to the region in order to make advantageous currency exchanges. In an July 24, 1986, letter to the Senate Foreign Relations Committee, State Department officials stated that

> "...an entrepreneur will retain those funds to make future dollar purchases, rather than convert them back and forth, an unnecessary transaction on which he would lose money. Or, if an entrepreneur can sell hard currency abroad at an advantageous rate (this is perfectly legal under U.S. and Central American laws), then he certainly will do so."

Payments to the Armed Forces

Our examination of the bank accounts also showed large payments to the armed forces of one country in the region. For one account, Treasury issued a payment of $243,750 for uniforms, based on invoices and receipts from a wood exporting supplier. After this payment, checks were issued from this account to the armed forces of a country in the region in the amounts of $113,750 and $130,000, totalling $243,750.

In another account, Treasury made a deposit of $896,122 on November 16, 1985, based on receipts for food and transportation, and on November 18, 1985, the supplier made a payment of $742,939 to the armed forces of a country in the region. Again, a Treasury deposit of $411,974 for food and consumables on January 8, 1986, was followed by a payment of $450,000 to the armed forces on January 10, 1986.

Without the Treasury deposits, these accounts would not have had sufficient funds to cover the amounts of the subsequent payments to the

armed forces. We therefore raised questions as to the basis for these transactions.

According to the State Department, payments to the armed forces of a country in the region were legitimate and reasonable transactions. In the case of the $243,750 payment from one account, NHAO officials explained that the uniforms were actually provided by the country's military. The supplier company listed on the invoice and receipt, which NHAO said is owned by military officers, acted as a middleman. Payments were subsequently made to the military from the U.S. bank account to which NHAO authorized payment. NHAO officials stated that this type of transaction was used to mask the military's assistance to the resistance. NHAO did not provide us with documentary evidence to support this explanation of the transaction.

According to NHAO officials, the other two payments to the armed forces, totalling about $1.2 million, represented (1) a loan repayment of $742,939 from the supplier to repay money borrowed from the armed forces and (2) a capital transfer in which the supplier paid $450,000 to the armed forces account in the Central Bank and received local currency in exchange. Regarding the loan repayment, NHAO officials again did not provide evidence supporting their explanation. In regard to the capital transfer, they showed us a check covering a local currency payment from the armed forces account to a party who NHAO said represented the supplier.

In its comments, the State Department contends that it provided documents supporting its explanations of the payments to the armed forces. However, the Department only provided us documents supporting its explanation of the $450,000 capital transfer.

Comments From the Department of State

United States Department of State

Washington, D.C. 20520

October 23, 1986

Dear Mr. Conahan:

I am replying to your letter of September 23, 1986 to the Secretary which forwarded copies of the draft report entitled "Humanitarian Aid to the Nicaraguan Resistance" under GAO assignment code 463742.

The enclosed comments on this report were prepared by the Nicaraguan Humanitarian Assistance Office.

We appreciate having had the opportunity to review and comment on the draft report.

Sincerely,

Roger B. Feldman

Roger B. Feldman

Enclosure:
As stated.

Mr. Frank C. Conahan,
Assistant Comptroller General,
National Security and
International Affairs Division,
U.S. General Accounting Office,
Washington, D.C. 20548

GAO DRAFT REPORT: HUMANITARIAN AID TO THE NICARAGUAN RESISTANCE

Overall comment

This GAO Draft Report addresses the narrow issue of the adequacy of conventional auditing and control procedures utilized in the disbursement of $27 million in humanitarian assistance to the Nicaraguan democratic resistance. As its point of reference, the GAO cites section 722(g)(4) of the International Security and Development Cooperation Act of 1985 that called for establishment of "appropriate procedures" to ensure that any U.S. furnished assistance would be used only for the intended purpose and not diverted for acquisition of lethal equipment or supplies.

At the outset, we must note a fundamental difference with the GAO over the standard to be applied under this law. GAO places the stress on the need to "ensure" against any diversion, and reasons that only procedures which could provide absolute assurance can be considered to be "appropriate." We believe, on the other hand, that Congress intended that procedures be adopted which would be "appropriate" in the extraordinary circumstances of this program, so as to provide a degree of confidence that a prudent administrator could regard as reasonable assurance in these extraordinary circumstances. Put differently, the fundamental issue is that the GAO assumes that Congress imposed an admittedly unreasonable standard and then criticizes program implementation when measured against that unreasonable standard. NHAO implemented the program based on the assumption that the statute should be construed so as to ascribe to Congress an intention of reasonableness. In this regard, we believe that the legislative mandate "appropriate procedure" should be read in the context of the entire statute and the underlying factual and policy context, and not in isolation.

The language of the Act and -- more dramatically -- of the related Conference Report reflected a sense of urgency and grave concern on the part of the Congress with respect to current developments within Nicaragua and the fate of the democratic resistance. This concern was well founded: in September 1985, when the Administration began to discharge the mandate to provide numanitarian assistance, the resistance movement was in desperate need of the food, clothing, and medical supplies authorized by the Congress. Thus, the overriding priority was to get the aid moving.

This was not an easy task. As the members of Congress well understood -- through extensive dialogue with the Administration in July and August 1985, when the terms and

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modalities of the assistance program were being discussed -- the combination of legislative constraints, political sensitivities in Central America, and potential threats to the personal security of anyone directly involved, placed unprecedented obstacles in the path of the stated goal, that is, getting aid through to the resistance. For example:

-- Central American facilities and personnel under the control of the United States Government were denied to the administering agency (NHAO) for purposes of procurement, transshipment and logistic support;

-- NHAO was not permitted (due to local political sensitivities) to have a physical presence in Central America, nor to maintain local bank accounts through which suppliers could be paid directly in their own currency;

-- Delivery of NHAO supplies by air from the United States was subject to control (and even to suspension, as later experience was to demonstrate) by political and military authorities in the region.

In short, NHAO was obliged to devise new and somewhat unconventional procedures if there was to be any hope of achieving the legislative objective in a timely and effective fashion.

NHAO was by no means unmindful of the need to strive for the highest levels of accountability possible under the circumstances. To that end, NHAO sought and received the advice and assistance of the Inspector General of the State Department to devise a system of internal controls for safeguarding the appropriated funds. NHAO also consulted with the auditing staff of the House Permanent Select Committee on Intelligence, the Agency for International Development, and other federal agencies.

Given the operating environment outlined above, the Department of State does not believe it is either reasonable or appropriate to apply conventional government auditing standards to the operations of NHAO -- aid to an insurgency, by definition an unconventional operation, must of necessity operate under less than ideal auditing controls. But the GAO has applied precisely such standards to this program. Perhaps it could not avoid doing so, under the terms of the request from Congress, but the end product is highly misleading. The GAO assessment focuses exclusively on procedural shortcomings, as seen from the GAO's limited purview, and completely ignores what NHAO was able to achieve in getting aid through to the democratic resistance.

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It is true that the evidence for that achievement lies well beyond the fiscal data which preoccupied the GAO. The GAO states it was denied access to intelligence reports that were NHAO's best source for verification of purchases and deliveries. However, those reports were fully available to the appropriate committees of the Congress.

Specific comments

Now on p. 7.

1. On page 8, in the final paragraph under the subheading "Inability to Verify Non-U.S. Purchases", GAO refers to an NHAO investigation that was still in progress as their report was being written. The issue concerned false invoicing and possible non-delivery of contracted supplies.

That investigation has been concluded to NHAO's satisfaction, inasmuch as NHAO is now in receipt of the following documentation:

a. A written explanation from the supplier giving precise dates, amounts and purposes of advance payments from the resistance officials to the supplier.

b. Copies of supplier invoices showing dates and quantities of supplies provided to the resistance.

c. Copies of internal resistance documents that record the issuing of specific quantities of supplies, with dates and names of the military commanders to whom the supplies were consigned.

These documents are available for examination by GAO.

It should be noted that NHAO may have been partly responsible for the problem's having arisen in the first place, due to its demands for urgent delivery and some misunderstanding between NHAO and this element of the resistance concerning acceptable procurement practices.

Now on p. 8.

2. On pages 8 and 9, under the subheading "Inability to Verify Delivery and Use of Items", GAO has chosen to apply a severe and rigid standard of verification that cannot in practical terms be applied to an operation of this kind. However, NHAO made every effort to verify that supplies purchased with the funds it administered were delivered to those for whom they were intended. GAO states: "NHAO was generally not able to verify the final delivery of any of the items and their end-use in the region, whether purchased in or out of the United States." (Underscoring added.) That conclusion flies in the face of several facts:

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a. The NHAO Director and two logistics officers made several trips to the region, during which they were able to inspect UNO records in detail, visit rear-area warehouses and forward bases, and personally observe the physical presence of various kinds of supplies (food, clothing, pharmaceuticals, vehicles, equipment, etc.) which could be specifically identified as having been purchased with NHAO funds. In each case, the NHAO officer wrote a trip report detailing his findings and observations, and these reports were made available to GAO. In addition, GAO officials interviewed the NHAO personnel at length.

b. The intelligence reports provide detailed accounts of deliveries to the forward areas, including types and quantities of supplies, thus verifying the movement of supplies from rear-area warehouses to the front with no apparent diversion.

Now on p. 8.

3. On page 10, under the subheading "Use of funds generated through currency exchanges", GAO states "it is not clear to us whether the use of the official exchange rate was required by law." NHAO based its decision to use the official exchange rate on U.S. Treasury Department regulations and advice from Treasury officials who administer those regulations. (See U.S. Treasury Fiscal Manual, Volume I, Part 6, Chapter 8000, Sections 8070.15 and 8070.30.)

Now on pp. 9 and 10.

4. On page 11, under the subheading "Questions Raised on Disposition of Funds", GAO suggests that there are discrepancies between NHAO records and suppliers' written statements (submitted to NHAO) concerning amounts they had been paid.

On receipt of the GAO Draft Report, NHAO undertook a re-examination of the statements in question. In NHAO's view, the apparent discrepancies are the result of three factors:

a. Poor bookkeeping by the suppliers (who have consistently agreed with NHAO when their errors have been pointed out to them);

b. Disparities in the time frame under review, whereby suppliers' statements lag behind NHAO records of payment; and

c. Misinterpretation by NHAO and GAO as to what the suppliers' statements were intended to include.

NHAO's re-examination of this problem resulted -- according to NHAO's analysis -- in a reduction of discrepancies from GAO's figure of $707,000 (actually $731,134) to $9,178. This last figure relates to two suppliers whom NHAO has not yet been able to contact directly. NHAO is of course prepared to share this recent analysis with GAO.

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Now on pp. 10 and 11.

5. On pages 13 and 14, under the subheading "Payments to the Armed Forces", GAO repeats NHAO's explanations concerning several transactions but suggests that the documentary evidence to support these explanations was inadequate.

The evidence which NHAO provided included photo-copies of cancelled checks, bank statements matching by date and amount the figures in question, and a memorandum from the military forces relating step-by-step the various transactions, with photocopies of substantiating documents attached. It is difficult to surmise what further documentation might reasonably be required.

Conclusion

Contrary to the draft report, we believe that NHAO established adequate procedures as required by law, and that there was in fact no significant diversion of U.S. assistance provided under this program from authorized purposes.

R. W. Duemling

Robert W. Duemling
Director
Nicaraguan Humanitarian
Assistance Office

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