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REPORT TO THE CONGRESS

Social Development Activities
In Latin America
Promoted By
The Inter-American Foundation
Fiscal Year 1972 B-135075

B-135075

*BY THE COMPTROLLER GENERAL
OF THE UNITED STATES*

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FILE COPY - COMP. GEN.

JULY 23, 1973



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D C 20548

B-135075

To the President of the Senate and the
a Speaker of the House of Representatives

This is our report on the activities of the Inter-American Foundation during the fiscal year ended June 30, 1972. It complies with requirements of the Government Corporation Control Act (31 U.S.C. 841).

This is our second report on the Foundation's activities. Our first report (B-135075, Feb. 29, 1972) covered the Foundation's operations during the fiscal year ended June 30, 1971--a period in which only administrative activities occurred. At that time, the name of the Foundation was the Inter-American Social Development Institute.

We are sending copies of this report to the Director, Office of Management and Budget, the Administrator, Agency for International Development, and the President, Inter-American Foundation.

A handwritten signature in cursive script that reads "James B. Stacks".

Comptroller General
of the United States

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ABBREVIATIONS

AID	Agency for International Development
GAO	General Accounting Office
IAF	Inter-American Foundation
PADF	Pan American Development Foundation

D I G E S T

WHY THE REVIEW WAS MADE

This review was required by the Government Corporation Control Act. The report provides information about first year activities of the Inter-American Foundation (IAF) and includes IAF's financial statements and GAO's opinion of them.

IAF's intended role

The Congress created IAF to rectify social development shortcomings in prior U S assistance efforts in Latin America. The intent was that IAF would provide assistance primarily through private channels rather than through governmental channels, meaning that the principal participants in the development effort would be United States and Latin American private groups.

FINDINGS AND CONCLUSIONS

IAF provided assistance to Latin American private groups, but none to United States private groups. The main feature of IAF's approach is to rely solely on Latin American groups to conceive and implement development efforts.

Another feature of IAF's approach is to provide assistance on easy terms. IAF accomplished this primarily by providing all the

assistance in the form of grants, most of which supported projects or types of projects previously promoted with U S loan assistance. IAF also softened the prior practice of requiring the Latin American recipient to obtain local matching funds.

GAO believes these two features of IAF's approach are potentially detrimental to the U S social development program in Latin America. They introduce the chance that beneficial participation by others will be excluded, and they may be setting the stage for losing opportunities to stimulate Latin American effort.

Opinion of financial statements

In GAO's opinion, the financial statements included in this report present fairly IAF's financial position as of June 30, 1972, and the results of its operations and the source and application of its funds for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year and with applicable Federal laws.

RECOMMENDATION

To provide the maximum U S help to Latin American development efforts, GAO recommends that IAF broaden its

approach The approach should include the providing of assistance through private U S organizations and the use of a greater variety of assistance terms specifically tailored to development objectives

AGENCY ACTIONS AND UNRESOLVED ISSUES

IAF is opposed to changing its approach IAF apparently perceives its intended role to be of a limited nature--that of promoting Latin American experimentation--and

believes that its approach is appropriate for that role GAO believes that IAF was established to do more, that much of IAF's assistance actually went for nonexperimental projects, and that IAF should therefore reconsider the propriety of its approach

MATTERS FOR CONSIDERATION BY THE CONGRESS

The Congress may wish to consider whether IAF's intended role is adequately defined and understood

CHAPTER 1

INTRODUCTION

The Inter-American Foundation (IAF), a U S Government corporation, completed its first full fiscal year of operations on June 30, 1972. IAF was established during fiscal year 1970 pursuant to part IV of the Foreign Assistance Act of 1969 (83 Stat 821-824), but it was not operational that year. Operations commenced with the appointment of a board of directors in September and October 1970, followed by the appointment of a staff of officers beginning in March 1971. Until February 1972, IAF operated under the name of the Inter-American Social Development Institute.

IAF was created to provide support for developmental activities designed to achieve improved living conditions for Latin Americans. The Congress expected IAF to rectify shortcomings in prior U S assistance efforts in Latin America by improving the social development aspects of the assistance (See app I.)

Improving the social development aspects of U S assistance has been recognized as requiring the development of innovative approaches. This report discusses the innovations developed by June 30, 1972, and includes a letter from the President of IAF stating IAF's views on this subject (See app II.)

IAF's financial statements and our opinion of them are included in this report beginning on page 16

CHAPTER 2

ASSISTANCE PROGRAM

IAF initiated its assistance program during fiscal year 1972 by making 20 grants of various amounts totaling \$2.8 million. In making these grants, IAF supported projects or types of projects previously promoted with U.S. assistance, but to a large extent it changed the methods of providing the assistance.

The major changes introduced by IAF were

- 1 It adopted a direct-funding practice, i.e., it provided assistance only to private Latin American organizations for projects proposed by them and thereby discontinued a prior practice of providing assistance indirectly through private U.S. organizations
- 2 It directed most of the granted funds to projects or types of projects previously promoted with loans
- 3 It softened the prior practice of requiring the Latin American recipient to obtain local matching funds to qualify for assistance

Of these changes, direct funding is the central feature of IAF's plan for rectifying past shortcomings in U.S. assistance. IAF intends to support only worthwhile projects of capable indigenous organizations, to encourage the submission of Latin American proposals for new initiatives, and to avoid further saturation of Latin America with new organizations and programs conceived by outsiders. IAF recognizes that new and innovative efforts are needed, but it believes that the proposals for new initiatives must come from within Latin America.

The other two changes are intended to complement direct funding by removing impediments to the accomplishment of project objectives. For example, a recipient can afford to be more experimental with assistance that it does not have to

repay and frequently can obtain the assistance more quickly when the requirement for matching funds is eliminated. IAF believes that its relaxation of the assistance terms will encourage innovative efforts and hasten the achievement of immediate benefits.

The manner in which IAF's approach differs from prior practices is illustrated by its support of three Latin American financing institutions, called national development foundations. These foundations had formerly been supported by the Agency for International Development (AID) with loans incorporating a matching-fund requirement, but AID's assistance had been provided indirectly through a private U S organization. The private U S organization had initially conceived the idea of establishing the foundations and had actively promoted their establishment with AID's funds.

No longer eligible to be a direct participant under IAF's program, the private U S organization responded to the new ground rules by helping the foundations submit proposals directly to IAF. As a result IAF granted \$1.6 million directly to the three foundations for expanded versions of projects previously financed with AID loans and also eliminated the matching-fund requirement for two of the three foundations. In this way, IAF assumed the role formerly played by the private U S organization except for proposing new initiatives--a function which IAF believes must now be performed only by the Latin Americans.

There are a reported 800 private U S organizations engaged in social development work in Latin America. The Congress envisioned that these organizations could play a role in IAF's program (see app. I), but as long as IAF continues its direct-funding practice, they will have to make any future contributions independently from IAF.

During fiscal year 1972, IAF rejected 182 proposals for assistance projects in Latin America generally because the organizations submitting the proposals were not indigenous.

The 20 grants made by IAF during the year and their financial status at the end of the year are summarized below

	<u>Number of grants</u>	<u>Amount of grants</u>	<u>Amount disbursed</u>
Business-oriented projects			
National development foundations	3	\$1,597,000	\$175,000
Cooperative business ventures	<u>4</u>	<u>521,000</u>	<u>92,000</u>
Total	<u>7</u>	<u>2,118,000</u>	<u>265,000</u>
Other types of projects			
Community services	11	709,000	174,000
Conferences	<u>2</u>	<u>20,000</u>	<u>13,000</u>
Total	<u>13</u>	<u>729,000</u>	<u>187,000</u>
Total	<u>20</u>	<u>\$2,847,000</u>	<u>\$454,000</u>

The above summary shows that, although IAF had approved grants totaling \$2.8 million, it had disbursed only \$454,000 by June 30, 1972. IAF has followed the practice of disbursing funds to the grantee as they are needed.

IAF intends to evaluate the results achieved with its funds. Because the program is new, however, no evaluations were made by the end of fiscal year 1972.

NATIONAL DEVELOPMENT FOUNDATION PROJECTS

IAF agreed to support projects proposed by the three national development foundations, because it recognized that the projects were desirable and because it believed that the foundations were capable of successfully implementing their proposals. The foundations and their projects stemmed from efforts of the Pan American Development Foundation (PADF), a private U.S. nonprofit corporation engaged in social development work in Latin America.

Prior to IAF's entry, PADF organized and assisted a number of national development foundations throughout Latin America, utilizing U.S. assistance provided by AID. PADF established the foundations as intermediate credit institutions to bring marginal communities into the cash economy of their areas and country. Some of the foundations extended credit directly to community groups, some guaranteed bank loans to such groups, and some provided a combination of the two services. In all cases, however, the ultimate objective was to enable persons to secure commercial credit independently from the foundations.

The three foundations whose projects were supported by IAF are located in El Salvador, Mexico, and the Dominican Republic. The Salvadorean and the Mexican foundations were relatively new, whereas the Dominican foundation, having received substantial U.S. assistance beginning in 1966, was a more established organization.

In recent years, each of these foundations received almost all of its U.S. assistance from PADF in the form of loans. The total amounts received as loans are compared below with IAF's grants during fiscal year 1972.

	PADF loans <u>(note a)</u>	IAF <u>grants</u>
El Salvador	\$ 80,000	\$ 625,800
Mexico	85,000	500,000
Dominican Republic	<u>325,000</u>	<u>471,000</u>
Total	<u>\$490,000</u>	<u>\$1,596,800</u>

^aReported by PADF in its 1972 annual report. Also PADF reported that grants totaling \$541,533 had been provided to the three foundations, almost all of which were provided to the Dominican foundation in 1966.

IAF's grants provided for substantial increases in the foundations' operations, particularly in El Salvador and Mexico. IAF's grant to the Salvadorean foundation was for loans to finance 1,000 low cost housing units for persons with marginal incomes, which represented a significant expansion of the foundation's pilot project previously financed with PADF's assistance. For the Mexican foundation,

whereas PADF's assistance had financed the establishment of one regional service center to help farmers obtain bank loans, IAF's grant was made to increase the foundation's operations to 16 service centers

A similar expansion of beginning efforts was not involved in IAF's grant to the Dominican foundation because this foundation had already made good progress, having a portfolio of 2,398 loans valued at \$1.7 million and benefiting 150,000 persons. For this reason IAF rejected the Dominican foundation's first request for assistance, which indicated that nothing new was being added to its program. IAF later approved the request when the foundation agreed that IAF's grant disbursements would be limited to the amount of credit obtained from commercial banks by former clients of the foundation, based on evidence of such bank loans submitted to IAF.

IAF's grant to the Dominican foundation therefore served as leverage to obtain evidence that the foundation was accomplishing its originally intended objective. The Dominican foundation was free to use the granted funds, however, for the same purposes it had previously used loan funds.

IAF believes that providing grants instead of loans will help make it possible for the foundations to be more effective in its expanded efforts. IAF expects, for example, that the foundations will direct their efforts to the population segment having greater need now that the burden of loan repayments has been lifted. IAF believes also that grants, representing an immediate injection of capital that can be re-used as clients repay their loans, will create greater confidence and investment in the foundations and give them more independence from U.S. organizations.

With regard to IAF's concern about the foundations' degree of dependence on U.S. organizations, PADF had always included a matching-fund requirement in its loans to the foundations, believing that such a requirement was a key factor in stimulating Latin American private sectors to contribute to their foundations. IAF, on the other hand, included a matching-fund requirement only for its grant to the Mexican foundation, although the Salvadorean foundation did agree

to obtain about 30 percent of the total project cost from local sources. IAF apparently believes that it should include a matching fund requirement only when the recipient would have no difficulty in obtaining matching funds. When difficulty is anticipated, IAF eliminates the requirement to prevent it from impeding new and experimental initiatives.

IAF has stated that the foundations' projects illustrate the innovative features inherent in its projects and funding as well as the new direction and emphasis toward social development in Latin America (See app II)

GRANTS TO COOPERATIVE BUSINESS VENTURES

In granting \$521,000 to cooperative business ventures, IAF departed from the traditional practice of providing U S assistance to profit-earning enterprises in the form of loans. IAF's grants consisted of \$424,400 to develop farms for rural members of a labor union in Colombia, \$23,300 to purchase trash-processing equipment for trash collectors in Colombia, \$68,142 to purchase a fishing vessel for a group of fishermen in Peru, and \$5,460 to purchase a truck for small farmers in Brazil.

In each case the objective was to increase the income of the individuals participating in the cooperative business venture. The recipient organizations, which had existed for 2 to 25 years before receiving the grants, had records of marginal success in increasing their members' income.

None of the grant agreements required the recipient organizations to qualify for the grant by obtaining matching funds from other sources. The Colombian farming and trash projects, however, reportedly would be assisted with funds obtained from other sources totaling \$20,000 and \$8,050, respectively.

The agreements covering the Colombian farming and the Brazilian truck projects required recipient organizations to recover funds from their members over a period of years so that they could reuse the funds in similar endeavors. Thus, although the recipient organizations were not required to repay the funds, the ultimate beneficiaries were expected to repay the funds.

For the Colombian trash and the Peruvian fishing projects, the agreements contained no provision for recovering and reusing the funds in other projects.

COMMUNITY SERVICE PROJECTS

During fiscal year 1972, IAF approved grants totaling \$709,000 to support 11 community service projects. Five of the projects were in Brazil, two were in Colombia, and one each was in Honduras, Panama, Trinidad, and Ecuador.

Most of the projects were educational programs designed to achieve social change. They consisted of providing instructions in such diversified subjects as canning and preservation of food, arts and crafts, management methods for small business, social law, health, and mechanics. Generally the education was not intended to be conducted in a formal classroom environment. Projects such as these have traditionally been supported with U S assistance in the form of grants.

For 6 of the 11 projects, the grantee was expected to obtain from other sources at least half of the funds needed for the project. IAF agreed to provide more than half of the funds for three projects and all the funds for two.

Community Service Grants During Fiscal Year 1972

<u>Country</u>	<u>Description of project</u>	<u>Source of funds</u>	
		<u>Foundation</u>	<u>Other</u>
Brazil	Arts and crafts, manpower training	\$ 7,455	\$ -
Brazil	Literacy training	^a 50,650	47,650
Brazil	Agriculture, health, basic education	^a 15,500	15,000
Brazil	Manpower training	39,500	70,000
Brazil	University courses in social law	176,500	218,000
Colombia	Small business management	^a 135,800	113,800
Colombia	Small business management	71,000	-
Honduras	Food preservation and canning	124,850	25,000
Panama	Literacy training	6,800	750
Trinidad	Manpower training	9,500	31,652
Ecuador	Legal services and identification of problems	<u>71,882</u>	<u>4,050</u>
Total		<u>\$709,437</u>	<u>\$525,902</u>

^a IAF agreed to pay half of the project cost plus the entire cost of auditing and evaluating the project.

GRANTS FOR CONFERENCES

IAF approved two grants totaling \$19,700 to cosponsor two conferences. The major expenses covered by the grants were participants' air travel and per diem costs.

The first conference, "Evaluation of Social Development Projects," was held at Bogota during July 1972. IAF granted \$10,000 for this conference to the Inter-American Institute of Agricultural Science. The Institute's reported share of the total cost of the conference was \$5,596.

The second conference, "Caribbean Man and His Environment," was held at Barbados during January 1973. To cosponsor this conference, IAF granted \$9,700 to the Association of Caribbean Universities and Research Institutes. The grantee was to obtain \$17,750 from other sources.

CONCLUSIONS

IAF is attempting to promote social development in Latin America by limiting the U S contribution primarily to money. By providing the money only to Latin American organizations that ask for it, IAF seeks to insure that only Latin Americans will be involved in Latin American efforts. By providing the money on easy terms, IAF seeks to encourage maximum efforts by the Latin Americans. The only nonmonetary inputs needed in this approach are IAF judgments on whether Latin American development proposals deserve support.

We question the advisability of excluding all the private U S organizations. This feature of IAF's approach seems to be based on a conviction that the introduction of U S ideas and services will automatically damage Latin American initiatives, but history does not support that view. The private U S organization that sponsored the three national development foundations whose projects IAF supported, for example, did no apparent damage to Latin American initiatives even though it introduced the idea for the foundations, helped to organize them, and provided such additional services as helping the foundations obtain their funds.

It may be that some private U S organizations have not developed acceptable ways to promote Latin American efforts. By supporting those that have, however, IAF could both expand and coordinate the total U S. contribution. The possibility also exists that private U S. organizations might devise worthwhile new approaches to social development which IAF would be forced to ignore as long as it restricts its support to proposals coming from Latin America.

We question also the desirability of relaxing prior assistance terms without establishing a valid need for the easier terms. IAF justifies its reliance on easy terms by referring to its projects as experimental, and we recognize that clearly required experiments could be sufficient.

justification, but the national development foundation grant agreements contained no requirements that the funds had to be used for new purposes. Instead, the national development foundations were free to use IAF's funds for the same purposes they had previously used AID's funds.

We believe that these two features of IAF's approach are potentially detrimental to the U S social development program in Latin America. They introduce the chance that beneficial participation by others will be excluded, and they may be setting the stage for losing opportunities to stimulate Latin American effort.

RECOMMENDATION

To provide the maximum U S help to Latin American development efforts, we recommend that IAF broaden its approach. The broadened approach should include the providing of assistance through private U S organizations and the use of a greater variety of assistance terms specifically tailored to development objectives.

MATTERS FOR CONSIDERATION BY THE CONGRESS

We have based our recommendation to IAF on the belief that, although IAF was justified in providing assistance for projects or types of projects previously promoted with U S assistance, the Congress expected it to provide such assistance as part of a broader program designed to improve the total U S. social development effort in Latin America. In responding to our views, IAF has indicated that it perceives its intended role in more limited terms.

Our understanding of IAF's intended role was obtained from the legislative history leading to its establishment. That record shows that IAF was expected to assume responsibility for appropriate parts of AID's economic assistance program and was also expected to add a new emphasis and a new direction to social development, including the incorporation of research, innovation, and experimentation. The prevailing view was that a major change would be made in providing social development assistance, namely that the assistance would be provided primarily through private channels rather than through governmental channels. (See app I)

IAF has not interpreted the legislative record as a mandate to participate in the total U.S. social development effort. Instead, IAF apparently perceives its role to be limited to that of a promoter of Latin American experimentation and expects that AID will continue to provide assistance for social development activities not incorporated in IAF's program. IAF has therefore developed an approach which it believes is appropriate for Latin American experimentation and is opposed to changing that approach. (See app II)

The Congress may wish to consider whether IAF's intended role is adequately defined and understood.

CHAPTER 3

ADMINISTRATIVE ACTIVITIES

At the start of fiscal year 1972, IAF was seeking additional personnel to complete its organizational requirements. By the end of the year, it had reached an employment level of 44 officers and employees, an increase of 14 over the level at the beginning of the year. In February 1973, IAF informed us that its personnel strength was over 50 and its short-range goal was 60.

In our first report (B-135075, Feb 29, 1972), we reported that the Board of Directors had approved a plan for implementing the part of the authorizing legislation which required the establishment of a council for consultation purposes. The plan provided for periodic meetings with knowledgeable leaders from Latin American countries to insure that Latin American points of view were taken into account in making policy decisions. The first such meeting was held in June 1971 with leaders from South American countries.

IAF held no similar meetings in fiscal year 1972 but approved two grants to cosponsor conferences scheduled for fiscal year 1973. (See p 11.) Although IAF has not classified these grants as part of the expense of meeting its legal requirement for a council, it appears that the grants were made as a substitute for incurring council expenses.

In fiscal year 1972 the cost of administering IAF's program was about \$1 million. IAF has estimated that administrative costs will be about \$1.5 million for fiscal year 1973 and more for fiscal year 1974.

Although IAF's administrative costs are high in relation to the present size of its program, we understand that IAF plans to expand its program. We have noted that IAF has not yet established a strong controller operation to insure that its activities will be governed by sound financial management practices. GSA, for example, provides all IAF's accounting services. We believe that, before any significant program expansion occurs, an appropriate controller operation should be established within IAF.

CHAPTER 4

OPINION OF FINANCIAL STATEMENTS

We examined the accompanying financial statements (schs. 1 through 3) which were submitted to us by IAF. The statements were prepared from financial records maintained by the General Services Administration. The Administration performs--on a reimbursable basis--payroll, financial reporting, personnel, and all necessary accounting functions for IAF.

Our examination of the statement of financial condition as of June 30, 1972, the related statement of cost of operations and accumulated deficit from operations, and the statement of changes in financial position for the year then ended was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying financial statements present fairly the financial position of the Inter-American Foundation at June 30, 1972, and the results of its operations and the source and application of its funds for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year and with applicable Federal laws.

INTER-AMERICAN FOUNDATION
STATEMENT OF FINANCIAL CONDITION
JUNE 30, 1972

ASSETS

FUND BALANCES,	
Funds with U S Treasury (Note 1)	\$48,156,862
Cashier imprest fund (Note 2)	<u>90</u>
Total	\$48,156,952
OFFICE FURNITURE AND EQUIPMENT	
Initial cost	119,112
Less Allowance for depreciation (Note 3)	<u>2,127</u>
Net unrecovered cost	116,985
OTHER ASSETS	
Amounts due from overpayments	7,238
Employee travel advances	1,557
Prepaid expenses	<u>162</u>
Total	<u>8,957</u>
TOTAL ASSETS	<u>\$48,282,894</u>

LIABILITIES

CURRENT LIABILITIES	
Trade account payable	\$ 14,955
Owed to U S Government agencies	25,413
Accrued salaries & benefits	<u>43,994</u>
Total	\$ 84,362
CASHIER FUNDS ADVANCED BY TREASURY DISBURSING OFFICER (Note 2)	3,000
ACCRUED ANNUAL LEAVE	<u>50,939</u>
TOTAL LIABILITIES	138,301

U S GOVERNMENT INVESTMENT

INITIAL INVESTMENT	50,000,000
ACCUMULATED DEFICIT FROM OPERATIONS (Sch 2)	<u>1,855,407</u>
NET U S GOVERNMENT INVESTMENT (Note 4)	<u>48,144,593</u>
TOTAL LIABILITIES AND U S GOVERNMENT INVESTMENT	<u>\$48,282,894</u>

The notes on page 20 are an integral part of this statement

SCHEDULE 2

INTER-AMERICAN FOUNDATION

COST OF OPERATIONS AND ACCUMULATED DEFICIT

FROM OPERATIONS FOR THE FISCAL YEAR ENDED JUNE 30, 1972

SOCIAL DEVELOPMENT GRANTS

Undisbursed balance of grants, June 30, 1971	\$ -	
Grants approved in fiscal year 1972	<u>2,847,239</u>	
Total	2,847,239	
Undisbursed balance of grants, June 30, 1972	<u>2,393,229</u>	
Grant disbursements		\$ 454,010

ADMINISTRATIVE EXPENSES

Employee salaries and benefits	755,683	
Employee travel and transportation	86,680	
Annual leave expense (Note 5)	32,730	
Printing expenses	1,490	
Rental of office space & equipment	103,845	
Telephone and postage expense	25,537	
GSA administrative support service	28,050	
Consultant services	35,883	
GAO audit for fiscal year 1971	9,000	
Depreciation	2,127	
Office supplies	17,218	
Other expenses	<u>12,859</u>	
Total		<u>\$1,111,102</u>

COST OF OPERATIONS 1,565,112

PRIOR YEAR OPERATIONS

Accumulated deficit from operations June 30, 1971 (Note 6)	289,949	
Prior year adjustment	<u>346</u>	<u>290,295</u>

ACCUMULATED DEFICIT FROM OPERATIONS \$1,855,407

The notes on page 20 are an integral part of this statement

INTER-AMERICAN FOUNDATION
 CHANGES IN FINANCIAL POSITION
 DURING THE FISCAL YEAR ENDED JUNE 30, 1972

FUND BALANCES JUNE 30, 1971 \$49,808,591

NO FUNDS WERE PROVIDED IN FISCAL YEAR 1972

FUNDS WERE APPLIED TO

Cost of operations and prior year adjustment	\$1,565,458	
Less non-funded expenses (annual leave & depreciation)	<u>34,857</u>	
Funded expenses		\$1,530,601
Purchase of equipment		86,686
Increase in other assets		5,785
Decrease in current liabilities		27,662
Payment of annual leave to terminated employee		<u>905</u>
Total funds applied		<u>1,651,639</u>

FUND BALANCES JUNE 30, 1972 \$48,156,952

The notes on page 20 are an integral part of this statement

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 1972

- 1 In accordance with section 104 of the Government Corporation Control Act (31 U.S.C. 849), the Foundation may continue to obligate its funds up to its authorized ceiling of \$50 million. The Congress, however, may establish annual limitations on this authority. The Congress established a \$10 million limitation for fiscal year 1971, and a \$10 million limitation for fiscal year 1972.
- 2 The established cashier fund was \$3,000 on June 30, 1972, but the cashier had made cash payments totaling \$2,910 which were not replenished until after June 30, leaving a balance of \$90 actually on hand at the close of the year.
- 3 The annual depreciation rate is 6 percent for office furniture and 8 percent for office equipment. An adopted policy on depreciation is to charge no depreciation in the year of acquisition and a full year's depreciation in the year of disposal.
4. \$2.4 million of the reported net U.S. Government investment had been reserved at June 30, 1972, for approved but undisbursed grants (see Schedule 2).
- 5 Much of the annual leave expense represents the monetary value of annual leave owed to employees when they transferred to the Foundation from other U.S. Government agencies in fiscal year 1972.
- 6 The accumulated deficit from operations, June 30, 1971, resulted from start-up costs incurred during part of fiscal year 1971, the Foundation's first year of operations.

INTENDED ROLE OF THE INTER-AMERICAN FOUNDATION

In recommending the establishment of IAF, the Committee on Foreign Affairs, House of Representatives, suggested a new direction and a new emphasis for U S assistance efforts in Latin America. The suggestion emerged from a comprehensive reappraisal of the Alliance for Progress conducted early in 1969 by the Subcommittee on Inter-American Affairs, as well as from the full Committee's review of the overall framework of U.S. policy toward Latin America.

The Committee's recommendation was based on the following three major premises:

1. That, during the prior 8 years, all too little U S assistance had reached the masses of the Latin American people or had made a visible impact on their daily lives.
2. That, the social development goals of the Act of Bogota, the Charter of Punta del Este, and the Declaration of American Presidents, whose objectives of expanding opportunity for the great majority of people form the very cornerstone of the Alliance for Progress, had not been achieved in any substantial meaningful sense.
3. That, although Alliance for Progress programs operating at the government-to-government level had done an impressive job in promoting industrial and economic growth of Latin America, they had proved much less effective in responding to the requirements of social and civic change on that continent.

The establishment of IAF was intended to assist in rectifying these shortcomings and in restoring the necessary and proper balance between the economic and social objectives of Inter-American cooperation and development.

The Committee on Foreign Affairs believed that a number of development assistance programs administered by AID could and should be transferred to IAF. These were to include such activities as promotion of cooperatives, credit unions, and savings and loan associations, support for demographic research, planning, and related population programs, civic

APPENDIX I

development, including peasant leadership training, civic education, legal reform and aid, and democratic organization of labor, and other title IX-type undertakings

As envisioned by the Committee, the primary functions of the IAF staff would be (1) to review and support sound private undertakings in the field of social and civic development, (2) to stimulate research, innovation, and experimentation in overcoming bottlenecks to progress in education, agriculture, and basic environmental conditions relating to health, housing, and other social needs of the Latin American peoples, (3) to help support, when requested to do so, indigenous efforts toward developing local institutions required to facilitate broader popular participation in development, and (4) generally, to help the Latins pave the way for modernization of their societies in order that they may be able to achieve the social and human, as well as the economic, goals of the Alliance for Progress

A widely held view about IAF's planned program was that its support of private undertakings would encompass undertakings of both Latin American and U S private groups. Expressions of this view are quoted below

Committee on Foreign Affairs, November 1969

"As envisioned in the bill, the * * * [IAF] will operate primarily through private rather than governmental channels on a 'nation-to-nation', 'institution-to-institution' and 'people-to-people' level. There are some 800 non-profit organizations in the United States which are presently involved in social development activities in Latin America."

Statement by the President of the United States, August 1970

"The * * * [IAF] will provide grant support for innovative, experimental programs undertaken primarily by private non-profit organizations. It is designed as a pilot project to bring the dynamism of U.S. and Latin American private groups to bear on development problems through people-to-people programs * * *."

IAF's president, April 21, 1971

"The Legislation calls for support of both Latin American and Caribbean and international or regional as well as U S. institutions "

INTER-AMERICAN FOUNDATION

1515 WILSON BOULEVARD
ROSSLYN VIRGINIA 22209

February 26, 1973

Mr. Frank M Zappacosta
Assistant Director
International Division
U S. General Accounting Office
441 G Street, N W.
Washington, D. C. 20548

Dear Mr. Zappacosta

I have reviewed your draft report for fiscal year 1972 and appreciate the effort of your staff in reviewing the Foundation's activities. I am, however, disappointed in the program side of the report for reasons which I will explain.

PROGRAM ACTIVITIES

With respect to the analysis made of program activities, the report's fundamental weakness is in its limitation in factual basis and in its categorization of projects, organizations and funding as gleaned by the auditor from the grant agreements. Accordingly, without the benefit of any evaluation of program results, the report's conclusion is at best conjecture lacking fundamental support for a sound conclusion that the Foundation has restricted its chances for accomplishing its legislative purpose.

[See GAO note 1, p 38]

In carrying out its functions, the Congress envisioned that the fundamental concept of the Foundation would be that of a responder to the initiatives of Latin Americans as conceived by themselves rather than a prescriber of solutions for them. As to the establishment of new organizations and programs, the Congress intended that the Foundation help support, when requested to do so, indigenous efforts toward development of local institutions required for broader popular participation in the development process.

In this first year the Foundation was successful in seeking "a new direction" and "a new emphasis" by establishing its credibility with the dynamic leaders of Latin America as a direct funder of their innovative and experimental efforts, including their efforts toward development of new institutions and programs. As a result of that effort [See GAO note 2] "Projeto Piaui" recently funded by the Foundation is a unique and experimental effort involving a comprehensive civic and social reform program in the most undeveloped state of Brazil. The establishment of this new credibility, and innovative features in the specific projects and funding are important steps the Foundation has taken to attempt to

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rectify past shortcomings in U. S. assistance. These actions represent a sound beginning. It is unfortunate that these elements have not been adequately presented in the draft report in light of the above concept. Also, to attempt to strike a comparison between the Foundation's beginning and the path of others, particularly the creation of the NDF's, without discussing the underlying concepts which form a basis for the differing paths, is highly inappropriate.

Given the above shortcomings and the Congressional mandate, how is an effective beginning made toward rectifying past deficiencies? The Committee report speaks of a time lag of eight years in reaching the masses of Latin America with meaningful assistance. That time plus the delay in establishing the Foundation (to March, 1971) amounts to about a decade of neglect in U. S. assistance. I believe that the Foundation has taken the correct path in first determining that a sufficiency of capable indigenous organizations and dynamism exists in Latin America to make the Foundation's concept work, and at the same time, sowing the seed for new and innovative efforts. Proposals for new initiatives will come, as in the case of Projeto Piaui. However, they must come from within Latin America and therefore are not as predictable as with an organization working under the concept of intervening with its own ideas in Latin America. The path to meaningful development in Latin America in the 70's will not be improved by further saturation of their society with new organizations and programs conceived by outsiders. Our survey in Latin America has clearly underlined this and the wisdom of the Foundation's concept. While the Foundation must await initiatives for new organizations and programs to come from within Latin America, the Foundation has placed the proper emphasis on taking careful stock of existing organizations (new and old) and funding their specific projects, rather than general funding, which will effectively get at the shortcomings now. Innovative approaches inherent in the projects and funding should help to achieve a new impact in social development in Latin America. And, our primary and principal concern, in the spirit of the legislation, is the substance of the proposal and its potential for creating an ever broadening role for the people in the development process.

[See GAO note 1]

It is also inappropriate to generally categorize the Foundation's projects with "projects or types of projects previously supported with U S assistance " It is factual that the Foundation has funded organizations previously funded with U. S assistance, but its projects and rationale for funding differ substantially in light of its own concept This difference was aptly stated by Dr John Hannah, Director of AID, in a recent letter to the Pan American Development Foundation "AID will examine the general development lending needs of the operational NDF's, while the Inter-American Foundation stands ready to consider individual NDF proposals for seed or matching grants in support of specific projects or programs with clearly defined social development objectives " The Foundation, therefore, is not concerned with the general funding of the NDF's, but examines each NDF proposal on its own merits (as it does for any other indigenous organization) toward achieving its goal of a new direction and emphasis in social development for Latin America.

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Discussed below are three of the largest projects funded by the Foundation in fiscal year 1972. These specific NDF efforts illustrate the innovative features inherent in the Foundation's projects and funding as well as the new direction and emphasis that they represent toward social development in Latin America

Salvadorean NDF (Incorporated in 1969)

A generally recognized critical need in El Salvador is housing for marginal families. Total prior U S assistance to the Salvadorean NDF's revolving loan fund which is generally dedicated to meeting this need consisted of a \$2,500 grant and \$80,000 loan made through the Pan American Development Foundation (PADF) during 1971. As of the close of 1971, the NDF had made 58 loans aggregating \$22,000 and involving 245 people. Not all of these loans were used to finance construction of low cost housing. By the end of 1971 the NDF had completed and mortgaged 30 low cost housing units, and had invested \$186,000 in land and materials for the construction of another 629 units

The NDF proposed a unique five year plan to benefit 90,000 persons by creating urban communities among the slum dwellers of El Salvador's principal urban centers. Self-help housing (approximately 15,000 units) will be used as a tool to organize the people to form the communities, but a main focus in the plan is to stimulate group action, teach them useful trades, and deliver the civic and social services needed in breaking ground toward a better life. To our knowledge, this integrated approach has not been tried in this hemisphere although self-help housing and urban community organization have been subjects of unidimensional efforts in a number of settings. Moreover, this effort is sufficiently broad-scale to test the concept which, if successful, could reorient the housing policies of the Salvadorean Government and international lending agencies

The Foundation's grant of \$626,000 starts this five-year project off with funds for the construction of about 1,000 houses benefiting approximately 6,700 persons during the first year. The grant funds are to be used exclusively for self-help construction loans to persons whose income is on the average of \$30 per month and who do not qualify for housing assistance from other ongoing programs. The

NDF is to contribute \$425,000 (40 percent of first year costs) principally for land, administration and social development, and is obligated to attempt to stimulate contributions from the Government and private sector Grant funds will be used to establish a revolving loan fund from which the participating people can borrow the money needed to construct their homes and to cover community services Our grant also serves as leverage to secure the additional funds for the remainder of the five-year plan. [See GAO note 3]

From the above, it is evident that at the close of 1971, the Salvadorean NDF had just initiated its experimental effort toward working with the urban poor in El Salvador The program impacts on the social needs of the slum dwellers in an innovative, more relevant way which recognizes that housing alone does not build people oriented communities. It seeks to establish a base from which the poor may improve themselves and become recognized as a force in their community The Foundation's grant in February 1972 gave a timely and significant boost to that effort.

Relative to the above facts, the report's statement that, "The El Salvador foundation reportedly would obtain local, private and public support equal to about 30 percent of the project cost" is erroneous There is no "reportedly" about it The grant agreement obligates the NDF to contribute \$425,000 or 40 percent of first-phase project costs of \$1,051,000, and also requires the NDF to raise Government and private sector contributions for the future phases of its program The preceding facts also illustrate that the draft report fails in presenting enough facts or concept and in bringing these two elements together to make a reasonable conclusion. Further, to generally categorize this project as just another "project or type of project previously supported with U. S. assistance" is inappropriate. [See GAO note 3]

Mexican NDF (Incorporated 1968)

A critical problem in Mexico is rural development for the subsistence farmer. Prior to the Foundation's grant, the NDF experimented with a new system for integrating the subsistence farmer into social and economic life by combining community organization, social services, technical

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assistance and credit. This new systems approach is unique in the Hemisphere. It helps the farmers to organize for their own improvement and to understand modern social, agricultural and marketing techniques. Channeling credit to facilitate the application of these techniques is an important part of the system. The NDF, through the service centers, helps the farmers prepare their loan applications, and serves as a middleman with private banks in obtaining these loans. To facilitate private bank acceptance, the NDF obtains guarantees from Mexican private companies or gives these guarantees itself based on its own capital and reserves.

Prior U. S. support of the NDF included an administrative grant of \$6,000 made prior to 1971, and a loan of \$85,000 made in 1971. As of the close of 1970, the NDF had made 61 loans valued at \$208,000, while at the end of 1971, the NDF had a portfolio of 148 loans valued at \$706,000. Cumulative persons benefiting as of 1970 and 1971 totaled 6,005 and 6,500 respectively. Prior to the Foundation grant the NDF had tested its system in one region of one state, but that experience was insufficient for assuring the potential of this approach for incorporating the marginal farm population into the development process.

The Foundation's grant, made in June, 1972, is part of a \$1.1 million effort designed to promote and put into operation approximately 15 additional regional service centers. Our grant of \$500,000, together with an equivalent matching amount raised by the NDF, is to be used to increase loan-guarantee fund capital from approximately \$300,000 to \$1.3 million by December, 1973. Loans and guarantees to grass-root organizations are to be provided at the rate of \$2.4 million in 1973. The NDF will also contribute resources valued at \$120,000 for promotion and training of regional service center personnel and for the expansion of services to marginal farmers.

From the preceding facts, it can be seen that the Foundation's grant is a substantial input into the NDF's budding program which will allow a broad-scale test of the new system in reaching the masses of rural Mexico. Each of the new regions (involving 14 states) will have its own special needs and problems. The new emphasis made possible by the Foundation's grant, if successful, could well lead to new national policies for involving and transforming the lives of marginal peoples.

Dominican NDF (Incorporated in 1965)

As in Mexico, a critical need in the Dominican Republic is rural development. Since beginning operations in 1966, the NDF has made good progress through its revolving loan fund in building a portfolio of 2,398 loans valued at \$1.7 million and benefiting 150,370 persons. This progress was made possible by assistance from the U S and Organization of American States totaling \$858,000, including a \$90,000 administrative grant, \$222,000 emergency grant, and \$546,000 in loans according to the PADF 1971 annual report. In 1971, when funds available for loans could not meet the demand, the NDF requested Foundation support for their ongoing program and was turned down.

In a subsequent request for support the NDF proposed a significant innovation to its program, namely, to transfer its borrowers with good credit ratings to private sector lending institutions. Up to this time, the NDF saw itself as an exclusive source of credit for marginal farmers entering the economy, and, each time it ran short of funds it increased its liquidity by seeking additional loans from external aid organizations. This proposal represents a new initiative to draw on domestic private resources to meet its liquidity problems and links the private banking sector for the first time with grass-roots rural problems. The Mexican NDF, through its own experience and that of a sister organization, succeeded in involving private sector banks in making loans for rural development through guarantees by Mexico's business and professional community. The Dominican project and the way it is to be accomplished represents a significant new initiative in the Dominican Republic by setting up a system for opening up private bank credit to the marginal farmer. It is also the first time that an NDF which operates as a lending institution has initiated a program to integrate its former borrowers with good credit ratings into the usual private banking system of its country.

The Foundation funded this new approach in April, 1972 on a one to one matching basis, based on the following formula: disbursement of our grant funds is contingent upon receipt of certifications from private sector institutions showing that they have made loans equivalent to the amount requested.

of us and that the NDF has approved new loan applications in an amount at least equal to the requested disbursement Grant funds, with the exception of a small amount for technical and operational assistance, will be used exclusively for unsecured economic and social purpose loans to borrowers not yet qualified for credit from the private sector, which experience will be used to facilitate their later transfer to private sector lending institutions. The NDF is required to use its own funds as loan guarantees to the private sector institutions. The grant specifies a declining rate of guarantee by the NDF, and controls the maximum cost of credit charged former NDF borrowers by the private sector.

The above facts show that the Foundation's grant provides a new thrust in the Dominican NDF's loan program. If successful, the project will significantly broaden the NDF's impact in development, and serve as another example of the feasibility of the "transfer role" of the NDF's toward private sector financing of social development.

Funding of Projects

[See GAO note 1]

With respect to requiring a matching contribution, the view expressed in the report as that of the Foundation is incorrect. The Foundation considers the funding needs of each particular project in light of the capability of the proponent to contribute funds or other resources, the circumstances in his environment and his capability to marshal resources from other sources, and the degree of dependency risk in the funding plan. Although the maximum contribution possible is sought from the proponent and other sources, it is not in keeping with the Foundation's concept to apply an inflexible matching rule for new or existing organizations which would serve as an impediment to their new or experimental initiatives [See GAO note 4]

For example, in the Mexican private sector, banks and businessmen have been very active in financing of rural social development. Prior to establishment of the Mexican NDF, private banks had been making loans for rural development projects which were guaranteed by Mexican businessmen. Based upon existing capabilities, therefore, it was considered feasible to fund the Mexican NDF project on the basis of one dollar for each dollar contributed to the NDF from the Mexican private sector. A different situation exists in the Dominican Republic where the main thrust of the project is to begin a broad scale involvement of private sector banks and credit institutions in rural development.

In the Dominican project the most appropriate and desirable matching was perceived to be the resources mobilized by the NDF from private sector banks for loans to former borrowers of the NDF. This not only linked our input to performance by the NDF but facilitates the exclusive use of the NDF's own funds--including our grant--to break new ground for making unsecured economic and social purpose loans to those not previously within any credit system. Hence, our grant provides one dollar from us for each dollar of private bank loan arranged for by the NDF for its former borrowers. This mechanism permits the NDF's current borrowers to be later transferred to the private sector banks and to constantly reach out to service those in need.

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The Foundation uses grant agreements to fund its projects principally because loans tend to discourage the innovation and experimentation needed to reshape old programs and methods and launch new endeavors. Also, within its concept of emphasizing broader social and civic development through the funding of sound private initiatives, the Foundation believes that with use of the loan instrument the proponent is faced with the administrative problem of repayment with interest, which tends to deflate the effort or direct the effort away from the general populace to a segment having a favorable repayment potential. In the Dominican NDF project, for example, grant funds are used exclusively to break new ground for unsecured loans not fundable by the private sector, whereas the NDF's old customers with some repayment potential will be transferred to the private sector as the reshaping phase of the total effort.

Several other benefits accrue from the Foundation's use of the grant instrument in line with its concept. In funding a specific project, the grant results in a capital injection to the organization's balance sheet which promotes confidence in the organization and its endeavor which is difficult to measure in tangible terms. The Foundation believes this has had a positive effect in stimulating inputs of resources from other sources. Several of the Foundation's grantees have experienced unusual inputs of non-U S resources during 1972. Also, grants for revolving fund projects have a multiplier effect emanating from the immediate reuse of capital upon repayment from the ultimate user. Loans have a deflating effect during the repayment cycle.

Although innovative and having a beneficial impact, the Foundation's policy of direct grant funding of indigenous organizations is not discussed or compared with previous U. S. assistance. For example in the case of the NDF's, the PADF is eliminated as a middleman in the chain between the U. S. taxpayer and the ultimate beneficiary. It is a reasonable assumption that the U. S. taxpayer has been bearing the cost of a portion of the administrative expenses of the PADF which currently are exceeding \$200,000 per year. Also, use of the loan instrument by the PADF and the resultant interest income,

[See GAO
note 5

which represents a growing source of revenue in the PADF's financial statements, helps assure a continuity of operations for the PADF. The interest cost, however, must be borne in country by the marginal groups or the NDF servicing them. The uncollectible accounts of less than five percent experienced by the NDF's in 1971 also suggests a degree of caution in utilizing PADF loans which may not be reaching the masses and the risks inherent therein, which is the Foundation's concept. Finally, general purpose funding through loans fosters a dependency on the PADF which is contrary to the Foundation's purpose.

We have focused above on NDF's and used them and their PADF support as examples of inaccurate factual presentation of our activity in the report, but of course the same basic objections apply to the discussions in the "Community Service" and "Cooperative Business Ventures" sections of the report.

To illustrate these inaccuracies, just compare the titles attributed to our projects on page 8 of your draft report with the titles listed below which substantively summarize the activities being carried out by our grantees [See GAO note 6.]

- Brazil - . Permanent civic education component built into community development program
- . Community development - civic and social training for urban citizens
- . Community development - civic and social training for rural citizens
- . Building skills and job possibilities for slum dwellers in Rio.
- . Restructuring legal education in Brazilian universities to meet the needs of people in the development process

- Colombia - . Adapting modern business management techniques to the needs of small, labor intensive enterprises.
- . Creating community-owned enterprises in the slums of Bogota.

- Honduras - . Organization of women for community participation

APPENDIX II

- Panama - . Involvement of students in rural literacy programs
- Trinidad - . Demonstration of potential for shifting church social activities from charity to job training
- Ecuador - . Civic and social education for subsistence farmers as part of total project for rural development

The classification of projects throughout the Report loses the essence of our effort to support social and civic development. We have approved a mosaic of projects to test new approaches for providing opportunities for people

- in the rural areas, the Mexican Development Foundation, the Dominican Development Foundation, FANAL, CEAS in Ecuador, the Honduras Rural Wives Program, FASE in Brazil and ANDE in Panama are testing new approaches for combining community organization, economic improvement and socio-civic action for integrating people into the development process and for effecting basic change.
- in the urban areas, MOC in Brazil, FASE in Brazil and the Salvadorean Foundation are applying innovative techniques of community organization and self-help action to awakening people to their potential for participation and improvement
- through seeking new approaches to job creation in urban and rural areas, coupled with social action training, FANAL, CEAS, COPAC, Ação Comunitaria, Coopeschi, FICITEC, Acción en Colombia and Christ College are affording us new experiences for seeing how far private action can stimulate and promote grass-roots initiative to solve the critical unemployment problem facing the people of Latin America and the Caribbean.
- for more effectively integrating the legal system into the development of justice, PUC in Brazil provides a unique testing ground for evaluating the degree to which Latin Americans can revamp their legal system to serve their people in the development process and promote change through the law

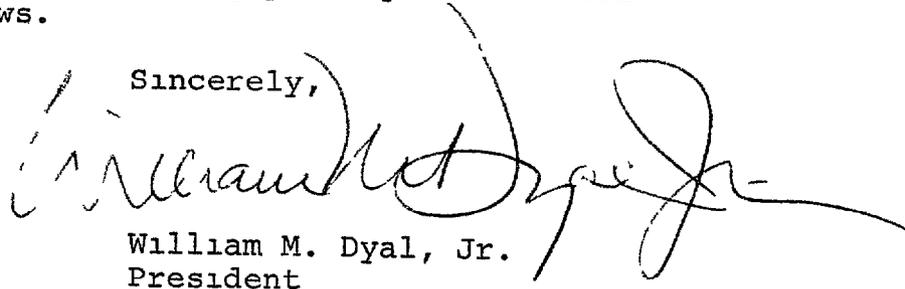
ADMINISTRATIVE ACTIVITIES

[See GAO note 1.]

Additionally, we have always estimated a level of at least \$1.5 million for program support for FY 1973 and more for FY 1974, making the "about \$1 million a year" projected cost of administration a gross underestimation

We do appreciate the opinion stated in Chapter 4 that the application of our funds for FY 1972 is in conformity with generally accepted accounting principles and with applicable Federal Laws.

Sincerely,

A handwritten signature in cursive script, appearing to read "William M. Dyal, Jr.", written in black ink.

William M. Dyal, Jr.
President

GAO NOTES

- 1 GAO has deleted material consisting of comments which no longer apply to the report
- 2 IAF funded "Projeto Piaui" during fiscal year 1973, after the period covered by GAO's review, and consequently the report does not include consideration of that project
- 3 IAF's references to \$425,000 and 40 percent are misleading in that the \$425,000 includes \$96,000 from AID. The national development foundation agreed to obtain \$329,000 from local sources, which is about 30 percent of the project costs
- 4 GAO's previous statement regarding IAF's view on matching funds no longer appears in the report. It was replaced with the current IAF view, as now stated by IAF
- 5 GAO knows of no valid evidence to support IAF's contention that the substitution of IAF for PADF has saved the U S taxpayer money
- 6 The titles referred to by IAF as being on page 8 of the draft report are on page 11 of this report

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THE INTER-AMERICAN FOUNDATION

AT JUNE 30, 1972

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