

## **Part I**

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### ***Executive Summary***

**INTRODUCTION**

The Swiss deposits under escrow at the Philippine National Bank (PNB) in the estimated aggregate amount of US\$658.175 million as of January 31, 2002, plus interest, was forfeited in favor of the government under Supreme Court Decision GR No. 152154 promulgated on July 15, 2003. A Writ of Execution was then issued by the Sandiganbayan on January 22, 2004 demanding PNB to remit the forfeited Swiss deposits to the Sandiganbayan.

The Trust Banking Group of the PNB certified that the market value of the assets subject of Writ of Execution as of January 30, 2004 was in the aggregate amount of US\$688.843 million. This amount is net of accrued expenses/fees deducted from the market value in the amount of US\$1.319 million as reflected in the accompanying schedule.

In compliance with the Order, the PNB and the petitioner, through the Presidential Commission on Good Government (PCGG) and the Bureau of the Treasury (BTr), reached an agreement to put the amount subject of writ to PNB under custodianship account. Thus, on January 30, 2004, the parties entered into Custodianship Agreement (CA) whereby the amount of US\$624.045 million to be transferred and delivered to the Republic of the Philippines will be held under custody by the PNB. The amount under custodianship account was recorded in the BTr books as fully remitted by the PNB on March 12, 2004.

Out of the certified balance of US\$688.843 million as of January 30, 2004, US\$624.045 million was transferred to the national government. This was claimed to be net of expenses and excluded the following accounts which were retained under escrow account at the PNB:

- the amount of approximately US\$22 million invested with West LB AG, Singapore Branch;
- the amount pertaining to Arelma Foundation; and
- the amount equivalent to at least 5% of the escrow funds or US\$30 million whichever is higher, which was set aside as contingent fund to answer for expenses in connection with unsettled claims and any lawsuit or potential lawsuit that may arise against PNB officers and employees.

This transfer was recorded and accounted in the BTr books on February 4, 2004 under Other Liability account in the amount of ₱35.043 billion. Funds are transferred from this account, upon request by the Secretary, Department of Budget and Management (DBM), to the Agrarian Reform Fund (ARF) for the

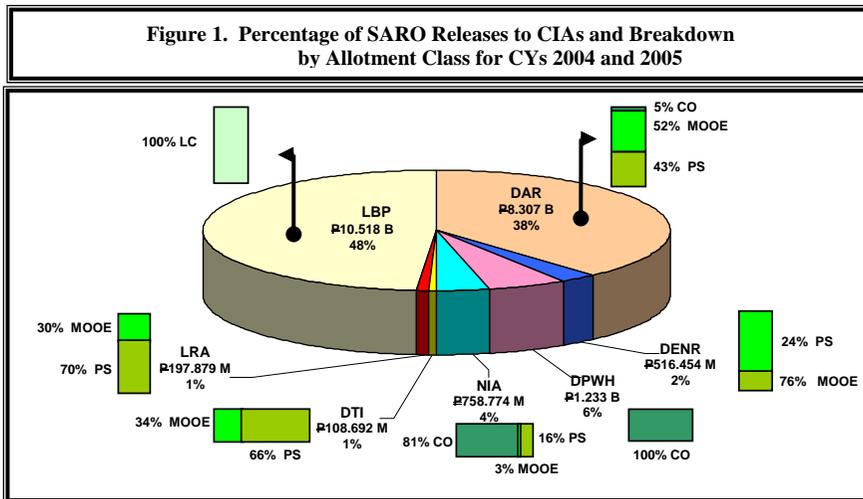
implementation of Comprehensive Agrarian Reform Program (CARP). The funds transferred to ARF were intended to reimburse the National Government on the corresponding amount of the Notice of Cash Allocations (NCAs) released by the DBM to CARP Implementing Agencies (CIAs). As of December 31, 2005, total requests by the DBM and actual transfers by the BTr amounted to ₱16.154 billion. The latest request for transfer of funds was on August 31, 2005.

As of December 31, 2005, total Special Allotment Release Orders (SAROs) issued by the DBM in CYs 2004 and 2005 amounted to ₱21.640 billion to cover personal services (PS), maintenance and other operating expenses (MOOE), capital outlay (CO) and landowners compensation (LC). Of this amount, ₱20.163 billion was covered by Notices of Cash Allocation (NCAs) of which ₱16.154 billion was already replenished to the ARF.

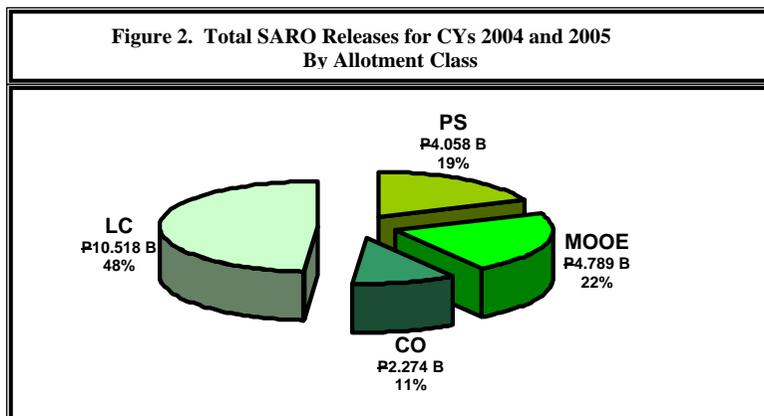
The allocations by CIAs follow:

Table 1. SARO and NCA Releases by CIA			
Agency	In ₱Million		
	2004	2005	Total
<b>Special Allotment Release Order (SARO)</b>			
DAR	₱ 4,424.872	₱ 3,881.713	₱ 8,306.585
DENR	190.266	326.188	516.454
LRA	98.980	98.899	197.879
LBP	6,644.033	3,874.227	10,518.260
DTI	54.506	54.186	108.692
NIA	570.568	188.206	758.774
DPWH	1,133.000	100.000	1,233.000
<b>Total</b>	<b>₱ 13,116.225</b>	<b>₱ 8,523.419</b>	<b>₱21,639.644</b>
<b>Notice of Cash Allocation (NCA)</b>			
DAR	₱ 4,377.006	₱ 3,696.379	₱ 8,073.385
DENR	200.565	307.860	508.425
LRA	93.747	89.650	183.397
LBP	6,644.033	3,874.227	10,518.260
DTI	51.821	48.987	100.808
NIA	373.594	161.230	534.824
DPWH	234.722	8.863	243.585
<b>Total</b>	<b>₱ 11,975.488</b>	<b>₱ 8,187.196</b>	<b>₱ 20,162,684</b>
<i>Legend:</i> DAR- Department of Agrarian Reform DENR- Department of Environment and Natural Resources DPWH- Department of Public Works and Highways DTI- Department of Trade and Industry LBP- Land Bank of the Philippines LRA- Land Registration Authority NIA- National Irrigation Administration			

The CIAs' percentage share on the total releases and the breakdown by allotment class is depicted on the chart shown in Figure 1.



The allocation by allotment classification is presented below:



Out of the total releases to DAR for MOOE of ₱4.319 billion, ₱677.450 million were released to different agencies/organizations for the implementation of various projects:

Agencies/Organizations	Amount (In ₱Million)
National Government Agencies (NGAs)	₱ 520.813
Non-Government Organizations (NGOs)	114.378
Government-Owned & Controlled Corporations (GOCCs)	42.258
<b>Total</b>	<b>₱ 677.449</b>

Likewise, releases to DAR intended for Capital Outlay of ₱199.228 million were transferred to the Local Government Units (LGUs) for the implementation of farm to market road projects.

### **AUDIT OBJECTIVE**

The audit was conducted to assess the effectiveness of allocation and utilization of the forfeited Swiss deposits transferred to the Agrarian Reform Fund (ARF) in ensuring the delivery of the required services to the intended CARP beneficiaries.

### **EVALUATION CRITERIA**

The performance of the CIAs in relation to the above objective was assessed using the following evaluation criteria:

- Appropriate fund disposition;
- Effective project implementation;
- Rationale identification of infrastructure projects;
- Accurate reporting of accomplishments; and
- Adequate funding for landowners compensation.

### **AUDIT SCOPE**

The audit covered the evaluation of selected transactions funded out of ARF releases to the different CIAs reimbursed from the forfeited Swiss deposits during CYs 2004 and 2005 including funds transferred by DAR to the Department of Agriculture and Philippine Coconut Authority (PCA).

The audit also covered evaluation of available records pertaining to Forfeited Swiss Accounts and subsequent releases therefrom maintained by the BTr, DBM and PCGG.

### **AUDIT LIMITATION**

The audit of funds released to DAR was limited to selected MOOE accounts and payment of allowances out of releases for PS. On the other hand, validation of reported accomplishments on infrastructure projects implemented by the DPWH, NIA, DAR and LGUs was limited to projects implemented in Regions II, III, IV-A and VI while validation of payments by the LBP to landowners and land distribution to beneficiaries were not covered in the audit.

The audit also intended to establish the accuracy of the amount of forfeited Swiss deposits transferred by the PNB to the BTr. However, this could not be undertaken as the PCGG, despite repeated requests, did not submit documents, particularly, an accounting on the movement of the funds under Escrow, the total amount retained at the PNB, the summary of expenses charged against the Escrow account and the amount retained at the PNB, and the computation of the amount transferred to the BTr.

### **AUDIT METHODOLOGY**

During the audit, the team performed the following procedures, among others:

- Obtained and reviewed available documents on the distribution and utilization of the forfeited Swiss deposits;
- Reviewed existing policies and procedures on the implementation of CARP;
- Traced the flow of funds from the CIAs' Central Offices to the Regional Offices, LGUs, NGAs and NGOs;
- Evaluated and reviewed selected transactions to assess propriety and eligibility of charging against the ARF;
- Verified and confirmed the receipt of funds/procured items by selected reported recipients;
- Assessed eligibility of projects implemented under CARP using as basis for evaluation the PARC guidelines on project identification and prioritization;
- Inspected selected CARP projects to determine existence and compliance with plans and specification; and
- Interviewed selected Agrarian Reform Beneficiaries (ARBs) to validate support services provided.

**AUDIT CONCLUSION**

The audit disclosed that substantial amounts intended to deliver the required services to CARP beneficiaries were not effectively utilized. The ARBs did not obtain maximum benefits from the amounts reimbursed from the Forfeited Swiss Deposits as they were not given preference under the program as manifested in the following:

1. An aggregate amount of ₱521.032 million were not appropriately disposed as these were used to finance excessive, unnecessary expenses and regular activities of the CIAs and other government agencies and projects unlikely to benefit the ARBs such as:
  - Operational requirements of the regular activities of the CIAs, unnecessary and excessive claims amounting to ₱419.556 million;
  - Advertising expenses of DAR in the total amount of ₱45 million which includes:
    - Simultaneous advertising of CARP anniversaries and DAR accomplishments in as many as eight (8) different print media at a cost of ₱4.721 million in CYs 2004 and 2005 which is considered unnecessary under existing COA regulation;
    - Advertising of various items as many as five (5) times in a month in addition to simultaneous coverage of DAR commercials in different stations almost year round;
  - Lease contracts for Information Technology and other office equipment entered into by DAR in the amount of ₱7.640 million exceeded the acquisition cost for similar brand new items by 27% to 297% or a cost difference of ₱2.947 million;
  - Procurement of ink cartridges amounting to ₱9.731 million in CYs 2004 and 2005 exceeding the prices offered by the Procurement Service by ₱2.226 million or by an average of 29.66%;
  - Financial assistance extended by DAR to other government agencies in the amount of ₱29.514 million to finance regular activities/special programs not intended to uplift the ARBs' condition and not within the coverage of CARP;
  - Investment of DAR in projects unlikely to benefit the ARBs in the amount of ₱58.558 million. The project costing ₱30 million was already non-

operational without return on investment yet, while the status of eight (8) others were uncertain due to the absence of reports;

- Excessive cost incurred by the LRA in the amount of ₱3.510 million in distributing patents with the assistance of Central Office officials and employees. The LRA spent ₱3.958 million in CYs 2004 and 2005 for distribution of 22,751 patents equivalent only to 18.87% of the total reported distributed patents of 120,516. In contrast, the Registers of Deeds (RDs) were able to distribute 97,765 at a cost of only ₱1.496 million. This manifests the RDs' capability of performing this function at lower cost without assistance from the Central Office.

The efficient utilization of ARF was also affected by the continuous allocation of funds to the CIAs' Regional Offices without commensurate accomplishments.

2. A number of projects were also not effectively implemented depriving the ARBs benefits therefrom. Validation of available distribution list of hybrid seeds and other farm inputs/implements procured under various programs/projects revealed that ₱81.17 million were released to non-ARBs, to recipients who are unknown at their given addresses or not released at all while validation of releases amounting to ₱45 million could not be undertaken as these remained unliquidated as of December 31, 2005. These cases are discussed below:

- The reported beneficiaries of farm inputs amounting to ₱50 million released to two (2) NGOs could not be located at their given addresses. The respective barangay officials certified that the listed recipients were not residents of their barangays. They were likewise not included in the Masterlist of DAR beneficiaries. Verification of the propriety of another ₱45 million released to four (4) NGOs as assistance to various farmers could not be undertaken as these remained unliquidated as of December 2005.
- Out of 13,960 bags of hybrid rice reportedly sold to farmers, only 1,106 bags were procured by ARBs. The balance of 12,854 bags amounting to ₱15.425 million were sold to non-ARBs. The status of farmers was validated from the masterlist of ARBs forwarded to the team by DAR and DENR.
- The 5 units fabricated shredder procured by DA-RFU IV for ₱3 million were also distributed in private farm and subdivision.
- Out of the total procurement of 3,750 bottles of liquid fertilizers by DA-RFU XI, 2,249 bottles amounting to ₱1.799 million were undistributed, the distribution of 777 bottles amounting to ₱.620 million were undocumented while out of the 724 documented distribution, 620 amounting to ₱.496 million were distributed to non-ARBs.

- Of the 2,138 listed recipients and 840 other intended recipients of fertilizers in Region VII, only two are ARBs with a total share of only 5 liters out of 6,000 liters. The listed recipients of 5,995 liters amounting to ₱8.993 million were non-ARBs.
- Two hundred sixty one (261) bags of seeds amounting to ₱.313 million reportedly distributed in six (6) distribution outlets by PhilRice were confirmed by the outlets to have been returned to the supplier and/or PhilRice while 435 others amounting to ₱.522 million remained undistributed in four (4) other outlets.
- Only 133 out of the 2,969 members of the 21 cooperatives reportedly trained by PEACE Foundation in relation to its contract with PCA are ARBs.

Substantial procurement of hybrid seeds by PhilRice were not supported with list of recipients and therefore could not be verified. Thus, there is no assurance that these items reached the intended beneficiaries. The lists were claimed to be maintained by the concerned LGUs, DA Field Regional Units (RFUs) and the distribution outlets.

3. Substantial amounts were also used to procure items at excessive prices, contract out the same activities twice and finance camp out/rallies of farmers at DAR and PCA offices as manifested below:
  - Procurement of farm inputs and implements exceeded the market price by ₱42.785 million in seven (7) selected regions alone.
  - The DAR and PCA contracted out the same activity to PEACE Foundation in the amounts of ₱4.50 million and ₱2.40 million, respectively.
  - The PEACE Foundation under its contract with the PCA used the funds released for advocacy amounting to ₱.716 million to finance the camp out/rallies of the Bondoc Peninsula Farmers to DAR and PCA Central Offices.
4. A great number of projects implemented in CYs 2004 and 2005 amounting to ₱1.175 billion were not among the priority projects validated for implementation, some of which were constructed in areas without ARBs while 96 projects implemented by NIA in the amount of ₱362.188 have no corresponding releases as discussed below:
  - Out of 1,093 projects implemented by DAR, DPWH, and NIA, 713 amounting to ₱1.175 billion were not included in the list of prioritized and validated projects. The eligibility of these projects to be funded under CARP and the benefits to ARBs were therefore not evaluated. Inspection of 348 unvalidated projects implemented in Regions II, III, IV-A and VI

revealed that 84 projects costing ₱96.84 million were constructed in areas without ARBs.

- Ninety six (96) projects in the amount of ₱362.188 million implemented by NIA were not included in the SARO released by the DBM. These projects replaced 95 other projects intended to be implemented in CY 2004.
5. Of the 535 farm to market roads (FMRs) inspected by the team, 353 costing ₱381.504 million were road regraveling which did not provide long term benefits to ARBs. As of inspection date, 66 projects constructed in the aggregate amount of ₱89.241 million already need rehabilitation while 17 others costing ₱33.700 million were already rehabilitated or undergoing rehabilitation.
  6. In four regions covered by audit, reported project accomplishments exceeded actual accomplishments by ₱39.939 million. Payments which were not commensurate with the reported accomplishments depleted the ARF and deprived ARBs full benefit on the use of the projects. Of the total noted deficiencies, ₱8.446 million were claimed to have been corrected by the implementing agencies after the team's inspection.

In addition, the allocation to LBP amounting to ₱10.518 billion representing 48% of the total SARO issued for CYs 2004 and 2005 was apparently inadequate to meet landowners compensation necessitating the LBP to make some advances. Outstanding advances by the LBP as of December 2005 remained at ₱1.133 billion. This is in addition to the reported unfunded obligations to landowners which amounted to ₱7.124 billion and bonds maturing yearly until CY 2015 which amounted to ₱24.410 billion as of December 2005. The allocation to LBP could have been augmented from the allocations to other CIAs which were used to finance programs/projects not eligible for funding under CARP.

#### CIAS'S COMMENTS

The team forwarded the draft audit report for comment to PARC Secretariat and DAR Secretary and pertinent portion of the draft report and/or audit observations to concerned CIAs from July 3 to 10, 2006. Initially, the CIAs were given 10 days to submit their comments. The prescribed timeline for submission of comments was extended for 70 days upon representations made by the Secretary of DAR. An exit conference was conducted with the PARC and DAR officials on September 7, 2006. The final CIA's comments were received by the Management Services on

September 18, 2006 with additional comments submitted on October 2, 2006. All comments submitted by the CIAs as of the said date were incorporated in the report, where appropriate.

The PARC Secretariat and DAR recognized the existence of the deficiencies raised in the report with some reservations and submitted explanations on the circumstances surrounding the issues.

They informed the team that efforts are being exerted to address the issues raised. They also committed to seriously consider and implement audit recommendations, adhere to established rules and regulations and endeavor to limit expenses within approved budget of DAR and PARC.

Other implementing agencies claimed that the expenses incurred are reasonable and valid although they are taking actions to reduce expenses within the amount authorized.

On the other hand, some projects found deficient were reported by the CIAs to have been corrected. They also claimed that deficiencies on other projects were constructed in another site which were not considered by the team.

### **AUDIT RECOMMENDATIONS**

In view of the noted deficiencies, the team recommended certain measures to be undertaken by the CIAs which are discussed in full under Part IV of the report. In summary, the CIAs should:

Stop the practice of using ARF for purposes other than those that would benefit the ARBs and financing unnecessary and excessive claims.

Require the refund of fund transfers which could not be liquidated, with inappropriate liquidation reports, used in payments of expenditures in excess of the prescribed limits and not within the CARP coverage.

Conduct thorough validation of all projects intended to be funded under CARP, evaluation of the benefits derived by the ARBs for each project, identification of the targeted beneficiaries before any release is undertaken, monitoring of project implementation to ensure that all programs and projects redound to the benefits of the ARBs and price evaluation before any procurement is undertaken.

Stop the practice of transferring funds to NGOs for procurement of farm inputs, implements and other items.

In addition, the team also recommends that the BTr should require the PCGG to account for the funds under escrow and determine the accuracy of the funds transferred by the PCGG to the BTr.