

PD-ABC 319

69251

**Agency for International Development
Washington, D. C. 20521**

**Office of the Auditor General
Area Auditor General - Latin America
Argentina Branch Office**

**Audit Report on
TWO-STEP LOANS
Argentina**

**Period covered by audit:
Through December 31, 1973
Audit Report No. : 1-510-74-64
Date Report Issued: February 22, 1974**

RECORD COPY

Table of Contents

	<u>Page No.</u>
Part I - Purpose and Scope	1
Part II - Background	2
Part III - Summary	3
Part IV - Statement of Findings and Recommendations	4
A. Generation and Use of Local Currency	4
B. First Borrower Repayments	5
Part V - General Comments	7
Exhibit A - Two-Step Loan Agreements	8
Exhibit B - Distribution of Audit Report	9

Part I - PURPOSE AND SCOPE

We have made a special examination of the two-step loans outstanding in Argentina. The purpose of this limited review was to determine the status of funds derived from the two-step procedure as of December 31, 1973.

Our audit was made in accordance with auditing standards adopted by the Auditor General and was generally limited to reviews of USAID and Central Bank records, and interviews with appropriate officials of both agencies.

Part II - BACKGROUND

AID has authorized three loans to the Government of Argentina (GOA) which provide for repayment under the two-step procedure. The terms of these loans are detailed in Exhibit A.

The two-step system consists of the first-step borrower making interest and amortization payments to the Central Bank as agent of the GOA in local currency at a higher interest rate and a shorter grace period than is granted the GOA which must make payments in dollars to AID and must bear the exchange risk. During the interval between the first repayment by the first-step borrower and the commencement of amortization by the Central Bank, the latter accumulates sizeable amounts of local currency. The accumulated funds in excess of amounts needed for loan servicing shall be used for social and economic development purposes as mutually agreed between the GOA and AID.

Only the Self-Help housing loan has been fully disbursed, and principal repayments for this loan by the Central Bank will begin in May 1974. Pesos generated by the loans now total A/P 5,947,119 (approximately \$ 605,000).

Part III - SUMMARY

The funds accumulated in special accounts from the two-step loans have not been used. Because of continuous devaluation of the local currency the value of the pesos needed to repay the loans in dollars has increased by \$ 360,000. We believe that since no agreements have been reached to use the idle funds USAID should follow the procedure as provided in AIDTO CIRCULAR A-184, dated 2/7/73 which permits the host government to use the local currency funds without USAID approval or special account arrangements.

We noted that in certain instances the notices of payment due (NPD) submitted by AID to the first-step borrower included amounts that had already been repayed by the first-step borrower to the Central Bank. This happened when loan management was centralized in Washington and USAID no longer had to report payments received by the Central Bank. We believe the procedure to bill the first-step borrower should be reviewed.

The above findings were reviewed with USAID personnel and their comments have been included in the report as considered necessary.

Part IV

STATEMENT OF FINDINGS AND RECOMMENDATIONS

A. Generation and Use of Local Currency

In our opinion, the USAID has not taken proper advantage of using the accumulated two-step funds in accordance with the underlying agreements.

Loan funds are presently available under the Self-Help Housing project and small amounts are available under the other two loans; however no agreements have been reached for the use of these funds.

In 1968 the GOA issued two Executive Orders - without previously consulting USAID - ordering the Central Bank to return to the first-step borrowers the funds not immediately needed for servicing the loans. The Central Bank refused to do so on the grounds that the payment agreements required USAID's consent. The fund at that time was generated by the Self-Help Housing Loan (510-L-012) and the USAID used its consent as a lever against the first-step borrower who was remiss in complying with certain loan obligations. Unfortunately no further use of the funds was ever agreed to.

In 1972 conversations started between USAID and the National Institute of Agricultural Technology (INTA) - the first borrower in loan 510-L-013 - regarding the use of these funds for training and related activities; however, the political events of 1973 took precedence and the conversations were discontinued.

As of December 31, 1973 the funds held by the Central Bank have a consolidated balance of 5.9 million Argentine pesos which at the present rate of exchange (A/P 9.93 to \$ 1) represents \$ 604,000. Applying the different rates of exchange when the payments were made to the Central Bank, the fund should equal \$ 965,000. The difference of approximately \$ 360,000 represents the decrease in value of the pesos while they remained idle with the Central Bank.

On December 13, 1971 the AID Administrator issued a policy directive prescribing that AID should not become involved in the programming of two-step loan funds. On February 7, 1973 AIDTO CIRCULAR A-184 indicated the USAID should review each outstanding two-step loan to determine whether AID should disengage itself from special account arrangements and/or eliminate requirements for AID approval of local currency utilization.

Our review revealed only a draft airgram prepared by the USAID Engineers which proposes that two-step funds be used to provide INTA with funding for research and teaching. This airgram was never issued.

Because no agreements have been reached and apparently none are contemplated, we believe that USAID should disengage itself from control of the two-step funds as provided in AIDTO CIRCULAR A-184.

Recommendation No. 1:

USAID should recommend to AID/W disengage from the control of two-step loan funds generated under 510-L-011, 510-L-012, and 510-L-013 as provided in AIDTO CIRCULAR A-184, dated February 7, 1973.

B. First Borrower Repayments

The AID/W Controller's office maintains ledgers recording the payments made by the first-step borrowers to the Central Bank, including interest and principal repayments, and sends notices of payments due (NPD) to the first-step borrower. Some of the NPD's received recently from AID/W have not credited the first-step borrower for prior installment and/or interest payments. The NPD show the prior payments overdue and compute additional penalty interest on the amounts presumably unpaid. This was caused by the fact that AID/W was not advised of such payments by the GOA or the USAID.

In prior years, the Missions notified AID/W of first and second borrower payments by cable, as payments were received by USAID. In July 1972, and in line with the centralization of loan management in AID/W, the missions were advised payments were to be made by the cooperating governments directly to AID/W. Consequently, reporting of payments received was discontinued and AID/W did not receive the notice of payments effected from the first-step borrowers; hence, billings were made for what was thought to be non-payment.

In view of the difficulties encountered, AID/W has requested that the USAID Controller report by cable the payments made by the first-step borrower to the Central Bank. This should be a satisfactory solution to updating AID/W records but it appears temporary in view of a future mission close out and appears to be a rather informal way of updating records which will be used as a basis for future billings.

Although the billing to the first-step borrower is required by M. O. 743.8, which is outdated, we are not aware of the reason why the billing is necessary at all. It appears that the payment agreement which requires the first-step borrower to make payment to the host government Central Bank would supersede the original agreement that required payment to AID. Therefore any billing to the first-step borrower should be made by the Central Bank and not by AID because the Central Bank must collect the money.

In view of the difficulty in determining what payments are being made by the first-step borrower to the Central Bank, we believe the whole billing procedure which requires the first-step borrower to be billed by AID should be reviewed. It appears that the procedure might be completely eliminated.

We have referred this finding to AG/AUD in Washington for further review and disposition.

Part V - GENERAL COMMENTS

An exit conference was held with Mission management on February 19, 1974 to discuss the findings contained in this report.

Three other audit reports include comments on two-step loans; report Nos. 2-510-71-112, 2-510-72-91 and 1-510-73-48. The reports indicate that the Mission is initiating conversations or is reaching agreements with the GOA on the use of the two-step funds. As pointed out in this report, no agreements have been reached and the funds have not been used.

8

TWO-STEP LOAN AGREEMENTS
 Status as of 12/31/73
 (Amounts in millions)

EXHIBIT A

Loan No.	Title	Borrower	Dated	Loan Amount in Dollars	Disbursed in dollars	Amount Generated in pesos
510-L-011	Grain Storage	Bco. Nación Argentina	1/9/69	10.0	3.1	1.4
510-L-012	Self-Help Housing	Prov. of Bs. As. Housing Inst.	9/1/63	2.0	2.0	3.6
510-L-013	Construction of Aftosa Lab.	INTA (Nat. Inst. of Agric. Technology)	5/24/66	1.4	1.3	0.9

LOAN TERMS

	<u>Borrower</u>		<u>Central Bank</u>		<u>Amortization</u>	
	Grace Period	Installments	Grace Period	Installments	1st. Payment Due Borrower	1st. Payment Due C. Bank
510-L-011	5 years	21	10 years	61	10/14/76	10/14/81
510-L-012	2 years	57	10 years	61	5/20/66	5/20/74
510-L-013	5 years	51	10 years	61	2/ 9/73	2/ 9/78

EXHIBIT B

Distribution of Audit Report

	<u>No. of Copies</u>
- USAID/Argentina	5
- Desk Officer ARA-LA/APU	1
- ARA-LA/OPNS	2
- AG/AUD	4
- AG/IIS Miami	1
- IGA/W	1
- AAG/LA Miami	1
- AG/AUD/PPP (Coded)	1
- ARA/LA/DR (Loan Officer)	1