

Regional Inspector General for Audit
Nairobi, Kenya

Audit of
USAID/Tanzania's Management of
Host Country-Owned Local Currency

Report No. 3-621-94-005
March 14, 1994





March 14, 1994

U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

MEMORANDUM

*Regional
Inspector General
for Audit/Nairobi*

TO : USAID/Tanzania Director, Dale B. Pfeiffer
FROM : RIG/A/Nairobi, Everette B. Orr *Everette B. Orr*
SUBJECT: Audit of USAID/Tanzania's Management of Host Country-Owned Local Currency

Enclosed are five copies of the subject audit report. Our audit work and written representations confirmed that USAID/Tanzania management responded positively to the new Agency guidance issued in 1991 on Managing Host Country-Owned Local Currency.

USAID/Tanzania has made excellent progress in implementing the new Agency guidance, although additional improvements could be made. For example, the Mission needs to amend its Mission Order to include detailed procedures for verifying the accuracy of reports received from banks managing special local currency accounts.

After extensive discussions with my staff, USAID/Tanzania withdrew its original comments on our draft report on February 17, 1994, but did not provide revised comments. Therefore, we consider the two recommendations unresolved. Please respond to this report within 30 days indicating any actions planned to implement the recommendations.

The representation letter you provided in conjunction with this audit was fully acceptable. As a result, this report contains no qualifying language on the positive aspects of the Mission's performance.

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

EXECUTIVE SUMMARY

Background

USAID issued Policy Determination No. 18 (PD-18) and supplemental guidance to provide better accountability and oversight over host country-owned local currency for non-project assistance. This policy was issued in July 1991 and superseded previous USAID policy and guidance and described controls over the generation, management, and programming of host country-owned local currency. Accountability standards for non-project assistance were provided in USAID's "Supplemental Guidance on Programming and Managing Host Country-Owned Local Currency" (the supplemental guidance) of June 1991. (See page 1.)

In Tanzania, local currency was generated under the Agricultural Transport Assistance Program (the Program) after the new policy became effective. This cash-transfer Program, designed to support policy reforms aimed at improving the Government of Tanzania's (the Government's) ability to rehabilitate and maintain its rural roads, has a \$46 million non-project component. Dollar assistance was to have been disbursed in tranches upon the satisfaction of specific Government policy reforms to allow for more private sector involvement in road maintenance. These dollars will be made available to private and public sector entities to import road construction equipment. In turn, private and public sector importers will deposit in a special local currency account the equivalent in Tanzanian shillings (Tsh.) of the dollar letter of credit value, using the commercial exchange rate in effect on the date deposits are made. As of May 31, 1993, importers had deposited about Tsh. 4.26 billion (\$13.6 million) into the special account; the Program is expected to generate a total of about Tsh. 14.4 billion (\$46 million) by the end of the Program on December 31, 1995. Ninety-five percent of the shillings generated from the \$46 million non-project assistance, plus any interest, will be used by the Ministry of Works to pay private contractors to rehabilitate and maintain rural roads. (See pages 1 and 2.)

Audit Objectives

The Office of the Regional Inspector General for Audit/Nairobi audited the Program as part of a worldwide audit of host country-owned local currency. Our field work was

conducted from June 28 through September 3, 1993¹, to determine whether USAID/Tanzania had followed USAID policy and the supplemental guidance in: (1) assessing the accountability environment in the host country, (2) designing the grant agreements and amendments to include specific requirements, (3) ensuring local currency generations were deposited and quickly disbursed, (4) ensuring local currencies were programmed and used for intended purposes, and (5) ensuring the impact of local currency programs were evaluated. (See pages 5, 7, 8, 13, and 14.)

Summary of Audit

The audit found that USAID/Tanzania had:

- (1) assessed the accountability environment in the host country;
- (2) included provisions in the grant agreement for
 - a special account,
 - the amount of dollar assistance and equivalent local currency to be deposited,
 - deposit of local currency in an interest-bearing account,
 - reporting on the special account, and
 - auditing the special account;
- (3) disbursed local currency consistent with sound programming;
- (4) adopted the specific sector programming option which is acceptable under PD-18; and
- (5) ensured the impact of the Program would be evaluated.

Although the Mission made considerable efforts to ensure local currency generated by the Program were deposited (see page 9), some shillings still need to be collected from importers and deposited into the special account. In addition, the Mission did not know for a time that the Cooperative and Rural Development Bank (the Bank) had not recorded in its general ledger books the interest earned on money in the special account. Consequently, the equivalent of \$396,889 in interest earnings had not been collected from importers and deposited into the special account. There is a potential for continued loss of interest earnings until the money from the importers is recovered. Also, the Bank had not properly accounted for an equivalent of \$4.9 million in interest. (See page 11.)

Summary of Recommendations

The report contains two recommendations to correct problem areas identified. First, the report recommends that USAID/Tanzania obtain a plan of action from the Ministry of

¹ Field work in Tanzania took place on two occasions: June 28 to July 16, and August 16 to September 3, 1993.

Finance to collect and deposit into the special account the equivalent of \$396,889 in interest earnings from importers. Second, the report recommends that USAID/Tanzania amend its Mission Order to include detailed procedures for verifying the accuracy of reports from banks managing special local currency accounts. (See page 11.)

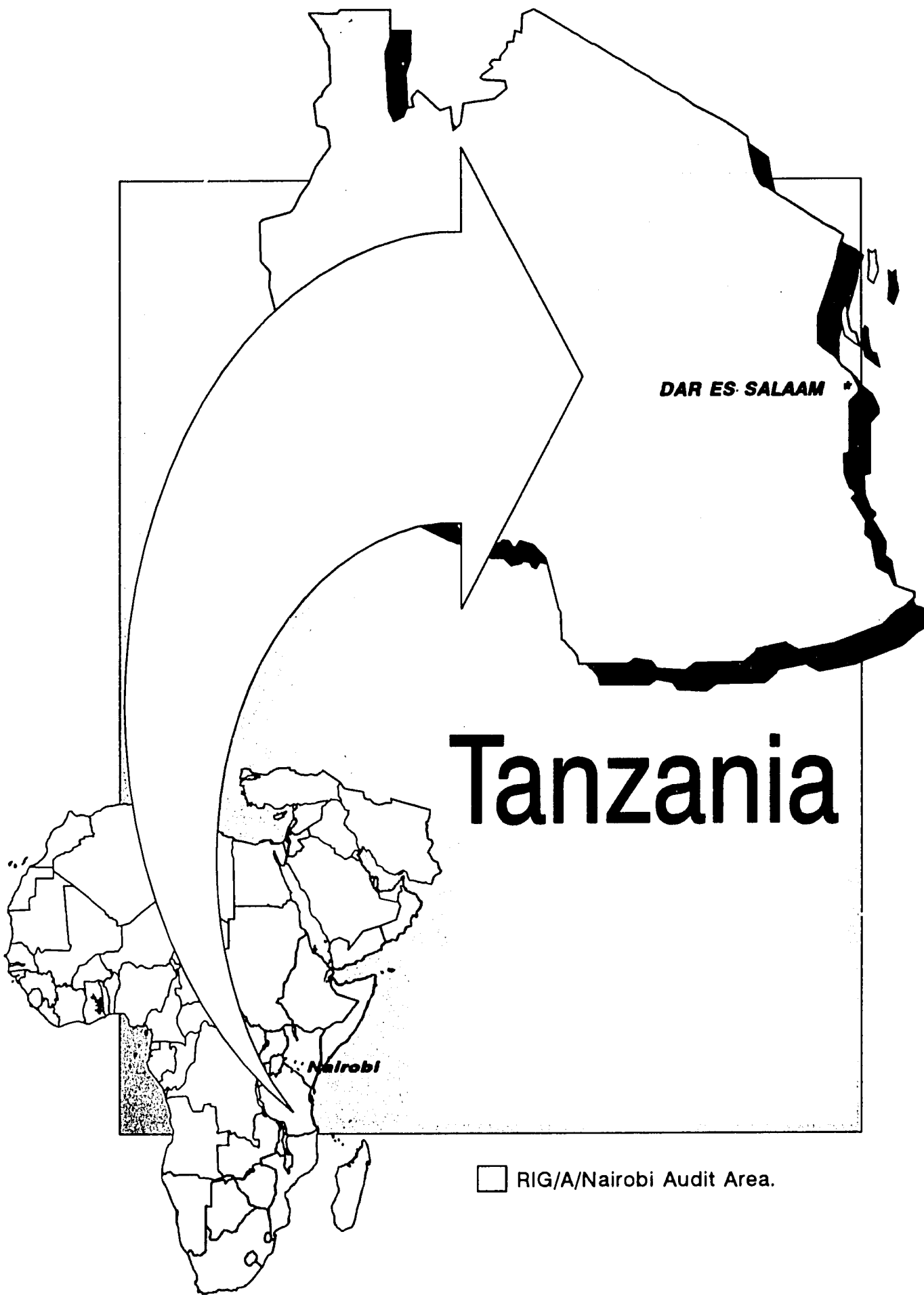
Management Comments

After extensive discussions with RIG/A/Nairobi staff, USAID/Tanzania withdrew its original comments on the draft report on February 17, 1994, but did not provide revised comments. Therefore, Recommendation Nos. 1.1 and 1.2 are unresolved.

Office of the Inspector General

Office of the Inspector General

March 14, 1994



DAR ES SALAAM *

Tanzania

Nairobi

RIG/A/Nairobi Audit Area.

TABLE OF CONTENTS

	Page
EXECUTIVE SUMMARY	i
INTRODUCTION	
Background	1
Audit Objectives	2
REPORT OF AUDIT FINDINGS	
USAID/Tanzania assessed the accountability environment in the host country as required by USAID policy and supplemental guidance.	5
USAID/Tanzania designed the grant agreement and amendments in accordance with USAID policy and supplemental guidance.	7
USAID/Tanzania ensured that local currency generations were deposited and disbursed as required by USAID policy and supplemental guidance.	8
Positive Management Actions Ensured That Local Currencies Were Accounted For	9
Not All Interest Earned Had Been Accounted For	11
USAID/Tanzania ensured that local currencies were programmed and used for the intended purposes as required by USAID policy and supplemental guidance.	13
USAID/Tanzania ensured that the impact of the local currency programs will be evaluated in accordance with USAID policy and supplemental guidance.	14
MANAGEMENT COMMENTS	15
APPENDICES	
Appendix I - Scope and Methodology	17
Appendix II - Report Distribution	20

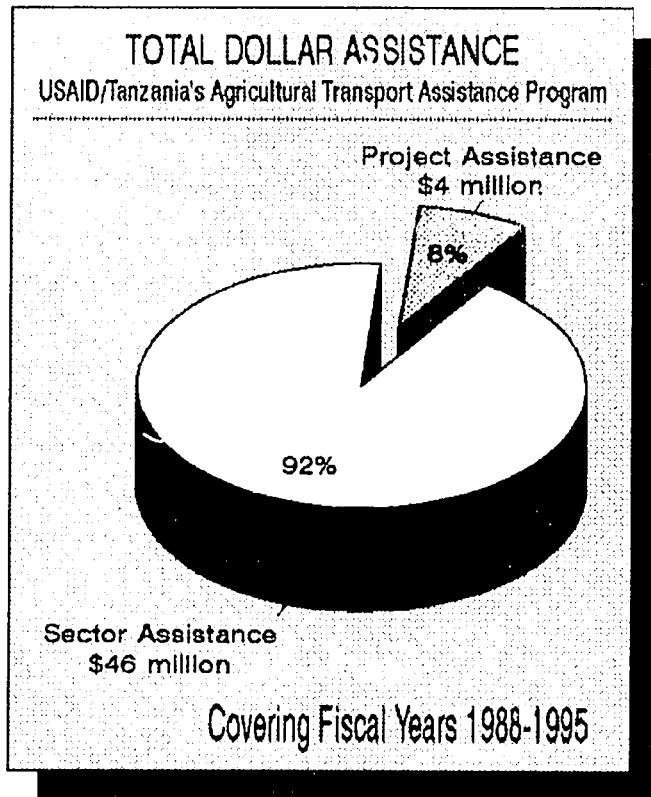
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INTRODUCTION

Background

Host country-owned local currency has been long recognized as an area of vulnerability in the USAID economic assistance program. The USAID Inspector General (IG) and the General Accounting Office (GAO) have reported on problems with USAID's oversight and accountability of local currency, including managing special local currency accounts and ensuring local currency is used for agreed-upon purposes. As a result, USAID issued detailed guidance to address the weaknesses in oversight and accountability.

In July 1991, USAID revised its policy on host country-owned local currency by issuing Policy Determination No. 18 (PD-18). This policy superseded both Policy Determination No. 5 of 1983 and its supplemental guidance of 1987. PD-18 describes controls over the generation, management, and programming of host country-owned local currency. Most importantly, it prescribes accountability standards for non-project assistance as explained in USAID's "Supplemental Guidance on Programming and Managing Host Country-Owned Local Currency" (the supplemental guidance) of June 1991.



In Tanzania, local currency was generated under the Agricultural Transport Assistance Program (the Program) after the new policy became effective on July 1, 1991. The cash-transfer Program is designed to support policy reforms aimed at improving the Government of Tanzania's (the Government's) ability to rehabilitate and maintain its rural roads. To do this, the Program is divided into 2 parts: (1) a \$46 million, non-project

assistance component, and (2) a \$4 million technical assistance and training component.²

The \$46 million non-project assistance was to have been disbursed in tranches upon the satisfaction of specific Government policy reforms to allow more private sector involvement in road maintenance. Since September 1991, these dollars have been made

USAID/TANZANIA'S AGRICULTURAL ASSISTANCE TRANSPORT PROGRAM <i>(Total actual and proposed obligations under the Program)</i>		
Fiscal Year	Non-Project Assistance Obligations (\$ in Millions)	Project Assistance Obligations (\$ in Millions)
1988	5.21	2.0
1989	5.20	0.0
1991	17.59	2.0
1992	8.65	0.0
1993	3.00	0.0
1994	3.00	0.0
1995	3.35	0.0
TOTAL	46.00	4.0

available to private and public sector entities to import road construction equipment. In turn, the importers were to have deposited in a special local currency account with the Cooperative and Rural Development Bank (the Bank) the equivalent value in Tanzanian shillings (Tsh.) of the dollar letter of credit, using the commercial exchange rate in effect on the date deposits were made. As of May 31, 1993, importers had deposited about Tsh. 4.26 billion (\$13.6 million) into the special account. The Program is expected to generate a total of about Tsh. 14.4 billion (US\$46 million) by the December 31, 1995 program end.

Ninety-five percent³ of the shillings generated from the

\$46⁴ million non-project assistance and any interest earned by the special account is to be used by the Ministry of Works to pay private contractors to rehabilitate and maintain rural roads. USAID, the Ministry of Finance, and the Ministry of Works will jointly decide use of the shillings for the Program. In addition, \$4 million of project assistance

² The program grant agreement for the Agricultural Transport Assistance Program was signed on August 31, 1988. The third amendment of the Program grant agreement, dated August 30, 1991, restated the agreement in its entirety to reflect the change from a commodity import program to a sector assistance cash transfer. The third amendment reobligated \$10.41 million, which was the amount deobligated by the second amendment dated May 23, 1991.

³ The fifth amendment to the program grant agreement required an equivalent of not less than 10 percent of the \$12.59 million third and fourth tranche (2 of 3 tranches from fiscal year 1991 obligations), and 10 percent of the \$8.65 million fifth tranche be deposited into the USAID trust account.

⁴ This is net of the Government's deposit of the shilling equivalent of \$732,715 for USAID trust fund as of May 31, 1993.

will provide for technical assistance, training, and commodities to support policy reforms under the Program.

Audit Objectives

The Office of the Regional Inspector General for Audit/Nairobi audited USAID/Tanzania's Management of Host Country-Owned Local Currency (specifically, USAID/Tanzania's Agricultural Transport Assistance Program) as part of a worldwide audit of host country-owned local currency. USAID/Tanzania was selected for audit because it was one of those missions which were further along in implementing the new policy. The Program was selected for audit because it was one of two⁵ non-project assistance agreements in USAID/Tanzania signed after July 1, 1991, the date PD-18 and the supplemental guidance became effective. Our field work was conducted from June 28 through September 3, 1993⁶, to answer the following questions:

1. **Did USAID/Tanzania assess the accountability environment in the host country as required by USAID policy and supplemental guidance?**
2. **Did USAID/Tanzania design the grant agreements and amendments in accordance with USAID policy and supplemental guidance?**
3. **Did USAID/Tanzania ensure that local currency generations were deposited and quickly disbursed as required by USAID policy and supplemental guidance?**
4. **Did USAID/Tanzania ensure that local currencies were programmed and used for the intended purposes as required by USAID policy and supplemental guidance?**
5. **Did USAID/Tanzania ensure that the impact of the local currency programs will be evaluated in accordance with USAID policy and supplemental guidance?**

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

⁵ USAID/Tanzania signed the Finance and Enterprise Development Project, Project 621-0175 on August 28, 1992. RIG/A/Nairobi first learned of this fact on receipt of Mission comments to the draft audit report dated November 22, 1993. As a result, the Finance and Enterprise Development Project was not included in our field work.

⁶ Field work in Tanzania took place on two occasions: June 28 to July 16, and August 16 to September 3, 1993.

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REPORT OF AUDIT FINDINGS

Did USAID/Tanzania assess the accountability environment in the host country as required by USAID policy and supplemental guidance?

USAID/Tanzania assessed the accountability environment in the host country as required by USAID policy and supplemental guidance.

Section 2.3 of USAID's "Supplemental Guidance on Programming and Managing Host Country-Owned Local Currency" (the supplemental guidance) requires an assessment of the general accountability environment in the host country to ensure accountability for host country-owned local currency. Missions are required to examine factors such as:

- the general financial management capabilities of the host government;
- the quality of accounting and financial management personnel within the host government;
- the systems in place to allocate and expend funds;
- the external economic factors which might influence the use of local currency; and
- the mission's prior experience with ensuring accountability for USAID resources and local currency in that country.

In addition, section 2.5 of the supplemental guidance requires each Program Assistance Approval Document (PAAD) to include as part of the financial analysis section a detailed assessment of appropriate programming alternatives available to the mission based on the general assessment. If the mission's conclusion, documented in the PAAD, is that the implementing agency is unable to manage the special account, the mission should consider technical assistance or other means to strengthen the agency's capabilities prior to disbursement of funds.

According to section 5.1.A.1 of the supplemental guidance, if an agency or host government unit which has not previously managed a special account is to be responsible, a formal financial assessment should be performed. Further, if a host government agency has managed a special account previously and has a poor record (as indicated by things such as negative audits, or untimely, incomplete or inaccurate reports), then a formal financial assessment should be performed. That is, the accounting and financial

systems of the agency should be reviewed in order to determine whether sufficient personnel, systems, and internal controls exist to adequately manage the special account. However, if the designated host government agency has good experience in managing special accounts, then the mission may choose to rely on an informal assessment.

As required by the supplemental guidance, USAID/Tanzania conducted a general assessment of Tanzania's accountability environment in July 1991. The assessment expressed no confidence in the Government of Tanzania's (the Government's) implementing agencies' ability to maintain accountability of USAID funds. The Mission did not assess the Government's budgeting and reporting systems to ascertain its ability to accurately report budget allocations and expenditures from the General Fund. Based on this, the Mission felt it had no basis with which to express an opinion on the Government's budgeting and financial management systems.

The Mission also did not formally assess the accounting and financial systems of the agencies involved with the Agricultural Transport Assistance Program (the Program). These agencies included the Ministry of Finance, the Ministry of Works, and the Cooperative and Rural Development Bank (the Bank). USAID/Tanzania officials said they did not feel it necessary to conduct a formal assessment of the accounting and financial management systems of the two ministries because their general assessment had already concluded the Government's financial management systems were not reliable. In making the decision not to assess the Bank's management systems, USAID/Tanzania officials relied on a review of the predecessor program, the Africa Economic Policy Reform Program (the Reform Program), conducted by Deloitte Haskins & Sells in 1990, which concluded the Bank was effectively managing program accounts.

Did USAID/Tanzania design the grant agreements and amendments in accordance with USAID policy and supplemental guidance?

USAID/Tanzania designed the grant agreement and amendments in accordance with USAID policy and supplemental guidance.

Section 4.2 of Policy Determination No. 18 (PD-18) and section 3.0 of the supplemental guidance require local currency to be deposited into a special account for joint programming. Also, section 3.1 of the supplemental guidance requires the grant agreement to contain the value of dollar assistance which will be used to generate local currency, as well as, the exchange rate to be used to express that amount in terms of local currency. According to section 5.6 of PD-18 and section 5.2 of the supplemental guidance, local currency should be placed in interest-bearing accounts. In addition, according to section 6.3 of PD-18 and sections 5.1.B of the supplemental guidance, the program grant agreement must provide for appropriate reporting by the host government agency responsible for managing the special account. Further, section 6.3 of PD-18 requires that a provision for audit of the special account be included in the agreement.

Following the requirements of PD-18 and the supplemental guidance, USAID/Tanzania included these provisions in the grant agreement:

- establishment of a separate local currency account for the Program;
- generation of local currency from the whole dollar assistance under this grant, and the requirement that the amount of local currency to be deposited shall be determined by using the highest lawful rate of exchange on the date deposits are made;
- deposit of local currency into an interest-bearing account;
- quarterly reporting on deposits into and disbursements from the special account; and
- annual audits of the special local currency account by an independent auditor.

Did USAID/Tanzania ensure that local currency generations were deposited and quickly disbursed as required by USAID policy and supplemental guidance?

USAID/Tanzania ensured that local currency was generated and deposited into a separate interest-bearing account and disbursed consistent with sound programming as required by USAID policy and supplemental guidance. Although not all local currency had been collected, the Mission had taken steps, including initiating an Agency-contracted audit, to ensure the uncollected amounts of local currency were accounted for, recovered, and deposited into the special account. While these actions were very positive, the Bank had not deposited some interest earnings, and other interest earnings had not been entered in the Bank's general ledger books.

According to section 4.2 of PD-18 and section 3.0 of the supplemental guidance, local currency should be deposited into a special account for joint programming. Also, according to section 5.6 of PD-18 and section 5.2 of the supplemental guidance, USAID policy requires local currency be placed in interest-bearing accounts. Further, section 3.1 of the supplemental guidance requires the grant agreement to contain the dollar assistance which will generate local currency and the exchange rate that will be used to express that amount in terms of local currency. Finally, section 5.6 of PD-18 states that programmed local currency should be disbursed as quickly as is consistent with sound management and prevailing economic conditions in the recipient country.

As required by the above policy, USAID/Tanzania made sure local currency generated by the Program was deposited into a separate interest-bearing account at the Bank. A total of Tanzanian shillings (Tsh.) 4.26 billion (\$13.6 million) was generated and deposited into this account as of May 31, 1993. Also, following USAID policy, the grant agreement contained the dollar assistance amount to be used to generate the shillings and the rate of exchange to be applied. Further, the shillings were disbursed consistent with sound management practices.

The first deposit into the Program's special account was in September 1991, and the first disbursement was in May 1993. The Agricultural Transport Assistance Program's shillings were not used during this period because of an overlap between the predecessor program, the Africa Economic Policy Reform Program (the Reform Program), and the new Agricultural Transport Assistance Program. Local currency generated from both programs were to be used for the same purpose, rehabilitation of rural roads. The Reform Program's balance of about \$8.3 million (Tsh. 2.6 billion) had to be depleted before the Agricultural Transport Assistance Program's shillings could be used. Any adverse effect of the new Program's shillings remaining idle during that period, such as a loss in purchasing power, was negated by interest earnings.⁷ In addition, time was needed for the new Program to generate shillings and build up the private sector

⁷ The rate of inflation during this period was about 23 percent per annum, the bank interest rate was 16 percent.

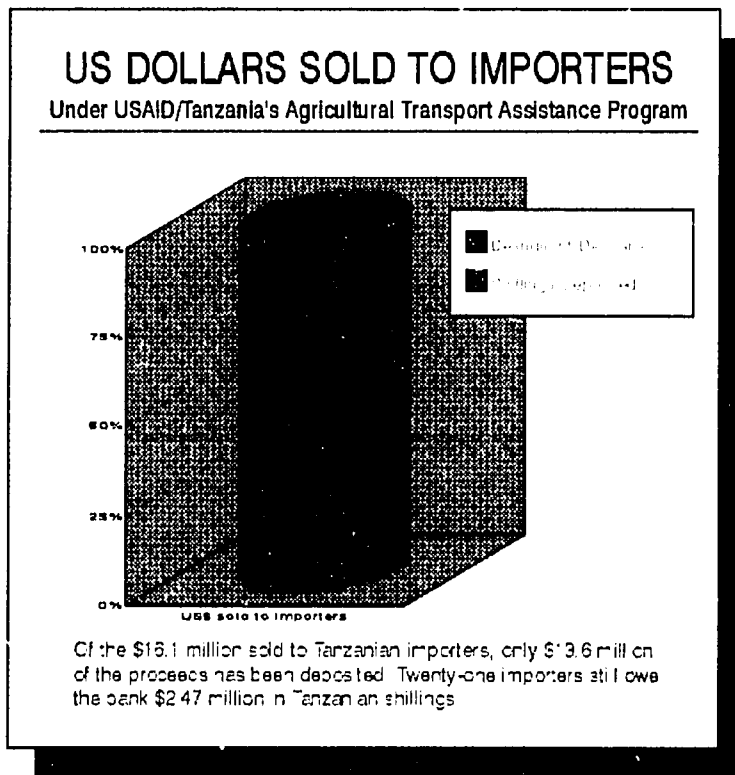
construction capability for rural road rehabilitation.

As discussed below, the Mission made considerable efforts to ensure local currency proceeds were deposited, although some shillings still need to be collected from importers. Also, interest earnings had not been recorded in general ledger books at the Bank from September 1991 to January 1993.

**Positive Management Action Ensured
That Local Currencies Were Accounted For**

According to section 4.2 of PD-18, local currency generations should be deposited into a special account for joint programming by USAID and the host country. Also, section 3.1 of the supplemental guidance states that USAID and the host government must specify in the grant agreement the exact amount of the dollar assistance which will be used to generate local currency and the rate of exchange to be applied.

The grant agreement provided that local currency for the Program was to be generated from the total dollar assistance using the highest lawful rate of exchange on the date deposits were made. As of May 31, 1993, \$28 million had been transferred to the Government under the Program, of which, importers received about \$16.1 million to buy road construction equipment. According to the grant agreement, the local currency equivalent of \$16.1 million (Tsh. 5.0 billion) should have been deposited into the special



account. However, as of May 31, 1993, the importers had deposited only about Tsh. 4.26 billion (\$13.6 million) into the special account. The difference of about Tsh. .7 billion (\$2.47 million) was still owed by 21 importers as of June 1993.

The above amount is owed by importers because the Bank did not closely monitor deposits into the special account. The Mission has been concerned with the Bank's management of the special account since the beginning of 1992 and had taken actions to correct these problems and to improve the Bank's performance. For instance, in early

1992, USAID/Tanzania contracted for an audit of the special accounts for the Reform Program and the Agricultural Transport Assistance Program (Audit Report No. 3-621-92-15-N dated July 31, 1993). The audit identified major internal control weaknesses in the management of the special account, as well as, an unreconciled difference of \$2.6 million (about Tsh. 819 million). In response to this audit, the Mission: (1) suspended the Program for four months while these problems were being corrected, (2) contracted with Peat Marwick to design and monitor the implementation of a new accounting system for the Bank (the system was put in place in July 1992 and Peat Marwick has been monitoring its implementation since October 1992), and (3) contracted with Peat Marwick to reconcile the special account.

The reconciliation of the special account was done in February 1993. Peat Marwick found that 21 importers had not made sufficient deposits to the shilling accounts of the two programs amounting to a deficiency of about \$2.47 million. On April 8, 1993, the Mission sent letters to the 21 importers informing them of the amounts owed. In addition, on June 14, 1993, the Mission wrote to Bank officials informing them that although the importers owed the shillings to the Government, the Bank was responsible for collecting the money because of their contractual relationship with the importers. Furthermore, the Mission started screening applicants to the Program to keep the delinquent importers from receiving further funding under USAID programs, and notified members of the donor community these importers owed money to USAID.

In spite of these actions, the Bank managed to collect and deposit only the equivalent of about \$55,000 (Tsh. 17.2 million) by the beginning of the audit on June 28, 1993. However, according to Mission officials, the Bank did collect and deposit the equivalent of \$666,276 (Tsh. 321.1 million) as of December 31, 1993, leaving an outstanding balance of about \$1.1 million⁸ (Tsh. 530.5 million). There is a potential for loss of interest earnings until the money owed is collected from the importers.

While these actions are very positive, some work remains to properly account for interest earned on local currency deposits.

Not All Interest Earned Had Been Accounted For

Section 4.2 of PD-18 requires local currency generations to be deposited into a special account for joint programming by USAID and the host country. Also, USAID policy

⁸ USAID/Tanzania agreed to the Government's request to denominate the \$2.47 million debt owed in Tanzanian shillings (Tsh.) rather than dollars. As a result of devaluation of the shilling from September 1991, the amount owed by importers is the equivalent of \$1,370,255, plus accrued interest of \$396,889. The amount outstanding is about \$1.1 million (\$1,370,255 plus \$396,889 minus \$666,276). The dollar amount owed and the interest owed was calculated using a rate of Tsh. 481 to US \$1, which was the rate in effect December 31, 1993.

requires local currency be placed in interest-bearing accounts with any interest earned used in the program. However, interest had not been collected from the delinquent importers. In addition, the Mission did not detect that the Bank had not recorded the interest earned on shillings in the Program's special account. This happened because (1) the Bank had not closely monitored deposits to the special account, (2) the Mission had not formally communicated to the Government the issue of interest owed by delinquent importers, and (3) USAID/Tanzania had not formalized procedures for monitoring local currency generations, including verification of Bank reports. Consequently, the equivalent of \$396,889 in interest had not been collected, and the Bank was delinquent in accounting for Tsh. 1.5 billion (about \$4.9 million) in interest.

Recommendation No. 1: We recommend that USAID/Tanzania:

- 1.1 obtain a plan of action from the Ministry of Finance, in conjunction with the Customs Department and the Cooperative and Rural Development Bank, to collect and deposit into the special account the equivalent of \$396,889⁹ in interest earnings owed by importers.**
- 1.2 amend Mission Order No. 10-22 to include detailed procedures for verifying the accuracy of reports received from banks managing special local currency accounts.**

According to section 4.2 of PD-18, local currency generations should to be deposited into a special account for joint programming by USAID and the host country. Also, section 3.1 of the supplemental guidance states that USAID and the host government must specify in the grant agreement the total amount of the dollar assistance which will generate local currency. In addition, according to section 5.6 of PD-18 and section 5.2 of the supplemental guidance, USAID requires local currency be placed into interest bearing accounts in deposit-taking institutions, with any interest used within the program, so long as such accounts are permitted under host country laws and regulations and do not undermine internationally-supported stabilization agreements and sound monetary policy.

The program grant agreement was properly worded to require the local currency generated from the dollar assistance be deposited into a special interest-bearing account. As of May 31, 1993, dollar disbursements to importers totaled \$16.1 million, which should have generated about Tsh. 5.0 billion. However, importers had only deposited Tsh. 4.26 billion (\$13.6 million) into the special account. The equivalent of about \$2.47 million (Tsh. .7 billion) was still outstanding at the time of the audit and would have earned the equivalent of \$396,889 in interest by December 31, 1993.

⁹ This is the amount of accrued interest agreed on by USAID/Tanzania and the Government of Tanzania using the exchange rate in effect December 31, 1993. However, assuming the exchange rate remains fairly stable, the exact amount of the dollar equivalent will most likely be higher because the agreement requires the amount owed by importers to continue to accrue interest at 17 percent until paid.

This happened because the Bank had not closely monitored the special account. Also, the Mission had not formally communicated to the Government that money in this special account, and any delinquent money owed, should earn interest. If the Mission had, the Government could have instructed the Bank to collect interest on Program funds. As a result, the Bank had not collected the equivalent of \$396,889 in interest from the 21 delinquent importers. Also, there is the potential for continued loss of interest earnings until the delinquent funds are recovered.

We are not making any recommendations to USAID/Tanzania on problems with the Bank because of actions the Mission has already taken to improve the management of the special account. (See page 9.) However, we are recommending that the Mission obtain a plan of action from the Program's implementing agencies for collecting the \$396,889 interest owed by importers.

As a related, but separate issue, the Bank had not properly recorded in its general ledger books interest earnings of Tsh. 1.5 billion (about \$4.9 million) on deposits into the Program's special account between September 1991 and April 1993. This problem was not detected for nearly a year and a half because the Mission was not given bank statements on the account. The Mission conducted a review in January 1993 to verify the accuracy of the Bank's monthly reports¹⁰ and found a significant discrepancy in the amount of interest reported. In response, the Mission reconstructed the amount of interest that should have been credited to the special account from the date of the first deposit in September 1991 to April 1993. Based on the results of this review, the Mission concluded the Bank failed to record in its general ledger books interest earnings of Tsh. 1.5 billion. The correct account balance should have been Tsh. 3.7 billion, not the Bank's reported balance of Tsh. 2.2 billion. On May 21, 1993, the Mission informed the Bank about the discrepancy and requested Tsh. 1.5 billion be entered into the general ledger books. The Bank agreed, and posted the required entries on July 5, 1993. In our opinion, this problem was detected more by chance than through the application of formalized local currency management procedures. If the Mission had followed such procedures, this discrepancy would have been detected earlier. As discussed below, the Mission needs to establish detailed management procedures, and utilize them, to ensure timely detection of local currency problems in the future.

During our second visit to Tanzania, the Mission issued Mission Order No. 10-22 dated August 25, 1993, for local currency management. The purpose of the Mission Order was to establish Mission procedures which fully comply with the requirements of PD-18 and supplemental guidance. However, our review of the Mission Order showed a lack of detailed procedures requiring Mission personnel to verify the accuracy of information provided by the Bank on shilling deposits and interest earned. Therefore, we concluded that USAID/Tanzania needs to amend Mission Order No. 10-22 to require:

¹⁰ The Bank had not provided USAID/Tanzania monthly bank statements showing the amount of interest credited to the special account from inception of the Program in September 1991 through January 1993.

- the Bank to provide monthly reports and bank statements to USAID/Tanzania; and
- Mission personnel to check, at least quarterly, the Bank's project and general ledger books against these reports to ensure interest earned on the special accounts has been properly recorded.

We believe following these procedures would require very little time and effort, but would significantly increase accountability. This latter point is especially important given the Mission's own general assessment that the Government's financial management systems are unreliable and that the Mission must be intimately involved in the management of special accounts.

These accountability problems occurred for two reasons. First, the Bank had not closely monitored the special account. Again, we are not making any recommendations to USAID/Tanzania on problems with the Bank because of actions the Mission has already taken to improve the management of the special account. (See page 9.) Second, USAID/Tanzania had not formalized procedures for monitoring shillings generated by the Program, including verification of Bank reports. As a result, the Mission did not know for a time the Bank had not properly accounted for Tsh. 1.5 billion (about \$4.9 million) in interest. We are recommending improvements to Mission procedures (Mission Order No. 10-22 dated August 25, 1993) for verifying reports from the Bank.

Did USAID/Tanzania ensure that local currencies were programmed and used for the intended purposes as required by USAID policy and supplemental guidance?

USAID/Tanzania ensured that local currencies were programmed and used for the intended purposes as required by USAID policy and supplemental guidance.

According to section 6.1 of the supplemental guidance, local currency generated by USAID programs can be used for budget support (which includes general budget support, general sector support, and specific sector support) and extra-budgetary activities (which includes projects or activities funded outside of the host country's budget). USAID/Tanzania programmed all local currency generations from the three tranches amounting to \$28 million, less deposits into the USAID trust fund, for specific sector support following USAID policy.

Section 5.1.B.1 of the supplemental guidance states that if the special account is to be audited by the host country audit agency, the PAAD should contain a discussion of the audit agency's ability to conduct an independent, fair and impartial audit. The Program's PAAD and amendments did not contain a discussion as required by the supplemental guidance. However, we did not consider this to be significant because (1)

USAID/Tanzania included provisions in the grant agreement for auditing the special account by an independent auditor¹¹ and (2) USAID/Tanzania and RIG/A/Nairobi are assessing the Auditor General's ability to conduct audits under the recipient-contracted audit program. According to Mission officials, USAID/Tanzania is now working with the Auditor General to schedule an annual audit of the special account¹².

Did USAID/Tanzania ensure that the impact of the local currency programs will be evaluated in accordance with USAID policy and supplemental guidance?

USAID/Tanzania ensured that the impact of the local currency program will be evaluated in accordance with USAID policy and the supplemental guidance.

According to section 7.0 of the supplemental guidance, missions are expected to develop, in collaboration with the host country, performance indicators to guide their programming of local currency by measuring the tangible results of the program. These performance indicators must be verifiable. The supplemental guidance provides further clarification on the nature of performance indicators and states that these indicators, like monitoring responsibilities, reflect the complexity of the program. Thus, performance indicators for projects will likely be very specific measures of project outputs. On the other hand, those for general sector support may simply demonstrate an increase in the level of funding for a sector.

USAID/Tanzania developed performance indicators for evaluating the impact of the local currency program and included them in the Program's PAAD. The grant agreement provided for evaluations at mid-program and again at the end of the program. Also, the grant agreement also provided for updates to a baseline survey undertaken in 1991. A mid-program evaluation was conducted in August 1993 by the Regional Economic Development Services Office for East and Southern Africa.

¹¹ A reconciliation of the special account was performed by Peat Marwick in February 1993.

¹² USAID/Tanzania scheduled this audit to begin February 1, 1994. The audit will cover the period January 1, 1992, to June 30, 1993. This audit will cover an 18-month period so the Mission can convert to the Government of Tanzania's fiscal year which ends on June 30.

MANAGEMENT COMMENTS

After extensive discussions with RIG/A/Nairobi staff, USAID/Tanzania withdrew its original comments on our draft report on February 17, 1994, and we requested the revised comments no later than March 11, 1994. As of the date of this report, USAID/Tanzania did not provide revised written comments.

Our office provided USAID/Tanzania with a draft report on November 22, 1993, and requested Mission officials to provide comments no later than December 18, 1993. At USAID/Tanzania's request, we extended that deadline to the first week in January. USAID/Tanzania provided written comments on January 19, 1994.

Although we did not receive final Mission comments in this instance, we are confident that we have considered their position and have reported all of the issues fairly and objectively. We made revisions to the draft report based on extensive discussions with Mission officials and on our analysis of their original comments. However, we believe that further delaying this report is not warranted nor would it be an effective use of time for either RIG/A/Nairobi or USAID/Tanzania.

The representation letter USAID/Tanzania provided on this audit was acceptable. As a result, this report does not contain any qualifying language on the positive aspects of the Mission's performance.

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APPENDICES

SCOPE AND METHODOLOGY

Scope

We audited USAID/Tanzania's Management of Host Country-Owned Local Currency in accordance with generally accepted government auditing standards. We conducted the audit from June 28 to September 3, 1993¹³, in the offices of USAID/Tanzania and concentrated on the Agricultural Transport Assistance Program (the Program). The Program's non-project assistance agreement was signed after July 1, 1991, the effective date of Policy Determination No. 18 (PD-18) and State cable No. 204855 entitled "Supplemental Guidance on Programming and Managing Host Country-Owned Local Currency" (the supplemental guidance) of June 1991.

In performing our audit, we obtained documentary and testimonial evidence from the offices of USAID/Tanzania, the Government of Tanzania's Ministry of Works, and the technical assistance contractor at the Ministry of Works. The audit covered the systems and procedures relating to (1) assessing the accountability environment in the host country, (2) designing of the grant agreement and amendments, (3) depositing and quickly disbursing local currency generations, (4) programming and using local currencies for intended purposes, and (5) evaluating the impact of the local currency program.

According to USAID/Tanzania's records, a total of about \$36.65 million was obligated for the Program, and about \$28 million disbursed as of May 31, 1993. The audit covered the entire local currency equivalent of about \$16.1 million¹⁴ (about Tanzanian shillings (Tsh.) 5.0 billion) that should have been deposited into the special account as of May 31, 1993, and the entire equivalent of about \$1.1 million (Tsh. 500 million) withdrawn at the time of the audit.

As part of this audit, we reviewed USAID/Tanzania's internal control assessment. We

¹³ Field work in Tanzania took place on two occasions: June 28 to July 16, and August 16 to September 3, 1993.

¹⁴ The audit did not cover the Government's deposit of Tanzanian shilling equivalent of \$732,715 (Tsh. 229 million) to the USAID trust fund as of May 31, 1993.

also reviewed six prior RIG/A/Nairobi audit reports relating to host country-owned local currency: (1) Audit Report Nos. 3-632-93-11 (Audit of USAID/Lesotho's Management of Host Country-Owned Local Currency), (2) 3-696-93-08 (Audit of USAID/Rwanda's Management of Host Country-Owned Local Currency), (3) 3-612-92-14 (Audit of Malawi Enterprise Development Program), (4) 3-615-92-03 (Audit of Kenya Commodity Import Programs), (5) 3-687-92-01 (Audit of Madagascar Sector Assistance Programs), and (6) 3-613-90-06 (Audit of Local Currency Generations Under USAID/Zimbabwe Programs). We also reviewed prior audit findings on USAID/Tanzania's Africa Economic Policy Reform Program contained in Audit Report No. 3-621-92-15-N dated July 31, 1992.

We did not test the reliability of computer-generated data used in the report because: (1) the reliability of the data was not crucial to accomplishing the audit objectives, and (2) computer-generated data has been used only to a limited extent, e.g. for background and informational purposes.

Methodology

The methodology to accomplish these audit objectives included:

- reviewing the Mission's assessment of the host government's accountability environment, the Program Assistance Approval Document (PAAD) and amendments;
- confirming that provisions on generating, programming, and managing host country-owned local currency required by PD-18 and the supplemental guidance were included in the Program's grant agreement;
- confirming that a special account was established as required by PD-18 and the supplemental guidance, that local currency generated by the Program (about Tsh. 4.26 billion) was deposited into an interest-bearing account, and that withdrawals amounting to Tsh. 500 million (about \$1.4 million) were made as of May 31, 1993;
- confirming that the programming method used by USAID/Tanzania was one of the four programming methods options given by PD-18, and discussing with USAID/Tanzania officials methods used to ensure the shillings were used for intended purposes;
- reviewing Ministry of Works supporting documentation for Tsh. 162 million (about \$451,679), out of Tsh. 500 million disbursed, to determine what goods and services were bought, and confirming that USAID/Tanzania used audits to ensure the shillings were used for authorized purposes;

Appendix I

Scope and Methodology

- reviewing the grant agreement and the PAAD, identifying verifiable performance indicators, and discussing with USAID/Tanzania officials how these indicators would be measured; and
 - confirming that USAID/Tanzania had made provision for the evaluation of the Program.
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Appendix II
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