The Audit of the Conversion of Foreign Exchange in Liberia

CASE NUMBER TWO: COMMODITY IMPORT PROGRAM PROJECT NO. 669-0214

Audit Report No. 7-669-90-12
July 27, 1990

AGENCY FOR INTERNATIONAL DEVELOPMENT
Office of the Regional Inspector General for West Africa

July 27, 1990

MEMORANDUM

TO : D/USAID/LIBERIA, AFRICA BUREAU, John Roberts

Larry J. Hoover

FROM : ACTING RIG/A/DAKAR, Larry L. Hoover

SUBJECT: Audit of the Conversion of Foreign Exchange in Liberia --Case Number Two--

The Commodity Import Program
Project No. 669-0214

Enclosed are five copies of the subject report. This is the second of three reports issued during this audit. The policy of the Office of the Regional Inspector General is to request and include formal comments from the Mission prior to issuing the final report. In this case, a copy of the draft report was sent to and received by the Mission in Monrovia in the latter part of May.

As you are aware, no formal comments were provided by the Mission staff before they were relocated to Washington in early June. U.S. Government personnel were removed from Monrovia to assure their safety while a civil war is being waged between the incumbent government and another political faction. While I know that it is not possible to act on the recommendation in the report at this time, I believe it is important that the report be issued so that the Mission can develop a strategy and, upon returning to Liberia, immediately comply with the recommendation on page 2 of the report. Immediate action will forego the loss of future interest and maximize the benefits that can be derived from an eroding Liberian Dollar.

The recommendation is considered unresolved and will remain so until you review the report and respond with formal comments. My office is available to work with the Mission to resolve the recommendation. An overall report on the foreign exchange issue involving various modes of assistance will follow later. We appreciate the cooperation and courtesies extended to our staff during the audit.

Background

The shortage of foreign currency and maintenance of a totally unrealistic exchange rate in Liberia has made it difficult for everyone--particularly small-scale enterprises

--to finance their imported commodities. The CIP for Liberia, started in 1987, was a USAID initiative to finance the U.S. Dollar costs of these commodities and then resell them to the Program's participants for local currency equal to the U.S. Dollar costs at the official exchange rate of one to one. The Liberian Government and USAID then jointly decided for which developmental activities this local currency was to be spent.

The primary focus of the CIP program was to assist the private sector, particularly small-scale producers and firms developing an export capability. Sixty-five percent (65%) of available U.S. Dollar funding was allocated to the private sector and thirty percent (30%) to the public sector. The remaining five percent (5%) was used to administer the CIP. According to USAID officials, this program was quite popular in Liberia because the participants were able to buy the commodities effectively at about half their value due to the unofficial exchange rate of two Liberian dollars to one U.S. Dollar.

Audit Objective and Finding

Did USAID/Liberia follow A.I.D. Policy Guidelines in handling the CIP program funds by depositing the local-currency proceeds in an interest-bearing account and by disbursing them quickly?

USAID did not comply with A.I.D. policies for handling CIP local currency due partially to the unresponsiveness of the Liberian government. Since June 1988, the CIP program has accumulated 4 6 million Liberian dollars in a non-interest-bearing account at Citibank, Monrovia. During that period, there were no disbursements and the purchasing power of the Liberian dollar eroded by more than 50 percent due to the continued rise of the parallel exchange rate. It is likely that this erosion will continue because the Liberian Government has not developed any sound economic and monetary policies to stop it.

Recommendation: **We recommend that the Director, USAID/Liberia:**

A. **Immediately transfer the CIP-generated local currency funds to interest-bearing accounts in an appropriate bank and make firm plans to disburse these funds;**

B. **Initiate no further CIP projects until all disbursements of these local currency funds are completed; and**

C. **Establish a mission policy that requires future CIP agreements stipulate that local currencies be placed in interest-bearing accounts and that local currencies be disbursed within a specific time period after which the funds revert to direct USAID control.**

Discussion

The CIP account was established in 1988 at Citibank in Monrovia to receive Liberian dollars generated by the sales of USAID imported commodities to local businesses and the Government of Liberia. At this time, the Liberian dollar was trading on the parallel market at two Liberian dollars to one U.S. Dollar.

Mission managers opened this non-interest-bearing account in order to fund the Government's Civil Service Reform Program--the major intended use of the local currency--which was to start soon. During this period there was an acute liquidity crisis and a virtual breakdown of the bank clearing system in Liberia. Depositors were not able to withdraw their money on demand. So, Citibank agreed to keep the physical cash on hand to guarantee its availability at any time.

For providing this banking service, Citibank received a 7.5 percent service fee which amounted to approximately 320,700 Liberian dollars. Shortly after this arrangement was enacted, the liquidity problems with the Liberian dollar eased, but the arrangement remained unchanged.

As a result of this arrangement, 4.6 million Liberian dollars of CIP revenues were sitting idle in the Citibank without earning any interest. While these funds were languishing in the vaults, their value--or purchasing power--eroded by 50 percent because the parallel exchange rate had gone to three to one. U.S. Embassy economic officers believe this erosion is likely to worsen.

A.I.D. Policy on the handling of local currencies generated through CIP sales was detailed in a Department of State cable on October 21, 1987 titled *Supplementary Guidance on Programming Local Currency*. This cable directs that local currency be placed into an interest-bearing account in a deposit-taking institution, with any interest earned to be programmed as if it were principal. This guidance also stipulates that when an interest-bearing account is not used, a determination not to follow A.I.D.'s preference for interest-bearing accounts should be made by the highest A.I.D. Official at post and copies of this determination should be sent to the appropriate regional assistant administrator and the Bureau for Program and Policy Coordination. We found no evidence that these determinations were made.

During the audit survey phase, we formally recommended to the Mission Director that he take immediate action to transfer the CIP local currency to an interest-bearing account and/or to make firm plans to disburse these funds quickly.

In response to our memo, the Mission cited the reasons mentioned earlier for opening the non-interest-bearing account. The Mission added that the disbursement of funds has been slower than anticipated because the Government of Liberia did not follow through with the civil service reform program, the major intended use of the local currency. In fact, the Liberian Government did not reprogram any of these funds until March 1990, so no disbursements were made. The Government has now agreed to use the funds for:

- Nimba County Disaster Relief,
- Chamber of Commerce Private-Sector Training,
- School Rehabilitation, and
- Government Development Budget.

Though they had agreed to these broad categories, the Government had not prepared a detailed disbursement plan by the time we finished our audit work.

From the time the CIP account was open until the time of our audit, the supply of Liberian currency mushroomed. Now the banks have excess Liberian dollars. Nonetheless, they are still able to make **short-term, high-interest loans** of large amounts of local currency to mining and timber companies for their operating expenses. Thus, the CIP funds were attractive to them, and the terms and conditions of the accounts were negotiable in some banks.

In the CIP Grant Agreement, USAID and the Government selected Citibank to initially administer the account. They also agreed that other banks might participate later after A.I.D. and the Government assessed the needs of the program and the performance of Citibank. In mid-March, 1990, the Mission Director instructed Citibank to:

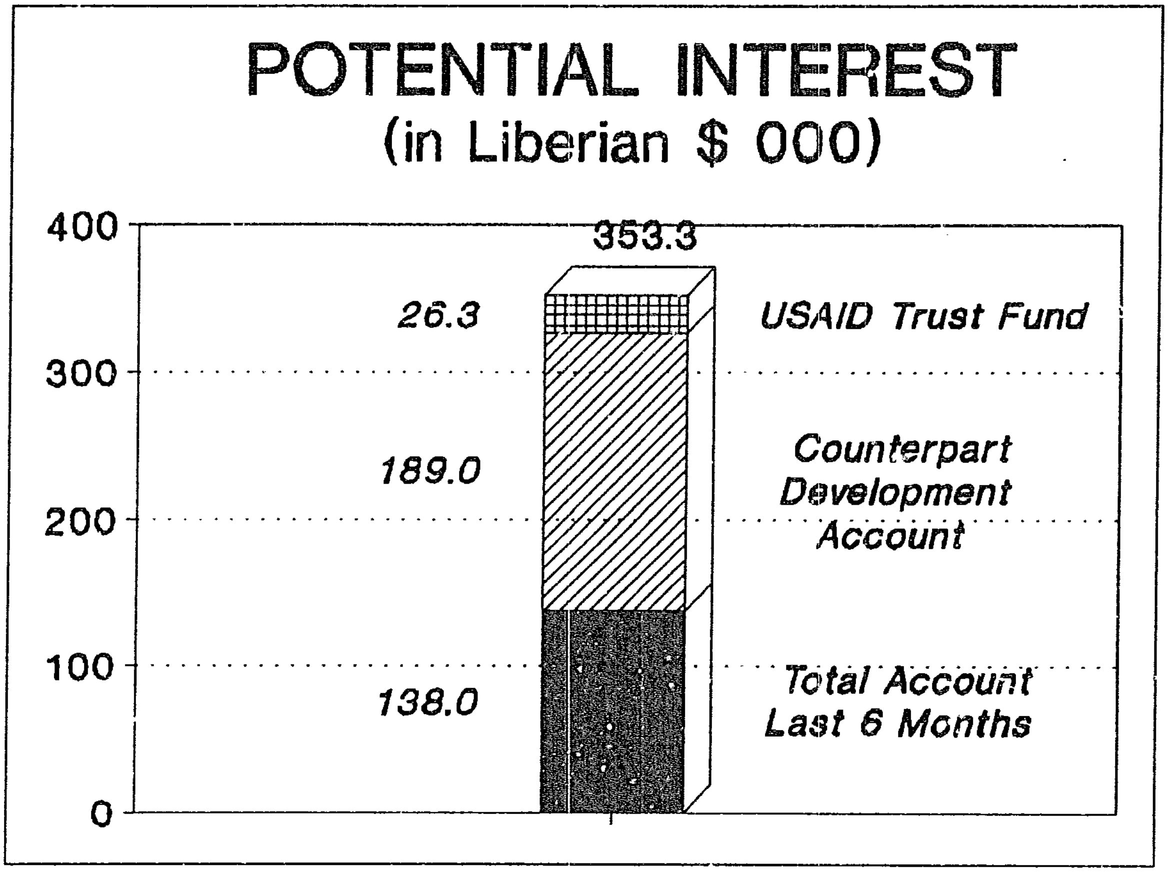
- transfer the sum of 3.6 million Liberian dollars into the CIP Counterpart Development Fund Account at the International Trust Company (ITC) bank;

- transfer 0.5 million Liberian dollars into a Special Account in Citibank for Nimba County Disaster Relief; and

- put 0.5 million Liberian dollars into a Trust Fund at Citibank for USAID operating expenses.

However, none of these accounts were interest-bearing either. The Mission officials said that ITC was selected only because a Ministry of Planning official had verbally requested it. USAID Officials made no assessment of Citibank's performance and gave no serious consideration to alternative banking arrangements. Further, neither the Controller nor the CIP project officer were actively involved in the decision to transfer the money to ITC.

We still believe there are substantial opportunity costs (shown in the accompanying chart) to USAID for not moving the CIP funds into interest-bearing accounts. We estimated that, for the last six months preceding the transfer of the CIP funds to the new accounts, the 4.6 million in local currency would have earned approximately 138,000 Liberian dollars. We also estimate that,



if the 3.6 million Liberian dollars of the CIP counterpart development funds were now deposited in interest-bearing accounts and evenly disbursed over a two-year period with a minimum interest rate of 6 percent, the total future interest earned would amount to 189,000 Liberian dollars. Using these same assumptions, we estimate that the CIP Trust Fund account could earn as much as 26,300 Liberian dollars for a total gain of 215,300 (189,000 + 26,300) Liberian dollars.

OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives

The Office of the Regional Inspector General for Audit/Dakar conducted a performance audit of the conversion of foreign exchange in Liberia to see if abuses of U.S. Assistance Dollars was occurring due to the exchange rate problem there. During our survey we found that the USAID may not have been handling correctly the local currency generated by the Commodity Import Program (CIP). So during our review, we performed a limited audit of the CIP to answer the following audit objective:

Did USAID/Liberia follow A.I.D. Policy Guidelines in handling the CIP program funds by depositing the local currency funds in interest-bearing accounts and disbursing them quickly?

In answering this question we tested whether USAID/Liberia has complied with A.I.D's *Supplemental Guidance on Programming Local Currency*. Our test was sufficient to provide reasonable--but not absolute--assurance of detecting abuse or illegal acts related to the limited scope of our objective. We did not review all aspects of the CIP program for Liberia.

Scope

We reviewed USAID performance in handling all of the CIP local currency generated from June 1988 to April 1990 which amounted to 4.6 million Liberian dollars. We conducted this review from February 6 to April 6, 1990 in accordance with generally accepted government auditing standards. As noted below, we conducted our field work in the office of USAID/Liberia, Citibank, and ITC bank in Monrovia.

Methodology

We selected the CIP program because we found during our survey that 4.6 million Liberian dollars had been sitting in Citibank vaults without earning any interest and USAID and the Liberian Government did not have a firm plan to spend them in the near future.

To accomplish the audit objective, we determined specifically whether

(1) the CIP generated funds were deposited in interest-bearing accounts by discussing the question with bank officials;

(2) interest-bearing accounts were available in banks in Liberia by speaking with bank officials;

(3) USAID/Liberia had investigated alternative banking opportunities offered in Monrovia by questioning bank and responsible mission officials; and

(4) USAID/Liberia and the Liberian Government had agreed on a firm plan to spend the CIP generated local currency by reviewing agreements and project documents and discussing the matter with Mission officials.

We reviewed the CIP program files and interviewed responsible officials within the Mission, the banking community and the private sector. We also examined the CIP grant agreement, bank statements, management reports, project implementation letters, and various correspondence.

APPENDIX II

MISSION COMMENTS (APPENDIX II) WERE NOT SUBMITTED

REPORT ON INTERNAL CONTROLS

The Office of the Regional Inspector General for Audit/Dakar conducted a performance audit of the conversion of foreign exchange in Liberia to see if abuses of U.S. Assistance Dollars was occurring due to the exchange rate problem there. During our survey we found that the USAID may not have been handling correctly the local currency generated by the Commodity Import Program (CIP). So, during our review, we performed a limited audit of the CIP to answer the following audit objective:

> **Did USAID/Liberia follow A.I.D. Policy Guidelines in handling the CIP program funds by depositing the local currency funds in interest-bearing accounts and disbursing them quickly?**

In answering this question we tested whether USAID/Liberia has complied with A.I.D's *Supplemental Guidance on Programming Local Currency.* We did not review all aspects of the CIP program for Liberia.

We reviewed USAID performance in handling all of the CIP local currency generated from June 1988 to April 1990 which amounted to 4.6 million Liberian dollars. We conducted this review from February 6 to April 6, 1990 in accordance with generally accepted government auditing standards. As noted below, we conducted our field work in the office of USAID/Liberia, Citibank, and ITC bank in Monrovia.

To test the internal controls associated with the audit objective, we interviewed responsible USAID and commercial bank officials and reviewed agreements and project documents to determine specifically whether

(1) the CIP generated local-currency funds were deposited in interest-bearing accounts;

(2) interest-bearing accounts were available in banks in Liberia;

(3) USAID/Liberia had investigated alternative banking opportunities offered in Monrovia; and

(4) USAID/Liberia and the Liberian Government had agreed on a firm plan to spend the CIP generated local currency.

We found that the USAID had no internal controls to ensure that the provisions of A.I.D.'s *Supplementary Guidance on Programming Local Currency were followed.* Therefore, we recommended that the Director, USAID/Liberia Establish a mission policy that requires future CIP agreements to stipulate that local currencies be placed in interest-bearing accounts and that local currencies be disbursed within a specific time period after which the funds would revert to direct USAID control.

REPORT ON COMPLIANCE

We reviewed USAID performance in handling all of the CIP local currency generated from June 1988 to April 1990 which amounted to 4.6 million Liberian dollars. We conducted this review from February 6 to April 6, 1990 in accordance with generally accepted government auditing standards. We conducted our field work in the offices of USAID/Liberia, Citibank, and ITC bank in Monrovia.

We selected the CIP program because 4.6 million Liberian dollars had been sitting in Citibank vaults without earning any interest, and USAID and the Liberian Government did not have any firm plan to spend them in the near future.

We limited our test of compliance to USAID's handling of the CIP local currency as related to the A.I.D.'s *Supplemental Guidance on Programming Local Currency.* We did not conduct an audit of the entire Program.

The results of our tests of compliance disclosed the following significant instances of noncompliance:

- USAID failed to ensure that the CIP funds were deposited in interest-bearing accounts.

- USAID failed to ensure that the CIP funds were disbursed quickly.

- USAID failed to make a formal determination to not use interest-bearing accounts and did not inform the assistant administrator about this determination.

Except as described above, the results of our tests of compliance indicate that, with respect to the items tested, USAID/Liberia complied, in all significant respects, with the provisions of the applicable A.I.D. policies. With respect to the items not tested, nothing came to our attention that caused us to believe that USAID/Liberia had not complied, in all significant respects, with those policies.

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