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Audit of  
the Government of Kenya Under the  
Rural Private Enterprise, Project No. 615-0220  
Loan No. 615-T-020

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Report No. 3-615-94-01-N  
October 6, 1993



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Nairobi, Kenya



U.S. AGENCY FOR  
INTERNATIONAL  
DEVELOPMENT

MEMORANDUM

October 6, 1993

**TO:** Director, USAID/Kenya, John R. Westley

**FROM:** RIG/A/Nairobi, Everette B. Orr *Everette B. Orr*

**SUBJECT:** Audit of the Government of Kenya Under the Rural Private Enterprise Project No. 615-0220, Loan No. 615-T-020  
Audit Report No. 3-615-94-01-N

*Regional  
Inspector General  
for Audit/Nairobi*

Attached are five copies of an Agency-contracted financial audit report of the Government of Kenya Under the Rural Private Enterprise Project No. 615-0220, Loan No. 615-T-020. The accounting firm of Price Waterhouse, Kenya performed the audit.

A.I.D. authorized the Rural Private Enterprise (RPE) Project No. 615-0220, Loan No. 615-T-020 on August 25, 1983. The purpose of the RPE project was to establish and expand rural private enterprises (businesses with strong linkages to agriculture, wherever located, and other business located outside Nairobi and Mombasa) in Kenya. The achievement of this purpose was to contribute directly to the fulfillment of the Government of Kenya's and USAID/Kenya's goal of increased rural production, employment and income.

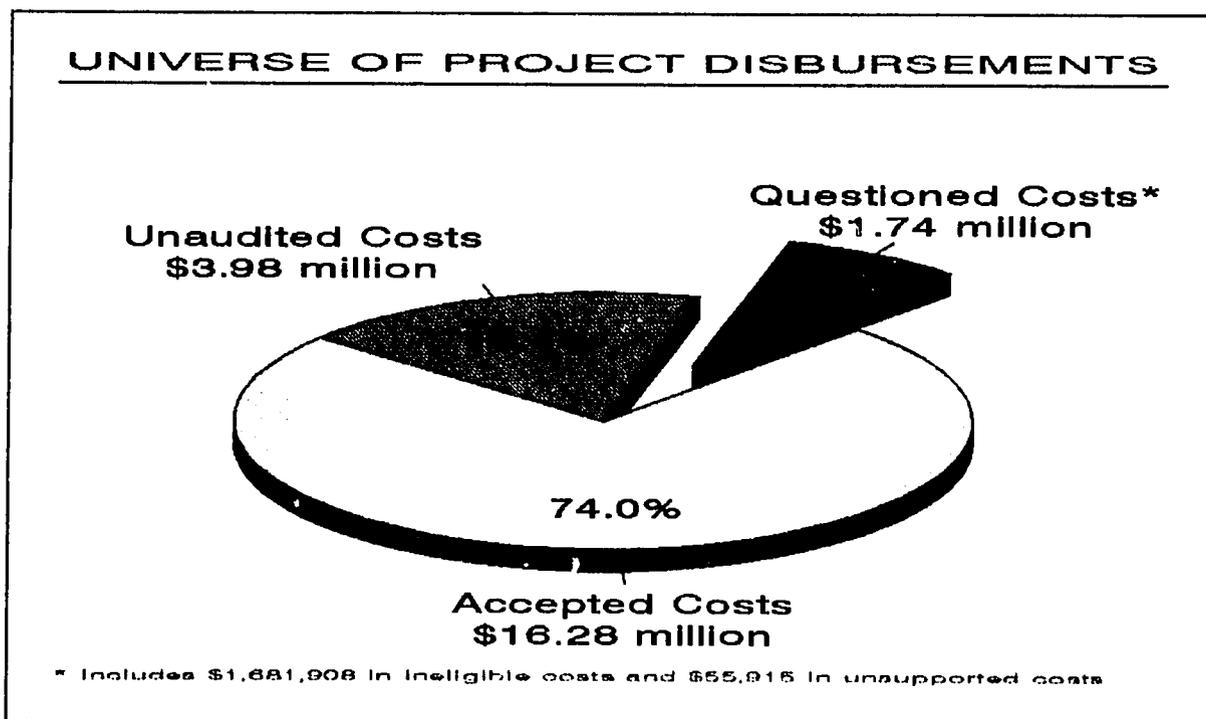
The objectives of this project were to be attained through the provision of credit and technical assistance to commercial banks (or finance companies which were part of a commercial bank group) active in Kenya which were, in turn, to make loans and provide business advice to entrepreneurs. The implementation of this project occurred through the Ministry of Finance(MOF)/the Central Bank of Kenya (CBK) assisted by the following participating banks and financial institution:

- The Kenya Commercial Bank;
- The Kenya Commercial Finance Company;
- The Standard Chartered Bank of Kenya; and
- The Barclays Bank of Kenya.

The audit covered project disbursements totalling \$22,000,073 for the period August 25, 1983 through August 31, 1992. The auditors tested disbursements of \$18,021,360 (81.9 percent). The audit did not cover reflows of RPE funds (interest and principal payments from the participating banks) which under the project terms are continuing.

The objective of the audit was to examine the RPE's Fund Accountability Statement (FAS) and express an opinion as to whether the statement presents fairly, the use of funds in accordance with the project agreement. In order for the auditors to answer the objective, they were to consider the RPE's internal control structure so as to determine the auditing procedures for the purpose of expressing an opinion on the FAS. The auditors were required to report on significant internal control deficiencies and material weaknesses. As part of obtaining reasonable assurance about whether the FAS was free of material misstatements, the auditors were required to test the RPE's compliance with the terms of the project agreement and report on any identified material instances of noncompliance.

Price Waterhouse issued an adverse opinion on the Fund Accountability Statement because of the significant amount of questioned costs totalling \$1,737,823 (ineligible costs of \$1,681,908 and unsupported costs of \$55,915). As illustrated below, the amount of questioned costs represents about 7.9 percent of the amount audited.



The report on internal control structure noted material weaknesses which included:

- inadequate systems for monitoring and reconciling foreign procurement by MOF/CBK;

- inadequate controls in MOF/CBK for ensuring that funds not disbursed to entrepreneurs by the participating banks are repaid to USAID/Kenya;
- inadequate systems to ensure submission of regular reports of letters of commitment to CBK and USAID/Kenya by the participating banks;
- poor voucher filing and referencing practices in CBK;
- failure to maintain formal job descriptions for key project personnel in CBK; and
- inadequate monitoring of promissory notes by CBK.

Further, the report on compliance noted two material instances of noncompliance concerning:

- failure by participating banks to reimburse USAID/Kenya amounts received but not disbursed to entrepreneurs, resulting in ineligible costs of \$1,033,014; and
- failure by participating banks to reimburse USAID/Kenya amounts not used by the entrepreneurs for approved and intended purposes, resulting in ineligible costs of \$648,894.

The draft report was submitted to USAID/Kenya and the MOF/CBK for comment and their comments (Appendix I and Appendix II, respectively) were taken into consideration in the preparation of the final report by Price Waterhouse. CBK did not consider itself to be the MOF's implementing representative to ensure that the Government of Kenya's responsibilities under the project agreement were fulfilled. Rather, CBK saw itself as having properly relied upon the participating banks and the Project Contractor to carry out their specific tasks without the need for CBK to supervise, direct or take responsibility for their actions. However, under the project agreement, the ultimate responsibility for implementing the project rested with the Government of Kenya and, therefore, upon the CBK.

We are including the following recommendations in the Office of the Inspector General audit recommendation follow-up system.

**Recommendation No. 1:** We recommend that USAID/Kenya determine the allowability and recover, as appropriate, the following questioned costs from the Government of Kenya:

**1.1 Ineligible costs of \$1,681,908; and**

**1.2 Unsupported costs of \$55,915.**

**Recommendation No. 2: We recommend that USAID/Kenya obtain from the Ministry of Finance/Central Bank of Kenya a plan of action to correct internal control weaknesses and instances of non-compliance with the project agreement by ensuring that:**

**2.1 foreign procurements are monitored and reconciled;**

**2.2 funds not disbursed by participating banks to entrepreneurs are repaid;**

**2.3 participating banks submit regular reports of letters of commitment to the Central Bank of Kenya and USAID/Kenya;**

**2.4 the Central Bank of Kenya improves its voucher filing and referencing system;**

**2.5 the Central Bank of Kenya maintains formal job descriptions for key project personnel;**

**2.6 the Central Bank of Kenya improves monitoring of promissory notes; and**

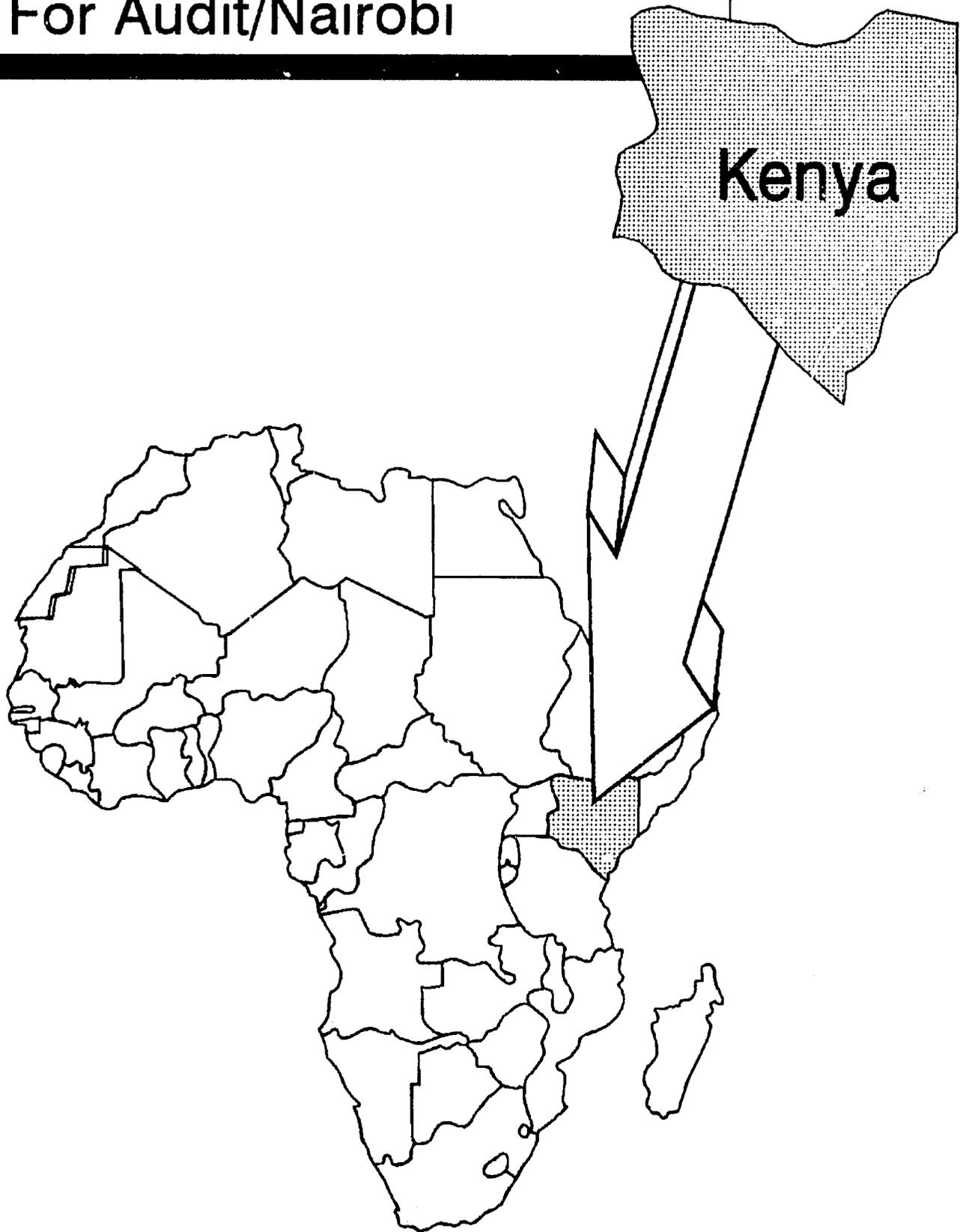
**2.7 funds not used by the entrepreneurs for the approved and intended purposes are repaid.**

We consider Recommendation Nos. 1 and 2 unresolved. Recommendation No. 1 may be resolved when the Mission makes a final determination concerning the allowability of the questioned amounts. The recommendation will be closed when the Mission takes action appropriate to the determination. Recommendation No. 2 will be resolved when the Mission obtains from the MOF/CBK an acceptable plan for corrective action. The recommendation will be closed upon implementation of the corrective action. Please respond to this report within 30 days indicating action planned or already taken to implement the recommendations.

Thank you for the cooperation extended to Price Waterhouse and Regional Inspector General for Audit representatives during the audit.

Attachments: a/s.

**Regional Inspector General  
For Audit/Nairobi**



AUDIT OF  
THE GOVERNMENT OF KENYA UNDER THE  
RURAL PRIVATE ENTERPRISE, PROJECT NO. 615-0220,  
LOAN NO. 615-T-020

ATTACHMENTS

UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT

AGENCY-CONTRACTED AUDIT OF THE GOVERNMENT OF KENYA UNDER THE  
RURAL PRIVATE ENTERPRISE (RPE) PROJECT NO. 615 - 0220, LOAN NO. 615-T-020

FINAL REPORT

AUGUST 16 1993

AGENCY-CONTRACTED AUDIT OF THE GOVERNMENT OF KENYA UNDER THE  
RURAL PRIVATE ENTERPRISE (RPE) PROJECT NO. 615-0220, LOAN NO. 615-T-020  
FOR THE PERIOD AUGUST 25 1983 TO AUGUST 31 1992

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## USAID/KENYA

### AGENCY-CONTRACTED AUDIT OF THE GOVERNMENT OF KENYA UNDER THE RPE PROJECT NO. 615-0220, LOAN NO. 615-T-020

#### SECTION 1 - INTRODUCTION

##### 1.1 BACKGROUND INFORMATION

###### 1.1.1 Participating Organisations

The Rural Private Enterprise (RPE) Project No. 615-0220 was undertaken on August 25 1983 in an agreement between USAID/Kenya and the Government of Kenya (GoK). The Ministry of Finance (MOF) assumed responsibility to ensure that GoK's responsibilities were met as the project proceeded.

The Central Bank of Kenya (CBK) controlled the flow of funds under the project, and acted as the liaison between the participating banks and USAID. The following commercial banks and financial institution participated in the project :

- . Kenya Commercial Bank (KCB)
- . Kenya Commercial Finance Company (KCFC)
- . Standard Chartered Bank (SCB)
- . Barclays Bank of Kenya (BBK)

###### 1.1.2 The RPE Project

The primary objective of the RPE project was to establish and expand rural enterprises in Kenya, as a result of intermediate lending to private sector entrepreneurs. The project also aimed to increase the capacity of the Kenyan banking system to administer intermediate lending, by providing technical assistance and business advice.

USAID's contribution of project finance consisted of a loan to GoK not to exceed \$24 million, and a grant ceiling of \$11.296 million.

The loan component was drawn down as the project proceeded and the participating banks made loans to entrepreneurs. Entrepreneurial loans were subject to strict eligibility criteria, and were supplemented by matching funds loaned by the participating banks in predetermined ratios. Many of the loans were disbursed in local currency, but foreign procurement were also made when required.

During the term of the RPE project, the total amount drawn down from USAID for loan purposes was \$ 22,000,073. This reflects a total number of 113 loans disbursed to entrepreneurs, prior to the final drawdown of USAID funds by CBK on April 1 1992.

### 1.1.3 Accounting and Contract Monitoring Systems

Accounting and contract monitoring systems were established with the assistance of the project's technical advisors. A computer based accounting system was installed at CBK specifically for the RPE project, facilitating the generation of reports including CBK disbursements to banks, loan disbursements to entrepreneurs by the banks, agency fees reports, and details of due & overdue promissory notes. In addition, a manual register was maintained at CBK in respect of its cash disbursements to the banks.

Principal documentary requirements were established as inputs to these systems :

- Form RPE1 formed the basis from which participating banks could claim reimbursement from CBK for each proposed entrepreneurial loan. The form comprised details of individual loans and associated financial and statistical details for RPE monitoring and evaluation purposes.
- Form RPE2 provided the means to request reimbursement for the USAID portion of the RPE loan.
- Other forms were established for foreign procurement, including means by which USAID funds were disbursed directly out of Washington to approved suppliers of foreign equipment for RPE loan purposes.

Reporting requirements were also established. In particular, CBK was required to submit monthly reports to Treasury and USAID, providing information including bank account balances, summary of loans disbursed, and approved loan reports.

## 1.2 AUDIT APPROACH

### 1.2.1 Audit Objectives and Scope

Price Waterhouse was contracted under Contract No. 623-0000-I-00-2003-00 to perform an audit of disbursements of loans under the RPE project, covering the period August 25 1983 to August 31 1992. This period covers the timeframe in which initial disbursements were made to entrepreneurs, for the final disbursement was made in April 1992. The audit period does not relate to reflows of RPE funds, which under the project terms are continuing. As explained below, this audit scope excludes a review of such reflows.

Expenditure reflected in the Fund Accountability Statement and relevant to the audit amounted to \$ 22,000,073.

The audit scope was defined in the Delivery Order and focused solely on the loan component of USAID funding, addressing only the initial disbursement of funds only progressing from USAID advances to disbursements to entrepreneurs. The following were **excluded** from the audit scope :

- . an examination of the grant component of the scheme
- . an examination of financial events subsequent to the initial downward disbursements (eg reflows were not included in the audit scope)
- . matters relating to an evaluation of the project or an assessment of whether the project's objectives were met

The objectives of the audit were to:

- . audit the RPE Fund Accountability Statement and express an opinion as to whether the Fund Accountability Statement presents fairly, in all material respects and in conformity with the basis of accounting described in the report, the use of the funds as they relate to the loan component in accordance with the RPE Project Agreement
- . consider the internal control structure in place at the implementing institutions, in order to determine the auditing procedures for the purpose of expressing an opinion on the Fund Accountability Statement and to report on significant internal control deficiencies and material weaknesses
- . test MOF's and CBK's compliance with the terms of the RPE Project Agreement in respect of the loan component, as part of obtaining reasonable assurance about whether the Fund Accountability Statement is free of material misstatement, and report on any identified material instances of noncompliance.

Our examination was performed in accordance with generally accepted auditing standards and Government Auditing Standards issued by the United States Comptroller General with the exception that we have not been subject to a quality control review by a non Price Waterhouse firm. Such reviews are not required or available to professional firms in Kenya. We do not believe that this departure has affected our audit. We were subject to a quality control review in July 1992 undertaken by a Price Waterhouse firm independent of our firm.

Our audit included such tests of the auditee's data and records and other auditing procedures as were considered necessary in the circumstances. The audit was performed under the supervision of the Regional Inspector General for Audit (RIG/A) based in Nairobi. Price Waterhouse also adhered to the guidelines contained in various chapters of the "Guidelines for Financial and Compliance Audits of A.I.D - Financed Agreements".

### 1.2.2 Methodology

A preliminary survey was conducted between November 8 1992 and November 15 1992 at the head office premises of CBK, KCB, KCFC, SCB, and BBK.

This survey was performed to secure an understanding of the RPE accounting systems in place, assess the overall strength of the systems of internal control, estimate the extent of compliance with the provisions and procurement regulations detailed in the Project Agreement (as amended and interpreted by Project Implementation Letters), and determine the degree to which supporting documentation would be available to the audit team. The survey provided the groundwork from which Price Waterhouse developed its detailed audit work plan.

The terms of the RPE Project Agreement and the cost principles contained in the applicable U.S Government regulations were used as criteria in the determination of unsupported or ineligible costs.

The detailed audit work included the following major procedures:

- review of the project agreement, implementation letters, handbooks, relevant government regulations and other related documents
- examination and testing of documentation at CBK supporting receipts from USAID and disbursements to the participating banks
- examination and testing of documentation at the participating banks supporting a sample of loan disbursements to entrepreneurs
- a study and evaluation of internal accounting controls and accounting practices to the extent necessary to render an opinion on the Fund Accountability Statement
- site visits to a sample of entrepreneurial recipients of loans under the RPE project, to ensure by inspection that funds were expended for eligible and intended purposes.
- reconciliation of RPE disbursements recorded in the CBK accounting system, to USAID's Mission Accounting Control System (MACS).

We also performed other audit procedures as we determined were appropriate under the circumstances and warranted to arrive at our conclusions.

### 1.2.3 Sample Methodology

Our audit was carried out in accordance with judgmental sample methodology, at the following three levels :

### **Central Bank of Kenya Level**

All loan disbursements were tested at CBK level, in order to satisfactorily reconcile figures reflected in the Fund Accountability Statement and review total disbursements per loan.

### **Participating bank level**

Forty seven loans were selected for testing at participating bank level, accounting for \$ 18,021,360 (or 81.91%) of total loan disbursements.

The sample was primarily selected to obtain satisfactory coverage of the respective sample populations, with respect to the following attributes :

- . value of loan, while still addressing smaller loans
- . lending institution, ensuring all four participating banks were covered
- . location of entrepreneur, ensuring regions throughout Kenya were addressed
- . type of loan disbursement, ensuring both foreign procurement and locally denominated loans were addressed.

Further, the sample was supplemented for loans identified at the survey stage for which we believed warranted testing on the basis of correspondence reviewed.

### **Entrepreneur Level**

Twenty eight loans were selected for testing at entrepreneurial level, accounting for \$ 12,336,484 (or 56.07%) of total loan disbursements. This sample was a "sub-set" of the participating bank-level sample, and accordingly reflects similar attributes.

#### **1.2.4 Limitation of Scope**

We were subject to a limitation of scope when reconciling foreign procurement information at the Central Bank of Kenya to that of USAID. No listing was available from USAID which could assist identification of the foreign procurement classified by entrepreneur. We are advised that A.I.D Washington did not maintain records which might assist such identification. This limitation has affected our auditor's report on the Fund Accountability Statement.

In addition, there were local disbursements equivalent to \$ 3,779,280 and foreign disbursements in the amount of \$ 199,433 which were not included in our audit sample at participating bank level. While we do not classify this as a specific limitation of scope, we have expressed no opinion on these disbursements in view of the high incidence of ineligible and unsupported costs identified from testing of the audit sample.

### 1.3 SUMMARY OF AUDIT RESULTS

#### 1.3.1 Introduction

This summary of audit results highlights only the significant findings. For further details of our findings, recommendations and observations, please refer to the appropriate sections.

#### 1.3.2 Fund Accountability Statement

We performed a financial and compliance audit of the Fund Accountability Statement of RPE relating to the Project Agreement with USAID for the period August 25 1983 to August 31 1992.

Audit tests on the Fund Accountability Statement revealed significant questioned disbursements in the amount of \$ 1,737,823, comprising ineligible disbursements of \$ 1,681,908 and unsupported disbursements of \$ 55,915. Questioned disbursements comprise 7.91% of total disbursements.

In addition, no recommendation has been made in respect of disbursements amounting to \$ 3,978,713 (18.08% of total disbursements). These disbursements were found acceptable by our testing at CBK level, but were not tested to commercial bank and entrepreneur level, as they were not included in the approved sample profile. In view of the high incidence of questioned disbursements arising from audit testing at bank and entrepreneur level, no recommendation has been made in respect of these disbursements.

Questioned disbursements affected our opinion on the Fund Accountability Statement. The full text of our opinion is presented in Section 2.

#### 1.3.3 Internal Accounting Controls

We made a study and evaluation of the system of internal accounting controls to the extent we considered necessary and required by generally accepted government auditing standards.

Our study and evaluation was designed to determine the nature, timing and extent of auditing procedures necessary to express an opinion on the Fund Accountability Statement. We do not, however, express an overall opinion on the system of accounting controls in place at CBK or any of the participating banks.

During the course of our audit the following internal control weaknesses were noted:

- Systems were inadequate to ensure proper monitoring and reconciliation of foreign procurement by CBK

- . CBK's controls were inadequate to ensure repayment to USAID when funds advanced by USAID were not disbursed to entrepreneurs
- . Participating banks did not submit regular reports of letters of commitments to CBK and USAID
- . CBK's voucher referencing system was poor
- . CBK did not maintain formal job descriptions in respect of key project personnel
- . Monitoring of promissory notes by CBK was inadequate

In view of the significance of questioned disbursements outlined in Section 2, we considered the above matters constitute a material weakness. The full text of our report is set out in Section 3.

#### **1.3.4 Compliance With Agreement Terms**

An evaluation of compliance with the RPE Project Agreement and US Government Regulations identified certain material instances of non compliance as follows.

- . contrary to the project agreement, USAID has not received repayment for funds advanced by it but never disbursed to entrepreneurs
- . certain loans were not utilised as per project agreement
- . one instance was identified where a participating bank did not use USAID-approved foreign bank when arranging a letter of credit.

#### **1.3.5 Summary of Management Comments**

USAID Mission and Central Bank of Kenya's comments are included in this report as Appendices I and II respectively. In respect of each finding, they have been summarised and incorporated in the body of this report.

The auditee responses are given by CBK on instruction from the Ministry of Finance. CBK's comments relate, for the most part, to its perception of its role in the project. CBK does not see itself as the Ministry of Finance's implementing representative to ensure the Government of Kenya's responsibilities under the Loan Agreement were fulfilled. Rather, it sees itself as having relied entirely on the commercial banks and the Project Contractor (Deloitte Haskins & Sells) to have carried out their specific tasks without the need for CBK to supervise, direct or take responsibility for their actions. Where this audit report raises areas where the commercial banks or the Project Contractor had the opportunity to prevent or rectify the adverse findings, CBK denies any responsibility. We note that a Ministry of Finance representative has signed the audit representation letter, reflecting the fact that under the loan Agreement the ultimate responsibility rests with the Government of Kenya.

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## *Price Waterhouse*



### **AGENCY-CONTRACTED AUDIT OF THE GOVERNMENT OF KENYA UNDER THE RURAL PRIVATE ENTERPRISE (RPE) PROJECT NO. 615-0220, LOAN NO. 615-T-020**

#### **SECTION 2 : FUND ACCOUNTABILITY STATEMENT**

##### **2.1 INDEPENDENT AUDITOR'S REPORT**

We have audited the Fund Accountability Statement prepared by the Central Bank of Kenya under USAID Rural Private Enterprise (RPE) Project Agreement No. 615-0220 for the period from August 25, 1983 to August 31, 1992. The Fund Accountability Statement is the responsibility of the MOF/CBK management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and the standards contained in the Government Auditing Standards issued by the Comptroller General of the United States (1988 revision) with the exception that we have not been subject to a quality control review by a non Price Waterhouse firm. Such reviews are not required or available to professional firms in Kenya. We do not believe that this departure has affected our audit. We were subject to a quality control review in July 1992 undertaken by a Price Waterhouse firm independent of our firm.

Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the Fund Accountability Statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Fund Accountability Statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1 to the Fund Accountability Statement, this statement was prepared on the basis of cash receipts and disbursements which is a comprehensive basis of accounting other than generally accepted accounting principals.

With respect to incurred disbursements, the results of our audit include questioned disbursements of \$ 1,737,823 which corresponds to the equivalent of Shs 41,698,490. Total questioned disbursements consist of ineligible disbursements of \$ 1,681,908 (equivalent to Shs 40,356,823) and unsupported disbursements of \$ 55,915, (equivalent to Shs 1,341,667). In addition, we were subject to a limitation of scope outlined in Section 1.2.4, whereby we express no opinion on the eligibility of foreign procurement unreconciled of \$ 200,927 nor amounts not audited at bank/entrepreneur level of \$ 3,978,713 (equivalent to Shs 95,219,001).

In our opinion, because of the significance of questioned disbursements referred to in the preceding paragraph, the Fund Accountability Statement does not present fairly, in conformity with the basis of accounting described above, the revenues and disbursements of MOF/CBK for the period August 25, 1983 to August 31, 1992.

Financial information contained in this report may be privileged. The restrictions of 18 USC 1905 should be considered before any information is released to the public. This report is intended solely for the information of the MOF/CBK and the Agency for International Development but is not intended to limit the distribution of the report, if a matter of public record.

March 31, 1993

*Russ Whitehouse*

**FUND ACCOUNTABILITY STATEMENT  
RURAL PRIVATE ENTERPRISE PROJECT  
PROJECT AGREEMENT NO.615-0220  
FOR PERIOD AUGUST 25 1983 TO AUGUST 31 1992**

	Note	US \$	K Shs
<b><u>REVENUE</u></b>			
<b>USAID advances</b>			
Local deposits to Treasury account		17,334,755	415,941,990
Letters of Commitment		<u>4,665,318</u>	<u>110,566,200</u>
<b>TOTAL REVENUE</b>	<b>2</b>	<b><u>22,000,073</u></b>	<b><u>526,508,190</u></b>
<b><u>DISBURSEMENTS</u></b>			
<b>Local disbursements</b>			
Standard Chartered Bank		4,048,327	97,138,334
Barclays Bank		4,783,356	114,775,112
Kenya Commercial Bank/Finance		<u>8,503,072</u>	<u>204,028,544</u>
<b>Total Local Disbursements</b>	<b>3</b>	<b><u>17,334,755</u></b>	<b><u>415,941,990</u></b>
<b>Foreign disbursements</b>			
Standard Chartered Bank		1,337,938	34,921,898
Barclays Bank		2,364,918	52,715,496
Kenya Commercial Bank/Finance		<u>962,462</u>	<u>22,928,806</u>
<b>Total Foreign Disbursements</b>	<b>3</b>	<b><u>4,665,318</u></b>	<b><u>110,566,200</u></b>
<b>TOTAL DISBURSEMENTS</b>		<b><u>22,000,073</u></b>	<b><u>526,508,190</u></b>

*In addition, as part of the disbursement process, interest of Shs 9,036,886 (approximately US\$ 376,620) was earned in the RPE Treasury Account, and a further amount of Shs 2,600,000 (approximately US\$ 108,357) was credited, representing a repayment by Barclays Bank in respect of RPE applications withdrawn for which USAID funds had previously been advanced. The combined balance of Shs 11,636,886 (approximately US\$ 484,977) was transferred to the RPE Project Reflows Account in August 1990.*

AGENCY-CONTRACTED AUDIT OF THE GOVERNMENT OF KENYA UNDER THE  
RURAL PRIVATE ENTERPRISE (RPE) PROJECT NO.615-0220, LOAN NO. 615-T-020

NOTES TO THE FUND ACCOUNTABILITY STATEMENT FOR THE PERIOD AUGUST  
25 1983 TO AUGUST 31 1992

1. Basis of Accounting

The Fund Accountability Statement has been prepared on a cash basis, which is a comprehensive basis of accounting other than Generally Accepted Accounting Principles. As noted in Notes 2 and 3 below, revenues and expenditures are recorded when cash is physically received or disbursed.

2. Revenues

Revenues refer to amounts advanced by USAID in the period August 25 1983 to August 31 1992, and comprise the following :

- **local deposit advances** to CBK, facilitating disbursements of loan funds by participating banks to approved entrepreneurs. These advances were effected by way of local currency cheques.

The US\$ equivalent amounts reflected in the Fund Accountability Statement represent the dollar equivalents determined by USAID at the time of each advance, as recorded in the Mission Accounting Control System.

- **foreign letters of commitment** effected by A.I.D./Washington directly to approved foreign banks, for the purposes of foreign procurement by entrepreneurs. These advances were effected in a variety of foreign currencies (eg US\$, Italian Lire, German Deuthschmark, etc).

The US\$ figures reflected in the Fund Accountability Statement represent the dollar equivalents of the transactions as recorded in the Mission Accounting Control System. The Kenya Shilling figures reflected in the Fund Accountability Statement represent shilling equivalents of the transactions as recorded in the Central Bank of Kenya RPE records.

3. Disbursements

Disbursements represent amounts disbursed as follows :

- **CBK advances to participating banks** for the purposes of locally denominated loan disbursements to approved entrepreneurs.

These transactions were effected in Kenya Shillings. The US\$ equivalents reflected in the Fund Accountability Statement for each participating bank represent the conversion of Kenya Shilling transactions at the weighted average exchange rate applicable to USAID local advances to CBK.

**foreign procurement made by entrepreneurs** under approved procedures with USAID and participating banks.

These transactions were effected in a variety of foreign currencies (eg US\$, Italian Lire, German Deutsche Mark, etc). The US\$ figures reflected in the Fund Accountability Statement represent the dollar equivalents of the transactions as recorded in the Mission Accounting Control System. The Kenya Shilling figures reflected in the Fund Accountability Statement represent shilling equivalents of the transactions as recorded in the Central Bank of Kenya RPE records. The link between these two records has not been established (See Section 3.2.1).

FUND ACCOUNTABILITY STATEMENT  
RURAL PRIVATE ENTERPRISE PROJECT  
PROJECT AGREEMENT NO.615-0220  
FOR PERIOD AUGUST 25 1983 TO AUGUST 31 1992

AUDIT OF DISBURSEMENTS CLAIMED

	CLAIMED US \$	AMOUNTS RECOMMENDED TO BE			NO RECOMMEND- ATION MADE US \$
		ACCEPTED* US \$	QUESTIONED		
			INELIGIBLE US \$	UNSUPPORTED US \$	
<b><u>DISBURSEMENTS</u></b>					
<b>Local disbursements</b>					
Standard Chartered Bank	4,048,327	2,947,570	561,708	44,454	494,595
Barclays Bank	4,783,356	3,744,223	108,358	0	930,775
Kenya Commercial Bank/Finance	<u>8,503,072</u>	<u>5,125,859</u>	<u>1,011,842</u>	<u>11,461</u>	<u>2,353,910</u>
<b>Total Local Disbursements</b>	<b><u>17,334,755</u></b>	<b><u>11,817,652</u></b>	<b><u>1,681,908</u></b>	<b><u>55,915</u></b>	<b><u>3,779,280</u></b>
<b>Foreign disbursements</b>					
Standard Chartered Bank	1,337,938	1,292,621	0	0	45,317
Barclays Bank	2,364,918	2,309,551	0	0	55,367
Kenya Commercial Bank/Finance	<u>962,462</u>	<u>863,713</u>	<u>0</u>	<u>0</u>	<u>98,749</u>
<b>Total Foreign Disbursements</b>	<b><u>4,665,318</u></b>	<b><u>4,465,885</u></b>	<b><u>0</u></b>	<b><u>0</u></b>	<b><u>199,433</u></b>
<b>TOTAL DISBURSEMENTS</b>	<b><u>22,000,073</u></b>	<b><u>16,283,537</u></b>	<b><u>1,681,908</u></b>	<b><u>55,915</u></b>	<b><u>3,978,713</u></b>

*Foreign procurements are accepted for audit subject to exchange rate conversion uncertainties which have generated unreconciled foreign procurements in dollar terms of \$ 200,927. See Exhibit II and Section 3.2.1.*

2.3 **FINDINGS AND RECOMMENDATIONS**

**FUND ACCOUNTABILITY STATEMENT**

2.3.1 **Finding on Funds never Disbursed to Entrepreneurs**

With respect to the following loans, USAID provided funds in the amounts shown but the banks did not disburse the amounts to the entrepreneurs because the loan applications were withdrawn :

Client	Amount Shs	US\$ equivalent
<b>Standard Chartered Bank</b>		
Colotec (K) Ltd	8,000,000	333,407
<b>Barclays Bank</b>		
New Era Enterprises	2,000,000	83,352
Belozl Industries	600,000	25,006
<b>Kenya Commercial Finance Company</b>		
Apollo Klare	266,666	11,114
Karsan Ramji & Sons Ltd	8,000,000	333,407
Union Textiles	<u>5,920,157</u>	<u>246,728</u>
	<u>24,786,823</u>	<u>1,033,014</u>

In the cases of New Era Enterprises and Belози Industries we are aware that Barclays Bank repaid the funds advanced, and this repayment was credited to the CBK RPE Project Account, and subsequently transferred to the RPE Reflows Account. For these and other instances identified above, the funds should have been repaid directly to USAID. Accordingly, the amounts are classified in all cases as ineligible.

Article D Section D.6 Section (a) of the Project Agreement states that "in the case of any disbursement which is not supported by valid documentation in accordance with this Agreement, or which is not made or used in accordance with this agreement, A.I.D, notwithstanding the availability or exercise of any other remedies provided for under this Agreement, may require the Government to refund the amount of such disbursements in United States Dollars to A.I.D within sixty (60) days after receipt of a request thereof".

#### **Recommendation No. 1**

**The Mission should determine the allowability and recover from Central Bank of Kenya, as appropriate, ineligible disbursements set out above of \$ 1,033,014 (historically equivalent to Shs 24,786,823).**

#### **Auditee Comments (CBK)**

Loans to New Era Enterprises, Belози Industries and Apollo Kiarie were repaid and funds transferred to the CBK RPE Project Account. These funds were subsequently reduced from our requests for funding to USAID since USAID did not request for payment under the project agreement.

We must emphasise here that we would not have been in a position to know of any funds reimbursed by CBK which may not have been disbursed by the banks to their entrepreneurs, as CBK had no direct dealing with entrepreneurs or with commercial bank branches. We only dealt with head offices of commercial banks who would normally advise us of any undisbursed funds as would the Project Contractor. Only on their advice would we debit the participating commercial bank.

#### **USAID Comments**

The Mission concurs with the audit finding.

#### **Auditor Response**

Under the Project Agreement, at the Article mentioned above, USAID has the authority to require repayment in US Dollars of funds not disbursed. USAID has yet to exercise this right as it was not aware that there were significant funds not disbursed. USAID still has the right to require repayment, and accordingly the audit recommendation stands.

Whether funds have been placed in a RPE Reflows account or otherwise does not alter the recommendation. Neither does an assessment as to whether the Central Bank of Kenya, participating commercial banks or the Project Contractor should be apportioned any blame. For our audit purposes, ultimate responsibility rests with the Government of Kenya under the Project Agreement, and failures of established internal controls to underpin this responsibility is the subject of Section 3 to this report.

**2.3.2 Finding on Funds not Used for Intended Purposes**

The following amounts were disbursed by the participating banks to the entrepreneurs but were not used for intended purposes :

Client	Amount Shs	US\$ equivalent
<b>Standard Chartered Bank</b>		
Malindi General Engineering	5,478,000	228,301
<b>Kenya Commercial Finance Company</b>		
Malaa Industries	<u>10,092,000</u>	<u>420,593</u>
	<u>15,570,000</u>	<u>648,894</u>

These amounts are considered Ineligible for the purposes of the project agreement.

**Recommendation No. 2**

**The Mission should determine the allowability and recover from Central Bank of Kenya, as appropriate, ineligible disbursements set out above of \$ 648,894 (historical equivalent Shs 15,570,000).**

**Auditee Comments (CBK)**

As we were not advised of these loans as not having been disbursed to the users, we consider them as performing and are accordingly included in our running amortization schedule.

**USAID Comments**

In order to determine the allowability of these costs, USAID/Kenya needs to know the purposes for which the loans were used.

**Auditors' Response**

Article D section D.6 section (a) of the Project Agreement provides A.I.D with the right to require refund of disbursements not used in accordance with the Agreement. This right may be exercised regardless of whether CBK was advised by the commercial banks or Project Contractor that the funds were not used for intended purposes. The commercial banks concerned have advised the auditors that the funds were not used for intended purposes; our attempts to identify the particular wrong purposes to which the moneys have been put have been unsuccessful, but the commercial banks have stated that the alternative uses would not have been allowable under the project. In both cases the banks have attempted to realise their security. The recommendation therefore stands.

**2.3.3 Finding on Unsupported Disbursements**

The following disbursements claimed from USAID are considered unsupported for audit purposes. They arise from audit visits to sampled entrepreneurs which were unsuccessful for reasons set out below :

Client	Amount Shs	US\$ equivalent	Reason disbursement is unsupported
<b>Standard Chartered Bank</b>			
Samuel Kai	1,066,667	44,454	Loan relates to dry cleaning equipment. We were unable to sight equipment. We are told it has been moved from Burnt Forest as a result of tribal clashes, and is hidden.
<b>Kenya Commercial Bank</b>			
Francis Giathi	275,000	11,461	Machinery and equipment was unable to be sighted as we are told it has been stolen, and that repayment of KCB's loan continues from other sources.
	<u>1,341,667</u>	<u>55,915</u>	

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**Recommendation No. 3**

The Mission should determine the allowability and recover from Central Bank of Kenya, as appropriate, unsupported disbursements set out above of Shs 1,341,667 (\$ 55,915).

**Auditee Comments (CBK)**

The above loans were reimbursed to commercial banks locally upon their requests. If these funds were unsupported, the Project Contractor would have notified the banks, USAID and Central Bank of Kenya and appropriate action would have been taken. We therefore consider these loans as performing under the project terms.

**USAID Comments**

USAID/Kenya requests that the auditors revisit the sampled entrepreneurs to determine whether the disbursements are still unsupported and amend the recommendation accordingly.

**Auditors' Response**

USAID comments were made in response to the draft audit report which had identified US \$ 1,389,544 in unsupported costs. As a result of revisits, this recommendation has been revised accordingly. We have not been provided with supporting evidence for the two remaining instances of unsupported disbursements.

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## *Price Waterhouse*



### AGENCY-CONTRACTED AUDIT OF THE GOVERNMENT OF KENYA UNDER THE RURAL PRIVATE ENTERPRISE (RPE) PROJECT NO. 615-0220, LOAN NO. 615-T-020

#### SECTION 3: INTERNAL ACCOUNTING CONTROLS

##### INDEPENDENT AUDITOR'S REPORT

We have audited the Fund Accountability Statement prepared by the Central Bank of Kenya under the USAID Rural Private Enterprise Project Agreement No. 615-0220 for the period from August 25 1983 to August 31 1992 and have issued our opinion thereon dated March 31 1993.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States (1988 revision) with the exception that we have not been subject to a quality control review by a non Price Waterhouse firm. Such reviews are not required or available to professional firms in Kenya. We do not believe that this departure has affected our audit. We were subject to a quality control review in July 1992 undertaken by a Price Waterhouse firm independent of our firm.

Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the Fund Accountability Statement is free of material misstatement.

In planning and performing our audit of the Fund Accountability Statement of the RPE Project for the period August 25 1983 to August 31 1992, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the Fund Accountability Statement and not to provide assurance on the internal control structure.

The management of MOF/CBK are responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure, policies and procedures. The objectives of an internal control structure are to provide management with a reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of the Fund Accountability Statement in accordance with the basis of accounting described in Note 1 to the Fund Accountability Statement. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in condition or that the effectiveness of the design and operations of policies and procedures may deteriorate.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

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#### CONTROL ENVIRONMENT

- Financial Management
- Management Control Methods
- Familiarity with USAID Rules

#### ACCOUNTING SYSTEMS

- General Record Keeping
- Reporting to USAID
- Disbursement of Funds

#### CONTROL PROCEDURES

- Authorization of Transactions and Activities
- Written Procedures
- Job descriptions
- Bank Reconciliation

For the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed the control risk.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation for the internal control structure that, in our judgement, could adversely affect the entity's ability to record, process, summarize and report financial data consistent with the assertions of management in the Fund Accountability Statement.

The following reportable conditions were observed :

- . systems were inadequate to ensure proper monitoring and reconciliation of foreign procurement by MOF/CBK
- . MOF/CBK's controls were inadequate to ensure repayment to USAID when funds advanced by USAID were not disbursed to entrepreneurs
- . participating banks did not submit regular reports of letters of commitments to CBK and USAID
- . CBK's voucher filing & referencing system was poor
- . CBK did not maintain formal job descriptions in respect of key project personnel

Monitoring of promissory notes by CBK was inadequate

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses and, accordingly, would not necessarily disclose all reportable conditions that are considered to be material weaknesses as defined above. However, we believe the reportable conditions described above constitute a material weakness in view of the fact that disbursements of \$ 1,737,823 were ineligible or unsupported.

Financial information contained in this report may be privileged. The restrictions of 18 USC 1905 should be considered before any information is released to the public. This report is intended solely for the information of the MOF/CBK and the Agency for International Development but is not intended to limit the distribution of the report, if a matter of public record.

*Peter Waterhouse*

March 31 1993

**3.1 INTRODUCTION**

**3.1.1 Definition**

American Institute of Certified Public Accountants' (AICPA) Codification of Auditing Standards, Section 319, defines an organization's internal control structure as consisting of the policies and procedures established to provide reasonable assurance that a specific entity's objectives will be achieved. The internal control structure comprises three elements :

- . the control environment
- . the accounting system
- . control procedures.

The control environment reflects the overall attitude, awareness and actions of management. The accounting system consists of methods and records established to identify, assemble, analyze, classify, record and report transactions. Control procedures are those policies and procedures in addition to the control environment and accounting system that management has established to safeguard the organization's resources.

**3.1.2 Work Performed**

Our review of the auditees' internal control structure was directed towards those elements which relate to the nature of project funding. The review encompassed the following:

- . **CONTROL ENVIRONMENT**
  - Financial Management
  - Management Control Methods
  - Familiarity with USAID Rules
- . **ACCOUNTING SYSTEMS**
  - General Record Keeping
  - Reporting to USAID
  - Disbursement of Funds
- . **CONTROL PROCEDURES**
  - Authorization of Transactions and Activities
  - Written Procedures
  - Job descriptions
  - Bank Reconciliation

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In making our recommendations, we appreciate that this audit addresses the disbursements of RPE funds which was completed in 1992. Accordingly, to avoid our recommendations being necessarily redundant, we have worded many of the recommendations in such a way as to apply if the project is extended. We understand that the extension or otherwise of the project has yet to be determined.

## 3.2 FINDINGS AND RECOMMENDATIONS

### INTERNAL CONTROL STRUCTURE

We set out below a number of weaknesses in the RPE internal control systems in operation for the period under review. In view of the possibility of reflow funds continuing to be lent to new entrepreneurs, we believe that the implementation of the recommendations below should strengthen control and accountability for these funds.

#### 3.2.1 Finding on the MACS Reconciliation

We were unable to satisfactorily reconcile foreign procurement disbursement between the auditee records and those of USAID (MACS) as a result of inadequate recording systems. As noted in Note 3 to the Fund Accountability Statement, the CBK records are denominated in Kenya Shillings and the USAID MACS figures are denominated in US\$, while the transactions were effected in a variety of foreign currencies.

We were unable to establish a sufficient link between the Kenya Shilling figures of CBK and the US\$ figures of USAID. Using exchange rates either specific to the foreign transaction or estimated as the rate applicable at the time of the transaction, we have attempted to reconcile the auditee and USAID records (see Exhibit 2). Our results suggest that the US\$ equivalent of the CBK records exceeds the US\$ figures recorded in MACS. This difference, of \$ 200,927, is unexplained. In view of the fact that the reconciliation supports a US\$ equivalent in excess of the USAID figures, the Mission may decide not to pursue the matter further.

In any event, the difficulties in reconciliation highlight a weakness in internal control whereby records maintained by CBK and USAID in respect of foreign disbursements were insufficient as to promote reconciliation. In particular, Central Bank of Kenya relied on the participating banks advice in respect of foreign procurement, for it had no direct role in the funding of such procurement. As noted in Section 4.2, CBK's monitoring of participating banks in this respect was unsatisfactory. Unfortunately we are advised that USAID/Kenya and A.I.D./Washington have not maintained records classified by entrepreneur to bridge the reconciliation gap identified above.

#### **Recommendation No. 4**

- 4.1 The Mission should determine whether to pursue the reconciliation of foreign procurement, and if so the Mission should undertake further work in conjunction with CBK, A.I.D./Washington and the participating banks in order to reconcile the unexplained difference of \$200,927.
- 4.2 In future, documents should be prepared and circulated in respect of foreign procurement to assist proper monitoring of such funds by CBK, including the enforcement of agreement provisions in respect of bank reporting as discussed in Section 4.2 of this report.

#### **Auditee Comments (CBK)**

Despite Central Bank's calling for the submission of letters of commitment by the participating commercial banks under advice to USAID, the banks did not comply even after repeated reminders. The role of Central Bank was to obtain the equivalent Kenya shilling amounts for the purpose of accruing interest payments and subsequent amortization of the loan principal. The bank would not have been in a position to know whether foreign transactions took place in the absence of information from the participating commercial banks.

#### **USAID Comments**

The Mission does not believe it would serve a useful purpose to do further work to reconcile the difference and therefore requests that recommendation 4.1 be deleted.

Although USAID/Kenya has no future plans for foreign procurement under this program, the Mission will address recommendation 4.2 by considering several monitoring options if such a program is ever planned in future.

#### **Auditors' Response**

We accept the Mission's comments and recommendation 4.1 is now closed. USAID/Kenya's comments on recommendation 4.2 is accepted.

#### **3.2.2 Finding on Disbursement Systems**

Controls over total disbursements were inadequate when funds were disbursed by USAID on the strength of approved RPE forms, but for any one of a number of reasons the entrepreneurs elected not to accept RPE loan finance. In these cases we have found controls in place were ineffective, as these funds were neither reimbursed directly to USAID nor offset against future USAID reimbursements. This weakness is reflected in the incidence of ineligible costs.

**Recommendation No. 5**

Any extensions to the RPE project should require improved systems at CBK level to achieve the following objectives :

- . identify funds not disbursed by the participating banks
- . recover such funds from the participating banks in a timely fashion
- . repay the funds to USAID.

**Auditee Comments (CBK)**

Our records show that all funds received from USAID were paid to the participating commercial banks. In addition, upon receipt of advice from participating commercial banks, an amount was refunded to Central Bank and subsequently transferred to the RPE Project Account.

We were not in a position to know of any funds paid to the commercial banks which may have not been disbursed by the banks to their entrepreneurs or to the commercial banks' branches. We only dealt with head offices of commercial banks who would normally advise us of any undisbursed funds.

**USAID Comments**

The Mission concurs with the audit findings.

**Auditors' Response**

CBK comments are noted, and its identification of the failure of the internal control systems to allow it to know of funds not disbursed is the subject of this recommendation.

**3.2.3 Finding on Referencing Systems**

CBK adopted no clear referencing system for filing of RPE documents. We found that for the most part documents were filed in an "ad hoc" manner, particularly so in the case of correspondence files which amount to a collection of all sorts of correspondence ranging from the monthly bank reconciliation reports to the Treasury and USAID to CBK requests for cash advances from USAID. Tracing of documents was accordingly very difficult.

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**Recommendation No. 6**

**CBK should improve their RPE referencing and document filing system to improve the audit trail and promote easy access to key documents.**

**Auditee Comments (CBK)**

It is Central Bank's practice that non general ledger vouchers are not referenced. We have General Management files for correspondence on the projects and individual bank files for RPE 1 and 2 for the loans and loan vouchers separately.

**USAID Comments**

The Mission concurs.

**Auditors' Response**

Accepted.

**3.2.4 Finding on Job Descriptions**

CBK were unable to provide formal job descriptions for the personnel handling USAID funds at the Central Bank of Kenya. While we reviewed informal descriptions specifically prepared for us by the personnel during the audit, we believe the monitoring of the project funds would have been assisted by the preparation of formal job descriptions. Such descriptions would have clearly identified responsibilities and duties for RPE-related personnel, and would have assisted the matching of responsibilities to personnel's respective qualifications.

**Recommendation No. 7**

**CBK should prepare job descriptions for the personnel handling USAID funds.**

**Auditee Comments**

Although this is not a requirement under the Project Agreement, Central Bank prepared job descriptions of the key project personnel for the audit team.

The name and position of the officer responsible for administering the Special Account was supplied to USAID.

**USAID Comments**

The Mission concurs.

#### **Auditors' Response**

CBK comments in respect of the Project Agreement are accepted. We believe however, that the preparation of job descriptions reflecting the Government of Kenya's responsibilities under the Project Agreement might have reduced or prevented incidence of adverse audit findings noted in this report. We do not question the abilities of the CBK personnel, but we believe their roles could have been more strictly defined.

#### **3.2.5 Finding on Promissory Notes Expiry Dates**

The monitoring of promissory notes expiry at the Central Bank of Kenya was found to be inadequate. It was found that some of the promissory notes of some RPE funds loaned to banks had expired and that CBK had not always ensured renewal, thereby possibly endangering its security position with the participating banks.

#### **Recommendation No. 8**

CBK personnel should ensure that agreed promissory note procedures are followed. Before the six months promissory notes are about to expire, a renewal notice should be sent to commercial banks requesting renewal of their security.

#### **Auditee Comments**

Some banks did not comply with the stipulated period to submit promissory notes. However, payment of interest is through direct debit to the banks' accounts with us without any recourse and this ensures 100 per cent repayment of interest and principal. Hence, there is no danger of Central Bank's security position being compromised with the participating banks.

#### **USAID Comments**

The Mission concurs.

#### **Auditors' Response**

Accepted.

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## *Price Waterhouse*



### AGENCY-CONTRACTED AUDIT OF THE GOVERNMENT OF KENYA UNDER THE RURAL PRIVATE ENTERPRISE (RPE) PROJECT NO. 615-0220, LOAN NO. 615-T-020

#### SECTION 4: COMPLIANCE WITH GRANT AGREEMENT TERMS AND APPLICABLE LAWS AND REGULATIONS

##### INDEPENDENT AUDITOR'S REPORT

We have audited the Fund Accountability Statement prepared by the Central Bank of Kenya under the USAID Rural Private Enterprise Project Agreement No. 615-0220 for the period from August 25 1983 to August 31 1992 and have issued our opinion thereon dated March 31 1993.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards, issued by the Comptroller General of the United States (1988 revision) with the exception that we have not been subject to a quality control review by a non Price Waterhouse firm. Such reviews are not required or available to professional firms in Kenya. We do not believe that this departure has affected our audit. We were subject to a quality control review in July 1992 undertaken by a Price Waterhouse firm independent of our firm.

Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the Fund Accountability Statement is free of material misstatement.

Compliance with the terms of the agreement and referenced laws and regulations is the responsibility of MOF/CBK management. As part of obtaining reasonable assurance about whether the Fund Accountability Statement is free of material misstatement, we performed tests of MOF/CBK's compliance with certain provisions of agreement terms and referenced laws and regulations. However, our objective was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

Material instances of non compliance are failures to follow requirements, or violations of agreement terms and referenced laws and regulations that cause us to conclude that the aggregation of misstatements resulting from those failures or violations is material to the Fund Accountability Statement. The results of our tests of compliance disclosed the following material instances of non compliance :

- failure to reimburse USAID for amounts received but not disbursed to the entrepreneurs, resulting in ineligible costs of \$ 1,033,014, equivalent to Shs 24,786,823
- failure to reimburse USAID for amounts not used by the entrepreneurs for approved and intended purposes, resulting in ineligible costs of \$ 648,894, equivalent to Shs 15,570,000.

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We considered these material instances of noncompliance in forming our opinion on whether the RPE Project Fund Accountability Statement is presented fairly in all material respects, in conformity with the basis of accounting described in Note 1 to the Fund Accountability Statement, and this report does not affect our report on the Fund Accountability Statement dated March 31, 1993.

We noted certain immaterial instances of noncompliance that are reported in Section 4.2 of this report.

Except as described above, the results of our tests of compliance indicate that, with respect to the items tested Central Bank of Kenya complied, in all material respects, with the provisions referred to in the third paragraph of this report. With respect to items not tested, nothing came to our attention that caused us to believe that Central Bank of Kenya had not complied, in all material respects, with those provisions.

Financial information contained in this report may be privileged. The restrictions of 18 USC 1905 should be considered before any information is released to the public. This report is intended solely for the information of the MOF/Central Bank of Kenya and the Agency for International Development but is not intended to limit the distribution of the report, if a matter of public record.



March 31 1993

## **COMPLIANCE WITH AGREEMENT TERMS AND REFERENCED LAWS AND REGULATIONS**

### **4.1 INTRODUCTION**

USAID requires all grantees, regardless of the country of legal entity, to comply with the terms and conditions included in the project agreement and its attached provisions and referenced procurement regulations.

Steps performed in this audit to test compliance with the project agreement and related provisions included:

- a review of the agreement provisions and related regulations to identify those provisions and regulations which could have a material effect on the financial statements
- audit procedures including detailed testing to evaluate the auditee's compliance with these provisions and regulations.

### **4.2 FINDINGS AND RECOMMENDATIONS**

#### **4.2.1 Finding on Un-disbursed Loans**

Contrary to the RPE Project Agreement, certain funds provided by USAID as set out in Section 2.3.1 were never disbursed to the Intended entrepreneurs and were not repaid.

Our recommendation in this respect is set out in Section 2.3.

#### **4.2.2 Finding on Loans Applied Other than for Intended Purposes**

Contrary to the RPE Project Agreement, certain funds provided by USAID and disbursed by the banks were not used for intended purposes by the entrepreneurs.

Our recommendation in this respect is set out in Section 2.3.

#### **4.2.3 Finding on non Approved Foreign Bank for Offshore Procurement**

Contrary to the RPE Project Agreement, Kenya Commercial Bank used a non approved foreign bank (Banco DI Roma) to facilitate an offshore procurement for Kenya Marble Quarries.

#### Recommendation No. 9

- 9.1 The Mission should determine whether there has been any negative impact caused by the use of a non approved bank which might cause the Mission to disallow the expenditure claimed.
- 9.2 The USAID Mission should be the focal point of future foreign procurement schemes established in any extensions of the RPE Project, in order to closely monitor offshore procurement and ensure no non-approved foreign banks are used.

#### **Auditee Comments (CBK)**

Central Bank was not directly involved in the maintenance of foreign procurement until after the payment was effected by USAID. We were only advised of the date and amount of foreign currency paid by the bank upon our enquiry. We understand that the bank followed up the matter with USAID and it was settled.

#### **USAID Comments**

Recommendation 9.1 has no negative impact on the program. USAID/Kenya requests that this recommendation be deleted.

Recommendation 9.2 will be considered in future by examining several monitoring options should the Mission decide to have foreign procurement in future.

#### **Auditors' response**

We accept the Mission's comments and recommendation 9.1 is now closed.

#### **4.2.4 Finding on Foreign Procurement**

Contrary to the special provision paragraph F of PIL No. 40, we found no evidence of any reports of letters of commitment ever being submitted to CBK and USAID. Consequently, CBK's only source of information regarding foreign disbursements was the participating banks by way of RPE Form 2. If a commercial bank failed to submit an RPE Form 2, CBK would have no other source of information of foreign procurement. Some foreign procurement were later changed to local procurement making it difficult to reconcile participating banks records with CBK.

Our recommendation in this respect is set out in Section 3.2.1.

#### **4.2.5 Finding on Quarterly Reporting Systems**

Contrary to the RPE Project Agreement, quarterly reports to banks were found not to be regularly submitted by CBK. The reason given was that the CBK records would usually be lacking in details of up-to-date information owing to delays in the submission of requisite returns (Forms RPE 1 and 2) by participating banks.

**Recommendation No. 10**

**Quarterly reports should be a strict requirement to be followed by CBK in any extensions or restructures to this project.**

**Auditee Comments**

Reports to commercial banks were sent as and when there were changes for reconciliation. Sometimes there was nothing to report to the banks due to delays in getting tranches from USAID and more so due to the de-obligatory exercise between USAID, Treasury and Central Bank of Kenya towards the Project completion date.

**USAID Comments**

The Mission concurs.

**Auditors Response**

Accepted.

- 2/9

**EXHIBITS**

**I AUDIT SUMMARY : BANK / ENTREPRENEUR TESTING**

Local Disbursements

Foreign Procurements

**II MACS RECONCILIATION**



RURAL PRIVATE ENTERPRISE PROJECT  
AUDIT SUMMARY : BANK/ENTREPRENEUR TESTING

SECTION 1 : LOCAL DISBURSEMENTS

ENTREPRENEUR	AMOUNT DISBURSED K Shs	US\$ Equivalent	BANK LEVEL TESTING						ENTREPRENEUR LEVEL TESTING (SAMPLE BASIS ONLY)				SUMMARY US\$				
			SEEN & IN ORDER			AMOUNTS DISBURSED		AUTHOR-ISED	MATCHING	CORRESPOND-	IN AUDIT SAMPLE ?	VISITED ENTREPR	SIGHTED ASSETS	FUNDS USED AS INTENDED	ACCEPTED US\$	INELIGIBLE US\$	UNSUPP US\$
			APPLICATN	RPE 1	RPE 2	CBK TO BANK	BK TO ENTR		ACHIEVED	ENCE IN ORDER							
<b>Barclays Bank</b>																	
World Ltd	2,984,115	124,368	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	124,368				
Mr & Mrs Aggrey Wahome	4,000,000	166,704	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	166,704				
New Era Enterprises	2,000,000	83,352	Y	Y	Y	Y	N	N/A	N/A	Y	Y	Y		83,352			
Balosi Industries Ltd	800,000	25,006	Y	Y	Y	Y	N	N/A	N/A	Y	Y	Y		25,006			
Silver Holding	18,117,333	671,704	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	671,704				
Timsales Ltd	34,500,000	1,437,818	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	1,437,818				
Taploca Ltd	868,887	27,784	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	27,784				
Mrs Mar Investments Ltd	29,333,333	1,222,493	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	1,222,493				
G G Gichuru	2,240,000	93,354	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	93,354				
<b>Total Barclays Bank</b>	<b>92,441,448</b>	<b>3,852,581</b>											<b>3,744,223</b>	<b>106,358</b>	<b>0</b>		
<b>Standard Chartered Bank</b>																	
Leather Industries	10,000,000	418,759	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	418,759				
Kenamin Industries	5,430,887	228,328	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	228,328				
Colotec (K) Ltd	8,000,000	333,407	Y	Y	Y	Y	N	N	N	N	N	INELIG.		333,407			
Kenya Clay Products Ltd	23,300,000	971,048	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	971,048				
Ufuta Ltd	12,000,000	500,111	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	500,111				
Samuel Nyamu Kai	1,068,887	44,454	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y			44,454		
Malindi General Engineering	5,478,000	228,301	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N	N	UNSUPP.		228,301			
Idara Investment Ltd	1,000,000	41,676	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	41,676				
Marich Pass Field Study	2,000,000	83,352	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	83,352				
Nyolke Farm	3,682,000	152,617	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	152,617				
Athi Stores Ltd	13,333,333	555,679	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	555,679				
<b>Total Standard Chartered Bank</b>	<b>85,270,687</b>	<b>3,553,732</b>											<b>2,947,570</b>	<b>561,708</b>	<b>44,454</b>		
<b>TOTAL TESTED</b>	<b>325,259,271</b>	<b>13,555,475</b>	<b>13,555,475</b>						<b>10,945,284</b>				<b>11,817,652</b>	<b>1,681,008</b>	<b>55,915</b>		
<b>TOTAL DISBURSED</b>	<b>415,941,990</b>	<b>17,334,755</b>	<b>17,334,755</b>						<b>17,334,755</b>								
<b>COVERAGE</b>	<b>78.2%</b>	<b>78.2%</b>	<b>78.2%</b>						<b>63.1%</b>								

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RURAL PRIVATE ENTERPRISE PROJECT  
AUDIT SUMMARY : BANK/ENTREPRENEUR TESTING

SECTION 2 : FOREIGN PROCUREMENTS

ENTREPRENEUR	AMOUNT DISBURSED US\$	K Shs Equivalent	BANK LEVEL TESTING							ENTREPRENEUR LEVEL TESTING (SAMPLE BASIS ONLY)				SUMMARY US\$			
			SEEN & IN ORDER			AMOUNT DISBURSED	LIC IN ORDER	IMPORT LICENSE	MATCHING ACHIEVED	CORRESPOND- ENCE REVIEW	IN AUDIT SAMPLE ?	VISITED ENTREPR	SIGHTED ASSETS	FUNDS USED AS INTENDED	ACCEPTED US\$	INELIGIBLE US\$	UNSUPP US\$
			APPLICN	RPE 1	RPE 2												
<b>Kenya Commercial Bank/Finance</b>																	
<b>Kenya Commercial Bank</b>																	
Athi River Mining Ltd	448,407	11,478,840	Y	Y	Y	Y	Y	Y	Y	N			448,407				
<b>Kenya Commercial Finance</b>																	
Thika Rubber Industries	291,308	5,788,942	Y	Y	Y	Y	Y	Y	Y	N			291,308				
Kenya Marble Quarries	124,000	3,585,212	Y	Y	Y	Y	Wrong bank	Y	Y	N			124,000				
<b>Total Kenya Commercial Bank/Finance</b>	<b>863,713</b>	<b>20,848,794</b>											<b>863,713</b>	<b>0</b>	<b>0</b>		
<b>Barclays Bank</b>																	
Wardli Ltd	425,892	10,349,218	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	425,892				
Budi Investment Ltd	918,351	22,315,989	Y	Y	Y	Y	Y	Y	Y	N			918,351				
Raymond Woolen Mills (K) Ltd	965,308	18,918,958	Y	Y	Y	Y	Y	Y	Y	Y	Y	Y	965,308				
<b>Total Barclays Bank</b>	<b>2,309,551</b>	<b>51,582,163</b>											<b>2,309,551</b>	<b>0</b>	<b>0</b>		
<b>Standard Chartered Bank</b>																	
Saj Ceramics	1,292,821	34,143,402	Y	Y	Y	Y	Y	Y	Y	N			1,292,821				
<b>Total Standard Chartered Bank</b>	<b>1,292,821</b>	<b>34,143,402</b>											<b>1,292,821</b>	<b>0</b>	<b>0</b>		
<b>TOTAL TESTED</b>	<b>4,465,885</b>	<b>108,574,359</b>				<b>4,465,885</b>					<b>1,391,200</b>		<b>4,465,885</b>	<b>0</b>	<b>0</b>		
<b>TOTAL DISBURSED</b>	<b>4,665,318</b>	<b>110,568,200</b>				<b>4,665,318</b>					<b>4,665,318</b>						
<b>COVERAGE</b>	<b>95.7%</b>	<b>98.4%</b>				<b>95.7%</b>					<b>29.8%</b>						

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FUND ACCOUNTABILITY STATEMENT  
RURAL PRIVATE ENTERPRISE PROJECT  
PROJECT AGREEMENT NO.615-0220  
FOR PERIOD AUGUST 25 1983 TO AUGUST 31 1992

Exhibit II

RECONCILIATION OF CBK TOTALS TO USAID MACS RECORDS

	Note	PER CBK US \$	PER MACS US \$	DIFFERENCE US \$
<b>Local advances</b>				
Standard Chartered Bank		4,048,327	NO	
Barclays Bank		4,783,356	SPLIT	
Kenya Commercial Bank/Finance		<u>8,503,072</u>	PROVIDED	
<b>Total Local Advances</b>		<u>17,334,755</u>	<u>17,334,755</u>	<u>0</u>
<b>Foreign advances</b>				
Standard Chartered Bank		1,411,053 *	1,337,938	(73,115)
Barclays Bank		2,472,339 *	2,364,918	(107,421)
Kenya Commercial Bank/Finance		<u>982,853 *</u>	<u>962,462</u>	<u>(20,391)</u>
<b>Total Foreign Disbursements</b>		<u>4,866,245</u>	<u>4,665,318</u>	<u>(200,927)</u>
<b>Other advances</b>				
Technical advice payment : DH&S	2	<u>0</u>	<u>151,400</u>	<u>151,400</u>
<b>TOTAL USAID FUNDS ADVANCED</b>		<u><u>22,201,000</u></u>	<u><u>22,151,473</u></u>	<u><u>(49,527)</u></u>

\* US\$ equivalents implied from Shs denominated totals in CBK records, converted at exchange rates known where possible, and estimated exchange rates where actuals For Fund Accountability Statement purposes, CBK has used the USAID MACS dollar totals.

**Notes**

1. Foreign Currency Discrepancy

As noted in Section 1.2.4, audit testing of foreign procurements has been unable to satisfactorily reconcile USAID figures to the US\$ equivalents of CBK records.

2. Technical advice payment : DH&S

Expenditure in the amount of \$ 151,400 was paid to the project's external advisors out of loan funds at USAID's approval, for at that time the grant component had been fully utilised. However, as this is not an RPE loan or a CBK loan disbursement, it is excluded from CBK's Fund Accountability Statement.

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**APPENDICES**

**I MISSION COMMENTS**

**II AUDITEE COMMENTS**



UNITED STATES OF AMERICA  
AGENCY FOR INTERNATIONAL DEVELOPMENT  
USAID MISSION TO KENYA

UNITED STATES POSTAL ADDRESS  
US AID MISSION TO KENYA  
BOX 201  
APO NEW YORK, NEW YORK 09675

INTERNATIONAL POSTAL ADDRESS  
POST OFFICE BOX 30261  
NAIROBI, KENYA

July 9, 1993

Mr. Andrew P. Hagger  
Project Manager  
Price Waterhouse  
P.O. Box 41500  
Nairobi Kenya

**Subject: USAID Contracted Audit of the Rural Enterprises (RPE)  
Project: Draft Audit Report dated June 24, 1993.**

Dear Mr. Hagger:

USAID/Kenya provides the following comments on the subject audit report as requested in your letter dated June 24, 1993. For more detailed clarification these comments should be read in conjunction with the Central Bank of Kenya's (CBK's) comments which will be forwarded to you directly by CBK.

Recommendation No. 1 requests the Mission to determine the allowability and recover from Central Bank of Kenya, as appropriate, ineligible costs of \$1,033,013.

**Response:** USAID/Kenya concurs.

Recommendation No. 2 requests the Mission to determine the allowability and recover from Central Bank of Kenya, as appropriate, ineligible costs of \$648,894.

**Response:** In order to determine the allowability of these costs, USAID/Kenya needs to know the purposes for which the loans were used. USAID/Kenya requests that the purposes for which these loans were used be included in the final report.

Recommendation No. 3 requests the Mission to determine the allowability and recover from Central Bank of Kenya, as appropriate, unsupported costs of \$1,389,544.

**Response:** USAID/Kenya requests that you try to revisit the sampled entrepreneurs to determine whether the costs are still unsupported. Please amend the recommendation accordingly should the second audit visit be successful and the costs found to be supported.

Recommendation No. 4 requests that:

- (a) the Mission undertakes further work in conjunction with CBK, AID Washington and the participating banks in order to reconcile the unexplained differences.
- (b) in future, documents should be prepared and circulated in respect of foreign procurement to assist proper monitoring of such funds by CBK, including the enforcement of agreement provisions in respect of bank reporting as discussed in Section 4.2 of this report.

**Response:** 4 (a) The Mission does not believe it would serve a useful purpose to do further work to reconcile the difference. USAID maintained its records in US\$ while the CBK maintained its records in Kenya Shillings and the transactions were effected in a variety of foreign currencies. The auditors have noted the difficulty in reconciling because of the differing exchange rates used. The RPE project is now closed and the funds used to fund it have expired (FY 84 funds). In addition, USAID is not aware of any outstanding claims for the foreign procurement. As the MACS records reflect the actual disbursements made by AID/W, the Mission does not deem it necessary to determine why CBK's books show a higher disbursement than USAID. We request that the recommendation be deleted. Although USAID/Kenya has no future plans for foreign procurement under this program, the Mission will address recommendation 4 (b) by considering several monitoring options if such a program is ever planned in future.

Recommendation No. 5 requests that any extensions to the RPE project should require improved systems at CBK level to achieve the following objectives:

- . identify funds not disbursed by the participating banks
- . recover such funds from the participating banks in a timely fashion
- . repay the funds to USAID.

**Response:** USAID/Kenya concurs.

Recommendation No. 6 requires that CBK should improve their RPE referencing and document filing system to improve the audit trail and promote easy access to key documents.

**Response:** USAID/Kenya concurs.

Recommendation No. 7 requests that the Mission should require that CBK prepare job descriptions for the personnel handling USAID funds. .

**Response:** USAID/Kenya concurs.

Recommendation No. 8 requires CBK personnel to ensure that agreed promissory note procedures are followed. Before the six months promissory notes are about to expire, a renewal notice should be sent to commercial banks requesting renewal of their security.

**Response:** USAID/Kenya concurs.

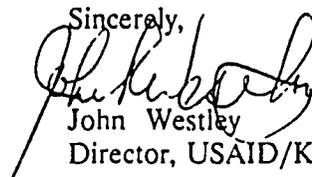
Recommendation No. 9 requests that:

- (a) the Mission to determine whether there has been any negative impact caused by the use of a non approved bank which might cause the Mission to disallow the expenditure claimed.
- (b) the Mission be the focal point of future foreign procurement schemes established in any extensions of the RPE Project, in order to closely monitor offshore procurement and ensure no non-approved foreign banks are used.

**Response:** Recommendation 9 (a) has no negative impact on the program. USAID/Kenya requests that this recommendation be deleted.  
Recommendation 9 (b) will be considered in future by examining several monitoring options should the Mission decide to have foreign procurement in future.

Recommendation No. 10 requires that quarterly reports should be a strict requirement to be followed by CBK in any extensions or restructures to this project.

**Response:** USAID/Kenya concurs.

Sincerely,  
  
John Westley  
Director, USAID/Kenya

CC: Mr. Jamasai Onyango  
Central Bank of Kenya  
P.O. BOX 60000  
Nairobi.

The Permanent Secretary  
Ministry of Finance  
P.O. BOX 30007  
Nairobi.

E. Cecile Adams, Mission Controller  
Everette Orr, RIG/A/N

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BANKI  
KUUYA  
KENYA



CENTRAL  
BANK OF  
KENYA

Ref: GM 862/1 Vol. X

July 26, 1993

1 Nile Sessue Avenue  
P.O. Box 60000 Nairobi Kenya

Mr. Andrew P. Hagger Telephone 22631 Telex 22321

Project Manager  
Price Waterhouse  
P.O. Box 41500  
NAIROBI

Dear Mr. Hagger,

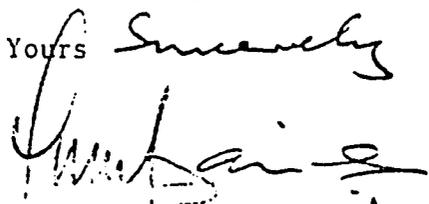
RE: USAID CONTRACTED AUDIT OF THE RURAL ENTERPRISES (RPE)  
PROJECT

Pursuant to your letter of June 24, 1993 pertaining to the Draft Audit Report on the above captioned programme, we are pleased to foreword to you our comments on the subject audit report.

We are of the opinion that a tripartite meeting comprising ourselves, as the Management Agency, the Treasury as the principal, USAID as the financiers be convened immediately by yourselves to discuss some fundamental aspects of the projects operational modalities which relate to the Central Bank's role and which we feel have not been treated objectively and adequately in the draft report prior to the enactment and adoption of the final report. We will then be in a position to sign the Letter of Representation after the requisite meeting.

Meanwhile, please accept our apology for the delay in submitting our reaction on the Draft Report within the scheduled time as it was occasioned by some circumstances beyond our control.

Yours

*Sincerely,*  


R.M. MARAMBA  
CHIEF BANKING MANAGER

CENTRAL BANK'S COMMENTS ON THE AUDIT  
REPORT ON THE USAID RURAL PRIVATE  
ENTERPRISE PROJECT

INTRODUCTION

Having perused the audit report of the USAID Rural Private Enterprise Project by M/s Price Waterhouse, we are of the view that the report is unnecessarily skewed negatively towards Central Bank of Kenya's perceived role in the project. The scope of the report purports to be limited to the loan component only while most of the adverse issues were directly the responsibility of the Project contractor.

It seems the auditors did not quite understand the designated role of the Central Bank in the project. The report is also quiet on the roles of USAID and the participating commercial banks and as it will be proved later, we do not agree with the assumption that the Fund Accountability Statement is entirely the responsibility of Central Bank. It was a joint responsibility with USAID and the Project contractor. We strongly believe that this report would have presented a fair and true picture of the project if at all the audit team had taken time to discuss the issues with us.

INTERNAL ACCOUNTING CONTROLS

1. Foreign Procurement:

The management of offshore procurements was directly under USAID and the participating commercial banks. The role of Central Bank was purely to receive transaction details, i.e. currency amount, payment date, and bank's client from both USAID and the banks in order to get the counterpart Kenya shilling equivalent for the purpose of accruing interest payments and subsequent principal loan amortisation.

The Bank would not have been in a position to know whether such transactions took place in the absence of such information. We took it upon ourselves to constantly seek this information from USAID and the commercial banks as evidenced by numerous correspondence in our files. Elsewhere in the report, the audit team admits that the Bank had no direct role in the funding of such procurements and that USAID, Nairobi and Washington did not maintain records on the same.

## 2. Disbursements

Our records show that all funds received from USAID were reimbursed to the participating commercial banks as evidenced by the USAID Rural Private Enterprise Project Account's balance which reads nil. However, upon advice by the participating commercial banks an amount of shs 3,066,666/= was paid back to Central Bank as prepaid loans. This amount was later, after opening of the USAID RPE Reflows Account, transferred to that account.

We must emphasise here that we would not have been in a position to know of any funds reimbursed by Central Bank of Kenya to commercial banks which may have not been disbursed by the banks to their entrepreneurs. Central Bank had no direct dealing with entrepreneurs or with commercial banks' branches. We only dealt with head offices of commercial banks who would normally advise us of any undisbursed funds. This same information would also be advised to us by the Project Contractor, who during their visits of the projects would know whether funds had been disbursed or not as spelt out in the Project Agreement. It is upon receipt of this advice that Central Bank would then debit the participating commercial bank concerned under advice to USAID, the bank and the Project Contractor.

Article D Section D.6 section (a) of the Project Agreement states that,

..../3

"In the case of any disbursement which is not supported by valid documentation in accordance with this Agreement, or which is not made or used in accordance with this Agreement or which was for goods or services not used in accordance with this Agreement, A.I.D., notwithstanding the availability or exercise of any other remedies provided for under this Agreement, may require the Government to refund the amount of such disbursement in United States Dollars to A.I.D. within sixty (60) days after receipt of a request thereof.

No request under the above case was made to us by USAID for payment.

Fund Accountability Statement

a) Funds never disbursed to Entrepreneurs

The Fund Accountability Statement was not only the responsibility of Central Bank of Kenya management but also of USAID management because it involved local, and offshore components and the grant component of the project loan.

It is stated in the audit report that the following loans reimbursed by Central Bank were not disbursed by the banks to their entrepreneurs:-

<u>Client</u>	<u>Amount Shs</u>	<u>US\$ Equivalent</u>
Standard Chartered Bank		
Colotec (K) Limited	8,000,000	337,408
Barclays Bank		
New Era Enterprises	2,000,000	83,352
Balori Industries	600,000	25,006
Kenya Commercial Finance Co.		
Apollo Kiarie	266,666	11,113
Karsan Ramji & Sons Limited	8,000,000	333,407
Union Textiles	5,920,157	246,728
Total	25,786,823	1,033,013
	*****	*****

... '4

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According to our records, loans to M/s New Era, Baloci Industries, Apollo Kiarie and Western Printers (under Kenya Commercial Bank which is not included in the report) were repaid by the banks to us and funds were transferred to the USAID RPE Reflows A/c. These funds were subsequently reduced (off-set) from our requests for funding to USAID since USAID did not request for payment under the project agreement. We were not advised either by the banks or the Project Contractor of the other loans not disbursed, and so, according to us, these loans are running and we consider them to be performing under the project terms.

b) Funds not used for intended purposes

<u>Client</u>	<u>Amount Shs</u>	<u>US \$ Equivalent</u>
Standard Chartered Bank		
Malindi Gen. Engineering	5,478,000	228,301
Kenya Commercial Finance Co.		
Malaa Industries	10,092,000	420,593
	<u>15,570,000</u>	<u>648,894</u>
	=====	=====

As we were not advised of these loans as not having been disbursed to the users, we consider them as performing, and are accordingly included in our running amortisation schedule.

c) Unsupported Costs

Following the audit team's visits to sampled entrepreneurs, the team came up with some costs claimed from USAID which they consider unsupported.

...../5

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<u>Client</u>	<u>Amount Shs</u>	<u>US\$ Equivalent</u>
Standard Chartered Bank		
Samuel Kai	1,066,667	44,454
Ufuta limited	12,000,000	500,111
Kenya Commercial Bank		
Francis Giathi	275,000	11,461
Kenya Commercial Finance Co.		
Kakuzi Limited	20,000,000	853,518
Total	33,341,667	1,389,544

The above loans were reimbursed to commercial banks locally upon their requests as required under the project. If at all the funds were put by the entrepreneurs to unsupported uses, the Project Contractor during their visits would have notified the banks, USAID and Central Bank and the appropriate action would have been taken. We, therefore, consider these loans as performing under the project terms.

4. Letters of Commitment Reports

Despite Central bank's calling for the submission of letters of commitment by the participating commercial banks under advice to USAID, the banks did not comply even after repeated reminders. We believe USAID would have played its role here as it was managing the foreign procurement element of the loan. Central Bank's role here was to obtain the equivalent Kenya shilling amounts for the purpose of accruing interest payments and subsequent amortisation of the principal loan.

5. Voucher referencing System

It is a normal practice in Central Bank of Kenya that non-general ledger vouchers are not referenced so our failure to

reference the USAID vouchers is not a default. We have General Management files for correspondence on the projects and individual bank files for RPE 1 and 2 for the loans and loan vouchers separately. These are in addition to the data we run in the computer system parallel to the manual system.

6. Formal Job Descriptions

It is alleged that Central Bank of Kenya did not maintain formal job descriptions in respect of key project personnel. We must emphasise that although this is not a requirement under the Project Agreement, Central Bank gave the audit team job descriptions prepared by the key project personnel i.e. Mr. Onyango and his assistant in the project Mr. Muthiani as requested. The work load was minimal to warrant assigning these two to the project's work only.

Article 5 (a) of the Project Agreement required the Government of Kenya to furnish to A.I.D. the name and position held by the officer at the Central Bank of Kenya who would be responsible for administering the Special Account. This information was supplied to USAID and they know the contact person at Central Bank of Kenya for the project who has been and still is Mr. Onyango, a senior superintendent with over 17 years Central Banking experience.

7. Monitoring of Promissory Notes

Some banks due to their wide branch network, when called upon to submit promissory notes did not comply within the stipulated period. We took it upon ourselves, instead of recalling the facility, to press the banks through moral suasion to submit the promissory notes. We used to send renewal notices requesting for new notes before the expiry dates.

Payment of interest is through direct debit to the banks' accounts with us without any recourse and this ensures 100 per cent repayment.



of interest and principal. Hence, there is no danger of CBK's security position being compromised with the participating banks.

8. Failure to use USAID - Approved bank for off-shore Procurement  
Kenya Commercial Bank once used a non-approved foreign bank to facilitate an off-shore procurement for Kenya Marble Quarries. As mentioned earlier, the Bank was not directly involved in the maintenance of foreign procurement until after payment was effected by USAID. The Bank was, therefore, not in a position to know whether the entrepreneur used a foreign bank that was not approved by USAID. We were only advised of the date and amount of foreign currency paid by the bank upon our enquiry. We are made to understand that the bank took up the matter with USAID and it was settled.

9. Quarterly Reporting

Reports to commercial banks were sent as and when there were changes for reconciliation. Sometimes there was nothing to report to the banks due to delays in getting tranches from USAID and more so due to the de-obligatory exercise between USAID, Treasury and Central Bank of Kenya towards the Project completion date.

CONCLUDING REMARKS

The Central Bank's internal controls and reporting systems as pertains to the monitoring of this project were very elaborate, consistent and foolproof. They were designed in such a manner that all the funds' movements initiated by ourselves were discernibly accountable and traceable by USAID and the Project Contractor.

CENTRAL BANK OF KENYA

DEVELOPMENT DIVISION

7th July, 1993

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REACTIONS BY SOME PARTICIPATING BANKS ON SOME PERTINENT  
ISSUES RAISED IN THE REPORT.....

01/15/2000

CLIENT	LOAN AMOUNT	ACTION TAKEN
<b>KENYA COMMERCIAL FINANCE CORP.</b>		
1) Karsan Ramji & Sons	8,000,000=	) Loan cancelled, funds placed in suspense Account, treated in CBK books as running and hence principal and interest being recovered normally.
2) Union Textiles	5,920,157=	)
3) Malaa Industries	10,092,000=	) Facility cancelled and funds recalled. There is an outstanding balance of shs 50,000=.
4) Kaku: i Ltd.	20,000,000=	) The bank feels the audit team should have arranged the visit to the entrepreneur through them.
5) Kenya Marble Quarries	3,585,212=	) The problem arose through the branch's oversight and was settled between the branch and USAID.

**KENYA COMMERCIAL BANK**

1) Francis Giathi	275,000=	The machinery was stolen but the loan is being serviced to the bank satisfactorily.
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**STANDARD CHARTERED BANK**

1) Samuel Kai	1,066,667=	The bank is aware that the Dry Cleaning machine has been transferred from Burnt forest to Nairobi as a result of tribal clashes. Loan being serviced normally.
2) Ufusa Ltd.	12,000,000=	The plant was closed due to unavailability of raw material. The loan was taken over by M/s Kenya National Mills, a member of Unga Group with the bank's permission and it is being serviced well.

3) Colotec (K) Ltd.	8,000,000	The loan was cancelled because the entrepreneur could not raise enough security. The bank has been holding the funds pending refund to CBK. Meanwhile the CBK recovers the principal and interest normally.
4) Malindi Gen. Engineering	5,479,000=	This was due to weak management by the branch which failed to monitor the usage of funds. They realised the security to recover the funds

The banks state that the above facts were made known to the Project Contractor who visited the projects, whose major role included physical verification and monitoring of the projects.

SB

ATTACHMENT II

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