

Regional Inspector General for Audit
Nairobi, Kenya

Audit of
the Technical Assistance to the
Capital Markets Authority Under
USAID/Kenya Project No. 615-0240

Report No. 3-615-94-014-N
August 31, 1994



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RELEASED TO THE PUBLIC.**





U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

August 31, 1994

Memorandum

To: Acting Director, USAID/Kenya, Kiert Toh
From: Acting RIG/A/Nairobi, David M. Conner
Subject: Agency-contracted Audit of the Technical Assistance to the Capital Markets Authority Under USAID/Kenya Project No. 615-0240, A.R. No. 3-615-94-014-N

*Regional
Inspector General
for Audit/Nairobi*

Attached are five copies of the subject audit report by the non-Federal accounting firm of Bellhouse Mwangi Ernst & Young, Nairobi, Kenya.

The Structural Adjustment Assistance Program (SAAP) Technical Assistance Project was signed on May 15, 1987 to provide technical assistance, training and commodities to support the analysis and implementation of Kenya's SAAP. The Capital Markets Development component of this project was designed to provide technical assistance in analyzing legislative requirements for the establishment of a Capital Markets Authority (CMA) and implementation once the CMA was established. USAID funding for the CMA component was initially authorized at \$600,000 but was later increased to \$775,000. As of August 31, 1993, \$453,826 had actually been disbursed.

The objective of the audit was to examine CMA's Fund Accountability Statement (Statement) and to express an opinion as to whether the Statement presents fairly the use of funds in accordance with the grant agreement. To answer the objective, the auditors were asked to consider CMA's internal control structure to determine auditing procedures necessary to express an opinion on the Statement, and to report on significant internal control weaknesses. As part of obtaining reasonable assurance the Statement was free of material misstatement, the auditors were required to test CMA's compliance with terms of the grant agreement and to report any identified material instances of non-compliance.

This audit covered all USAID funds disbursed to the CMA under Project No. 615-0240 amounting to \$453,826 for the period May 15, 1987, through August 31, 1993. The auditors selected an audit sample of \$412,453, which constituted 91 percent of the audit universe. The scope of the audit was limited by the auditors' reliance on USAID/Kenya's representations and photocopies of supporting documentation for expenditures amounting to \$88,539.

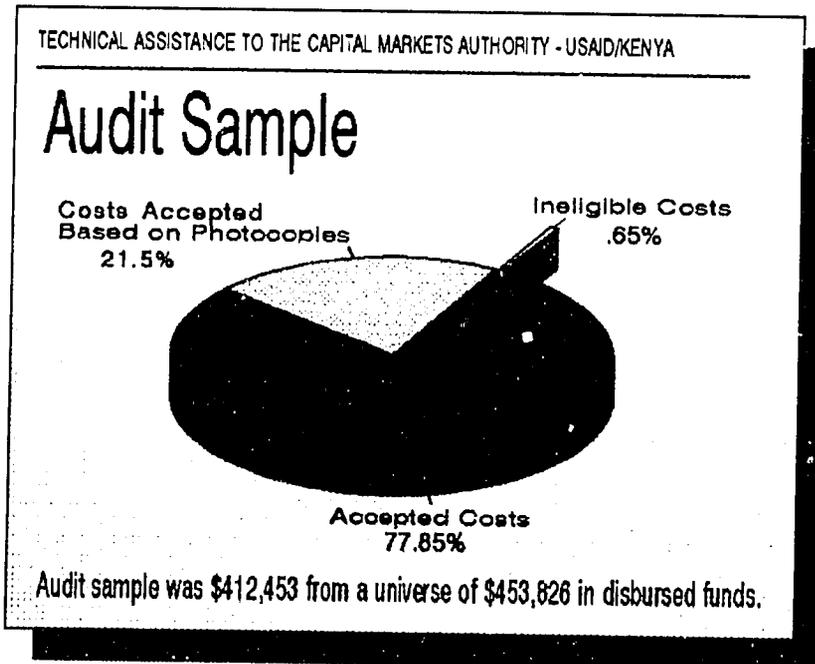
The auditors issued a qualified opinion on CMA's Statement since the audit identified \$2,698 in questioned ineligible costs and the aforementioned scope limitation. The audit identified three material instances of noncompliance with the grant agreement. The report on the internal control structure identified six areas that the auditors considered to be material weaknesses. Weaknesses identified can be summarized as follows:

- **inadequate accounting records maintained and a lack of written financial and accounting procedures, and**
- **incomplete accounting for USAID-funded commodities.**

The draft report was submitted to CMA and to USAID/Kenya for comments. CMA did not comment on the contents of the draft report. USAID/Kenya's comments were taken into consideration in the preparation of the final report and included in the final report as Appendix I. USAID/Kenya generally

agreed with the audit findings and recommendations included in the audit report but declared that \$88,539 in costs originally questioned as unsupported should be considered allowable costs as USAID had either placed the original supporting documentation in its archives or had them destroyed.

The report contains 11 recommendations concerning the questioned costs, internal control weaknesses, and compliance issues. It is USAID/Kenya's



responsibility to ensure appropriate action is taken on all the recommendations. We are including the following recommendations in the Office of the Inspector General's audit recommendation follow-up system:

Recommendation No. 1: We recommend that USAID/Kenya determine the allowability, and recover as appropriate from the Capital Markets Authority, questioned ineligible costs of \$2,698.

- 2 -

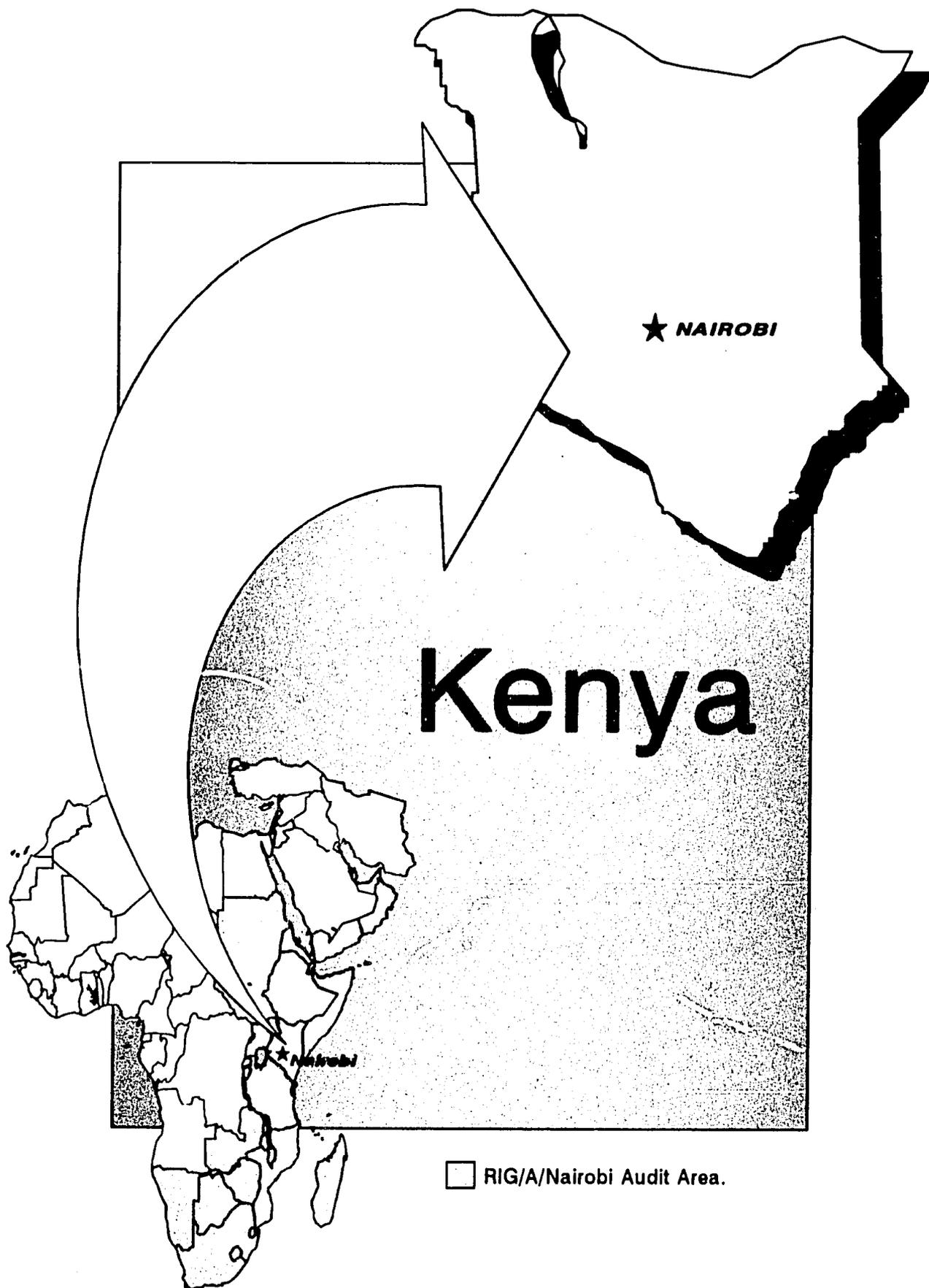
Recommendation No. 2: We recommend that USAID/Kenya obtain from the Capital Markets Authority a plan to improve its internal control structure which would include:

- 2.1 ensuring financial and accounting procedures are established;**
- 2.2 ensuring an accounting system is adopted that includes such records as project ledgers, creditor ledgers and debtor ledgers;**
- 2.3 ensuring all fixed asset acquisitions and disposals are recorded in its fixed assets register.**

We consider the recommendations to be unresolved. Recommendation No. 1 will be resolved when USAID/Kenya makes a final determination as to the allowability of the questioned costs. It can be closed when USAID/Kenya takes action appropriate to the determination. Recommendation No. 2 will be resolved when RIG/A/N receives an acceptable plan for corrective action and can be closed upon implementation of the corrective action. Please respond to this report within 30 days indicating action planned or taken to implement the recommendations.

Thank you for the cooperation extended to Bellhouse Mwangi Ernst & Young auditors and the Regional Inspector General for Audit representatives during the audit.

Attachments: a/s.



**Audit of
the Technical Assistance to the
Capital Markets Authority Under
USAID/Kenya Project No. 615-0240**

A.R. No. 3-615-94-014-N

ATTACHMENTS

**Audit of
the Technical Assistance to the
Capital Markets Authority Under**

USAID/Kenya Project No. 615-0240

**THE AGENCY-CONTRACTED
AUDIT OF THE STRUCTURAL ADJUSTMENT
ASSISTANCE PROGRAM - TECHNICAL ASSISTANCE
TO THE CAPITAL MARKETS AUTHORITY UNDER
USAID/KENYA PROJECT NO. 615-0240**

**THE STRUCTURAL ADJUSTMENT ASSISTANCE PROGRAM
 TECHNICAL ASSISTANCE TO THE CAPITAL MARKETS
 AUTHORITY UNDER USAID/KENYA
 PROJECT NO. 615-0240**

TABLE OF CONTENTS		PAGE
GLOSSARY OF TERMS		
SECTION		
1.	INTRODUCTION	
1.1	Background	1
1.2	Audit Objectives and Scope	1
1.2.1	Objectives	1
1.2.2	Scope	2
1.2.3	Methodology	2
1.3	Summary of Audit Results	2
1.3.1	Fund Accountability Statement	2
1.3.2	Internal Control Structure	3
1.3.3	Compliance with Grant Agreement and related provisions	3
1.3.4	Capital Markets Authority's Response	3
1.3.5	USAID/Kenya comments	3
2.	FUND ACCOUNTABILITY STATEMENT	
2.1	Independent Auditor's Report	5
	Fund Accountability Statement	7
2.2	Findings and Recommendations	8
2.2.1	Introduction	8
2.2.2	Sample Selection Criteria	8
2.2.3	Audit Results	8
2.2.4	Ineligible Costs	9
3.	INTERNAL CONTROL STRUCTURE	
3.1	Independent Auditor's Report	10
3.2	Work Performed	13
3.3	Findings and Recommendations	13
3.3.1	Accounting Systems	13
3.3.2	Control Procedures	15

**4. COMPLIANCE WITH GRANT AGREEMENT PROVISIONS
AND APPLICABLE LAWS AND REGULATIONS**

4.1	Independent Auditor's Report	16
4.2	Work Performed	18
4.3	Findings and Recommendations	18

APPENDICES

APPENDIX I	USAID/Kenya comments	
APPENDIX II	Costs supported by photocopies and USAID/Kenya's representations	

THE STRUCTURAL ADJUSTMENT ASSISTANCE PROGRAM
TECHNICAL ASSISTANCE TO THE CAPITAL MARKETS
AUTHORITY UNDER USAID/KENYA
PROJECT NO. 615-0240

GLOSSARY OF TERMS

USAID	:	UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT
US	:	UNITED STATES OF AMERICA
\$:	US DOLLARS
KShs	:	KENYA SHILLINGS
CMA	:	CAPITAL MARKETS AUTHORITY
SAAPTAP	:	STRUCTURAL ADJUSTMENT ASSISTANCE PROGRAM TECHNICAL ASSISTANCE PROJECT
NSE	:	NAIROBI STOCK EXCHANGE

**THE STRUCTURAL ADJUSTMENT ASSISTANCE
PROGRAM TECHNICAL ASSISTANCE TO
THE CAPITAL MARKETS AUTHORITY UNDER
USAID/KENYA PROJECT NO. 615-0240**

1. INTRODUCTION

1.1 Background

The Structural Adjustment Assistance Program Technical Assistance Project (SAAPTAP) was authorized on May 15, 1987 as part of the overall Structural Adjustment Assistance Program (SAAP) which was initially authorized on June 6, 1986 to provide technical assistance, training and commodities to support the analysis and the implementation of the SAAP. The six substantive components of SAAPTAP are:

- i. Sectoral Policy Analysis and Planning
- ii. Microcomputerization of the Budget Process
- iii. Capital Markets Development
- iv. Commodity Import Program (CIP) Monitoring
- v. Tax Modernization
- vi. Studies and Evaluation.

The Capital Markets Development component was designed to provide technical assistance in analyzing legislative requirements for the establishment of a Capital Markets Authority (CMA) and to continue to provide technical assistance in implementation once the authority was established. The estimated project assistance completion date was December 31, 1993.

The initial amount authorized for the CMA component was \$ 600,000, but this was incrementally funded to \$ 775,000 as of July 2, 1992. As of August 31, 1993, \$453,826 had been disbursed.

1.2 Audit Objectives and Scope

1.2.1 Objectives

Bellhouse Mwangi Ernst & Young were appointed by USAID under Contract No. 623-0000-I-00-2006-00 to carry out the audit of the CMA component of SAAPTAP for the period May 15 1987, through August 31, 1993.

The objectives of this engagement were to:

- a. Audit CMA's 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 funds in accordance with the Grant Agreement;

- b. Consider the CMA's internal control structure in order to determine the auditing procedures for purposes of expressing an opinion on the Fund Accountability Statement and to report on significant internal control deficiencies and material weaknesses;
- c. Test CMA's compliance with the terms of the Grant Agreement, as part of obtaining reasonable assurance as to whether the Fund Accountability Statement is free of material misstatement, and to report on any identified material instances of noncompliance; and
- d. To ensure that CMA's commodities listing could be reconciled to USAID/Kenya records.

The audit was undertaken in accordance with generally accepted auditing standards and the Government Auditing Standards issued by the US Comptroller General (1988 Revision). We were required to adhere to guidelines contained in the "Guide for Financial Audits Contracted by AID" and "Guidelines for Audits of Federal awards to Non-Profit Institutions".

1.2.2 Scope

Our audit covered all USAID funds disbursed to the CMA under Project No. 615-0240 amounting to \$ 453,826 for the period May 15 1987, through August 31, 1993.

In carrying out our audit, we did not comply with Government Auditing Standards 3.46 and 3.6 regarding External Quality Control Reviews and Continuing Professional Education respectively. It is our opinion that noncompliance with those standards did not impair our ability to perform the audit.

1.2.3 Methodology

The audit was performed using the Ernst & Young audit approach as modified by the Public Sector Services Manual Supplement.

A review of the project documentation was performed on January 14, 1994 at the CMA's offices after which an audit program was prepared for the approval of the Regional Inspector General/Audit/Nairobi (RIG/A/N). The audit fieldwork commenced immediately thereafter.

1.3 Summary of Audit Results

1.3.1 Fund Accountability Statement

Of the total expenditures for the period amounting to \$ 453,826 our sample for verification covered \$ 412,453 (91%). Of the amounts verified, costs amounting to \$ 2,698 (0.6%) were questioned all being ineligible.

1.3.2 Internal Control Structure

The following weaknesses in the internal control structure were noted:

- i. Lack of written financial and accounting procedures.
- ii. Failure to retain copies of original documents supporting project expenditures, submitted to USAID for reimbursement.
- iii. Failure to account for expenditures paid for directly by USAID to vendors.
- iv. Inadequate books of account.
- v. Incomplete accounting for commodities.
- vi. Lack of reconciliation between CMA and USAID financial records on the project and periodic financial reports on the project.

1.3.3 Compliance with Grant Agreement and related provisions

The following instances of noncompliance with the standard provisions of the Grant Agreement were noted:

- i. Inadequate and incomplete books and records relating to the project.
- ii. Incurrence of first class air travel costs.
- iii. Failure to publicize USAID participation on project sites and USAID's commodity purchases.

1.3.4 Capital Markets Authority Response

We had not received the Capital Markets Authority's response to the audit findings as at July 27, 1994.

This was after the expiry of the 30 day period within which the Capital Markets Authority was expected to respond.

1.3.5 USAID/Kenya comments

i. Fund Accountability Statement

Original supporting documents in respect of expenditures were received and retired by USAID/Kenya according to applicable procedures. Questioned expenditures amounting to \$88,539 classified as unsupported in the draft audit report should therefore be treated as allowable.

In respect of a first class fare amount of \$6,699, \$4,502 has been determined as the equivalent economy class fare. CMA should therefore refund the balance of \$2,197 to USAID/Kenya.

ii. Internal Control Structure

USAID/Kenya concurs with the recommendations.

iii. Compliance with Grant Agreement and related provisions

USAID/Kenya concurs with the recommendations.

**THE STRUCTURAL ADJUSTMENT ASSISTANCE PROGRAM
TECHNICAL ASSISTANCE TO THE CAPITAL MARKETS
AUTHORITY UNDER USAID/KENYA
PROJECT NO. 615-0240**

2. FUND ACCOUNTABILITY STATEMENT

2.1 Independent Auditor's Report

We have audited the Fund Accountability Statement of the Capital Markets Authority under Project No. 615-0240 for the period May 15, 1987, through August 31, 1993. This statement is the responsibility of the Capital Markets Authority. Our responsibility is to express an opinion on this statement based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards (1988 Revision) issued by the U.S. Comptroller General with the exception that we did not comply with sections 3.46 and 3.6 on External Quality Control Reviews and Continuing Professional Education. These standards required that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statement is free of material misstatement. Our audit included examining, on a test basis, evidence supporting the amounts and disclosures in the Fund Accountability Statement.

Our audit also included assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall Fund Accountability Statement presentation. We believe that our audit provided 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 principles.

The scope of our audit was limited by our reliance on photocopies of supporting documentation and USAID/Kenya's representations for expenditures amounting to \$88,539 (See Appendix II).

With respect to incurred expenditures, the results of our audit include questioned costs of \$2,698 considered to be ineligible.

Subject to the foregoing in our opinion, the Fund Accountability Statement presents fairly, in conformity with the basis of accounting described in the fourth paragraph above, the revenues and expenses of the Capital Markets Authority under Project No. 615-0240 for the period May 15, 1987, through August 31, 1993.

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 Government of Kenya through the Capital Markets Authority, and the United States Agency for International Development but this is not intended to limit the distribution of the report if a matter of public record.



**BELLHOUSE MWANGI ERNST & YOUNG
NAIROBI**

April 30, 1994

**THE STRUCTURAL ADJUSTMENT ASSISTANCE PROGRAM
 TECHNICAL ASSISTANCE TO THE CAPITAL MARKETS
 AUTHORITY UNDER USAID/KENYA PROJECT NO. 615-0240
 FUND ACCOUNTABILITY STATEMENT FOR THE PERIOD
 MAY 15, 1987 THROUGH AUGUST 31, 1993**

	US \$
Total Revenue	453,826
Expenditures:	
Capital expenses	117,092
Operating expenses	24,664
Technical assistance	193,922
Training	111,449
Nairobi Stock Exchange Support	6,699

Total Expenditures	453,826

Fund balance	-
	=====

Notes to the Fund Accountability Statement

1. Basis of Accounting

The Fund Accountability Statement is prepared on the basis of cash receipts and disbursements which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles.

2. Costs supported by photocopies and USAID/Kenya representations

Expenditures amounting to \$65,650 and \$22,889 included under capital and technical expenses respectively were accepted on the basis of USAID/Kenya representations and photocopies of supporting documentation. (See Appendix II).

2.2 Findings and Recommendations

2.2.1 Introduction

The Fund Accountability Statement was prepared from the PO4 paytrack records maintained by USAID/Kenya and is on page 7 of this report.

2.2.2 Sample Selection Criteria

For the expenditures incurred under the project, we established a key item value of \$ 4,500 and tested all transactions whose value was equal to or greater than this amount. This gave us a coverage of 91%. We considered this coverage to be adequate to enable us to form our opinion.

2.2.3 Audit Results

Of the total disbursements of \$453,826, \$451,128 were considered to be acceptable and \$ 2,698 (0.6%) were questioned. The questioned costs were all under ineligible costs. These costs can be analyzed as follows:

	Claimed	Accepted	Questioned		Note
	\$	\$	Unsupported	Ineligible	
	\$	\$	\$	\$	
Capital expenses	117,092	116,591	-	501	2.2.4(ii)
Operating expenses	24,664	24,664	-	-	
Technical assistance	193,922	193,922	-	-	
Training	111,449	111,449	-	-	
Nairobi Stock Exchange Support	6,699	4,502	-	2,197	2.2.4(i)
	<u>453,826</u>	<u>451,128</u>	<u>-</u>	<u>2,698</u>	
	=====	=====	=====	=====	

2.2.4 Ineligible Costs

i. Finding : Ineligible Nairobi Stock Exchange Support Costs

	Date	Details	Amount \$	Remarks
a.	08.23.93	Reimbursement of Airfare to T Cheng while attending Africa Stock Exchange Conference	2,197	Mr Cheng travelled first class. An amount of \$6,699 was authorized in a Project Implementation Letter (PIL) but there was no mention of first class travel in the PIL. The amount of \$2,197 represents the balance between the claimed amount and the equivalent economy class fare of \$4,502.

Recommendation No. 1.

We recommend that USAID determine allowability of the above cost.

USAID/Kenya Comments

Mission determines that the economy class fare equivalent to \$4,502 is allowable. CMA should refund the balance of \$2,197 being the ineligible amount.

Auditor's Response

We concur with Mission's determination.

ii. Finding: Ineligible capital expenses

	Date	Details	Amount \$	Remarks
	03.10.90	Capital expense incurred by NSE	501	Cost of one extra-large table disposed of without USAID approval

Recommendation No. 2

Our Recommendation No. 1 applies to this finding.

USAID/Kenya Comments

USAID/Kenya concurs with the recommendation.

**THE STRUCTURAL ADJUSTMENT ASSISTANCE
PROGRAM TECHNICAL ASSISTANCE TO
THE CAPITAL MARKETS AUTHORITY UNDER
USAID/KENYA PROJECT NO. 615-0240**

3. INTERNAL CONTROL STRUCTURE

3.1 Independent Auditors' Report

We have audited the Fund Accountability Statement of the Capital Markets Authority under Project No. 615-0240 for the period May 15, 1987 through August 31, 1993 and have issued our report thereon dated April 30, 1994.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards (1988 Revision) issued by the U.S. Comptroller General. These standards required that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statement is free of material misstatement.

In planning and performing our audit of the Fund Accountability Statement we considered the internal control structure established by the Capital Markets Authority in so far as it relates to grant funds, 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 the Capital Markets Authority is 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 reasonable, but not absolute assurance that the assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with the management's authorization and recorded properly to permit the preparation of the Fund Accountability Statement in accordance with generally accepted accounting principles. 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 conditions or that the effectiveness of the design and operation of policies may deteriorate.

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

Control Environment

- financial management capabilities
- familiarity with USAID rules

Accounting System

- budgeting and funds management
- general record keeping
- reporting to USAID
- disbursement of USAID funds.

Control Procedures

- authorization of transactions and activities
- written procedures

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

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under the 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 of the internal control structure that in our judgement could adversely affect the organization's ability to record, process, summarize and report financial data consistent with the assertion of management in the Fund Accountability Statement.

The following reportable conditions were observed:

- a. Lack of written financial and accounting procedures.
- b. Failure to retain copies of original documents supporting project expenditures submitted to USAID for reimbursement.
- c. Failure to account for expenditures paid for directly by USAID to vendors.
- d. Inadequate books of account maintained.
- e. Incomplete accounting for commodities.
- f. Lack of reconciliation between CMA and USAID financial records on the project and periodic financial reports on the project.

A material weakness is a condition in which the design or operation of one or more of the 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 Fund Accountability Statement 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 reportable conditions 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 are material weaknesses.

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 for the information of the Government of Kenya through the Capital Markets Authority, and the United States Agency for International Development but this is not intended to limit the distribution of the report if it is a matter of public record.



**BELLHOUSE MWANGI ERNST & YOUNG,
NAIROBI**

April 30, 1994

3.2 Work Performed

We reviewed the internal control structure of the Capital Markets Authority and obtained an understanding of the design, relevant procedures and we assessed control risk. Our review considered the significant internal control structure and procedures categorized as follows:

Control environment

- financial management capabilities
- familiarity with USAID rules

Accounting systems

- budgeting and funds management
- general record keeping
- reporting to USAID
- disbursement of USAID funds

Control procedures

- authorization of transactions and activities
- written procedures

3.3 Findings and Recommendations

3.3.1 Accounting Systems

a. Finding : Lack of written procedures

Being an organization autonomous from the Government, the CMA does not have written financial and accounting procedures, but follows the Government accounting procedures.

Recommendation No. 3

We recommend that the CMA should establish its own accounting and financial procedures that do not conflict with the requirements of the law or Government of Kenya regulations and have these written down as a permanent record for reference.

USAID/Kenya comments

USAID/Kenya concurs with the recommendation.

b. Finding: Incomplete document retention

As required by USAID regulations, the CMA claimed from USAID and were reimbursed allowable costs incurred on the project after submitting the original documents supporting such costs. However, we noted that the CMA, being the project implementation agency, did not retain copies of some of the original supporting documents, thus cannot have a full accounting of the project.

Recommendation No. 4

We recommend that the CMA obtain copies of all original documents supporting project costs and retain these as required by the Grant Agreement.

USAID/Kenya comments

USAID/Kenya concurs with the recommendation.

c. Finding : Inadequate books of Account

The CMA does not maintain the minimum books of account as required and found in a conventional accounting system, but only a cash book and votebook which also serves as a general ledger.

Recommendation No. 5

We recommend that the CMA adopt and maintain books of account as found in a conventional accounting system, such as creditors ledger, debtors ledger, project ledger etc.

USAID/Kenya comments

USAID/Kenya concurs with the recommendation.

d. Finding : Inadequate Commodity Accounting

The CMA did not fully account for commodities funded by USAID under the project. The assets register did not include assets held by the Nairobi Stock Exchange (NSE). A list of all assets transferred to the NSE was available and the assets were physically verified, however it could not be determined whether these were assets funded by USAID.

Recommendation No. 6

We recommend that the CMA should account for all assets funded under the project in full by showing the acquisitions and subsequent disposals or transfer in its fixed assets register.

USAID/Kenya comments

USAID/Kenya concurs with the recommendation.

3.3.2 Control Procedures

a. Finding : Lack of Reconciliation between USAID and CMA Records

We noted that CMA did not prepare any reconciliations between its records and those of USAID. This meant that CMA did not have a complete record of payments made directly to vendors by USAID.

Recommendation No. 7

We recommend that CMA obtain USAID financial reports (PO4) and reconcile these to its financial records to ensure that it has complete records on the project.

USAID/Kenya comments

USAID/Kenya concurs with the recommendation.

b. Finding : Lack of Financial Reports on the Project

The CMA does not prepare periodic financial reports on the project. Such reports would assist in the monitoring of the financial performance of the project.

Recommendation No. 8

We recommend that the CMA prepare periodic financial reports specifically on the project to enable sound financial management of the project.

USAID/Kenya comments

USAID/Kenya concurs with the recommendation.

**THE STRUCTURAL ADJUSTMENT ASSISTANCE
PROGRAM TECHNICAL ASSISTANCE TO
THE CAPITAL MARKETS AUTHORITY UNDER
USAID/KENYA PROJECT NO. 615-0240**

**4. COMPLIANCE WITH GRANT AGREEMENT PROVISIONS
AND APPLICABLE LAWS AND REGULATIONS**

4.1 Independent Auditors' Report

We have audited the Fund Accountability Statement of the Capital Markets Authority under Project No. 615-0240 for the period May 15, 1987 through August 31, 1993 and have issued our report thereon dated April 30, 1994.

We conducted our audit in accordance with generally accepted auditing standards and Government Auditing Standards (1988 Revision) issued by the U.S. Comptroller General. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the Fund Accountability Statement is free of material misstatement.

Compliance with laws, regulations, contracts, grants and binding policies and procedures applicable to the project funds is the responsibility of the management of the Capital Markets Authority. As part of our audit we performed tests of the Capital Markets Authority's compliance with certain provisions of laws, regulations, grants and binding policies and procedures. However, it should be noted that we performed those tests of compliance as part of obtaining reasonable assurance about whether the Fund Accountability Statement is free of material misstatement; our objective was not to provide an opinion on compliance with such provisions.

Material instances of noncompliance are violations of laws, regulations, contracts, grants, binding policies and procedures that cause us to conclude that the aggregation of misstatements resulting from those violations is material to the Fund Accountability Statement.

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

- a. Failure to maintain adequate and complete books and records relating to the project.
- b. Failure to publicize USAID participation on project sites and USAID's commodity purchases.
- c. Use of first class air travel under the project contrary to standard U.S. Government regulations.

We considered these instances of noncompliance in forming our opinion on whether the Capital Markets Authority's Fund Accountability Statement is presented fairly, in all material respects, in conformity with the basis of accounting as described in Note 2 to the Fund Accountability Statement, and this report does not affect our report on the Fund Accountability Statement dated April 30, 1994.

Except as described above, the results of our audit tests of compliance indicated that, with respect to the items tested, the Capital Markets Authority 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 the Capital Markets Authority, had not complied, in all material respects, with those provisions.

Financial information contained in this report may be privileged. The provisions of 18 USC 1905 should be considered before any information is released to the public.

This report is intended for the information of the Government of Kenya through the Capital Markets Authority and the United States Agency for International Development, but this is not intended to limit the distribution of the report if it is a matter of public record.



**BELLHOUSE MWANGI ERNST & YOUNG,
NAIROBI**

April 30, 1994

4.2 Work Performed

Our audit of the CMA component of the SAAPTAP Grant Agreement included obtaining assurances that the CMA complied with grant provisions and U.S. Government regulations. Procedures performed to test such compliance included the following:

- i. a review of the Grant Agreement provisions and related regulations to identify those provisions and regulations which could have a material effect on the Fund Accountability Statement; and
- ii. audit procedures including detailed testing to confirm the CMA's compliance with these provisions and regulations.

4.3 Findings and Recommendations

Our findings and recommendations on compliance issues are set out below:

a. Finding : Inadequate and incomplete books and records

The CMA does not maintain adequate and complete books and records on the project, as noted under the findings on the internal control structure, contrary to the standard provisions of the Grant Agreement.

Recommendation No. 9

Our recommendations No. 3 and 4 apply to this finding.

USAID/Kenya comments

USAID/Kenya concurs with the recommendations.

b. Finding : Publicizing of USAID Participation

We noted that USAID's participation has not been publicized on project sites or on USAID funded commodities contrary to USAID regulations.

Recommendation No. 10

We recommend that with the assistance of USAID, the CMA should publicize USAID's participation by having the USAID emblem on all USAID-funded commodities and at project sites.

USAID/Kenya comments

USAID/Kenya concurs with the recommendation.

c. Finding : Contravention of USAID international travel regulations

As noted in our finding under section 2.2.4 of this report international air travel on first class was charged to the project contrary to USAID international travel regulations.

Recommendation No. 11

Our recommendation No. 1 applies to this finding.

USAID/Kenya comments

USAID/Kenya concurs with the recommendation.

APPENDIX I
USAID/KENYA COMMENTS



UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT
U.S.A.I.D. MISSION TO KENYA
OFFICE OF THE DIRECTOR

USAID/
UNIT 64102
APO AE 09831-4102

POST OFFICE BOX 30261
NAIROBI KENYA

July 20, 1994

Bellhouse Mwangi Ernest & Young
Alico House
P.O. Box 44286
Nairobi

Attention: Mr. C.A. Otolo

Dear Sir,

Subject: Response to the Draft Audit Report of the Capital Markets Authority

Thank you for the draft audit report of the Capital Markets Authority (CMA). The Mission has the following comments on the draft report.

Recommendations No. 1 & 2

Grant funds for the grantee were either paid directly to the suppliers or reimbursed to CMA after submission of all the original supporting documents to the Mission. Prior to July 1990, all the original documents were remitted by the Mission to USAID/W for storage, as required by the AID retirement policy. However, the original documentation for expenditures after this date were retired to the USAID/Kenya warehouse for archiving and subsequent shredding.

Based on this, the Mission has determined that unsupported capital and technical assistance costs which were questioned in the draft audit report amounting to \$65,650 and \$22,889 respectively are allowable and should be reflected as such in the final audit report.

Recommendation No. 3

Mission determines that the economy class fare equivalent to \$4,502 is allowed. CMA should be required to refund the balance of \$2,197, being the ineligible amount.

Recommendation No. 4

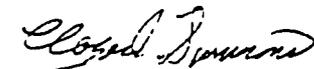
The Mission concurs.

Recommendation Nos. 5 to 13

The Mission concurs.

Mission regrets late submission of the response letter and looks forward to receiving the final audit report soon.

Yours sincerely,


Roger Simmons
Acting Director
USAID/Kenya

APPENDIX II

**COSTS SUPPORTED BY PHOTOCOPIES
AND USAID/KENYA REPRESENTATIONS**

APPENDIX II

COST SUPPORTED BY PHOTOCOPIES AND USAID/KENYA'S REPRESENTATIONS

	Date	Details	Amount \$	Remarks
a.	01.26.90	Office improvement	25,497	Supported by photocopies.
b.	08.30.91	Reimbursement for construction of NSE offices & trading floor	9,851	Supported by photocopies.
c.	09.30.91	Certified contractors' work certificates No. 4 and 5	5,573	Supported by photocopies
d.	11.21.91	Purchase of magnetic boards	6,608	Not supported at all. Physically verified.
e.	02.24.92	Purchase of office equipment	18,121	Not supported at all except for \$11,938 supported by photocopies. Physically verified.
			65,650	

	Date	Details	Amount \$	Remarks
a.	09.29.90	IESC consultancy services. Drafting of operational rules and regulations for CMA by Mr John Evans.	3,884	Airfare not supported at all.
b.	03.15.90	Capital Market Study Tour Seminar	19,005	Not supported at all.
			22,889	
			88,539	
		Total Costs	88,539	
			=====	

ATTACHMENT II*Report Distribution*

U.S. Ambassador to Kenya	1
Director, USAID/Kenya	5
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AA/AFR	2
AA/FA	1
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M/FM	1
LPA	1
GC	1
PPC/CDIE/DI, Acquisitions	2
M/MPI	1
REDSO/ESA	1
REDSO/ESA/RCO	1
REDSO/ESA/RFMC	1
REDSO/ESA/Library	1
IG	1
AIG/A	1
D/AIG/A	3
IG/A/FA	1
IG/A/PSA	1
IG/LC	1
IG/RM/C&R	5
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ATTACHMENT III
Major Contributors to this Report

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