OFFICE OF INSPECTOR GENERAL

AUDIT OF USAID/NIGERIA'S MICROFINANCE ACTIVITIES

AUDIT REPORT NO. 7-620-08-002-P
NOVEMBER 5, 2007

DAKAR, SENEGAL

Office of Inspector General

November 5, 2007

MEMORANDUM

TO: USAID/Nigeria Mission Director, Sharon Cromer

FROM: Regional Inspector General/Dakar, Nancy Toolan /s/

SUBJECT: Audit of USAID/Nigeria's Microfinance Activities
(Audit Report No. 7-620-08-002-P)

This memorandum is our final report on the subject audit. In finalizing this report, we considered management's comments on our draft report and included them in Appendix II.

This report contains three recommendations with which you concurred in your response to the draft report. Final action has been taken on Recommendation No. 2 and no further action is required of the Mission. Based on your proposed actions in response to Recommendations Nos. 1 and 3, management decisions have been reached but these two recommendations will remain open until the planned actions are completed by the Mission. Please coordinate final actions on these recommendations with USAID's Audit Performance and Compliance Division within the Management Bureau's Office of the Chief Financial Officer (M/CFO/APC).

I appreciate the cooperation and courtesies extended to the members of our audit team during this audit.

U.S. Agency for International Development
Ngor Diarama, Petit Ngor, BP 49
Dakar, Senegal
www.usaid.gov

CONTENTS

SUMMARY OF RESULTS

The Regional Inspector General/Dakar conducted this audit as part of a worldwide audit executed by the Office of Inspector General. The objectives of the audit were to determine whether (1) USAID/Nigeria implemented its microfinance activities efficiently, and (2) USAID/Nigeria's microfinance activities achieved planned results (see page 4).

For the first objective, we concluded that for the most part, USAID/Nigeria implemented its microfinance activities in the *Promoting Improved Sustainable Microfinance Services* (PRISMS) program efficiently. The Mission complied with the requirements regarding efficiency and cost-effectiveness in the Microenterprise Results and Accountability Act of 2004. We found increased efficiency in the operations of the primary microfinance institution (MFI) receiving technical assistance from PRISMS based on the results of four financial indicators used to determine efficiency and productivity. Additionally, compared to industry benchmarks, results for three of the four indicators indicated efficient operations, although one indicator (operating expense ratio) still remained higher than the industry standard (see pages 5-6). Although the Mission monitored the program to ensure the program's achievement of its intended results it did not ensure that eligibility conditions were met before agreements were signed with microfinance institutions according to USAID guidance pertaining to microenterprise development programs. The Mission's interpretation of the Automated Directives System (ADS) language led it to believe that the requirements were not applicable to the Mission or that the partner was responsible for ensuring that such conditions were met (see pages 6-8).

For the second objective, we concluded that USAID/Nigeria's microfinance activities achieved planned results. The microfinance activities implemented through PRISMS met or exceeded the targets for its 11 project indicators for fiscal year (FY) 2006 as well as for six of seven financial indicators used to determine sustainability, profitability, and portfolio quality In addition, PRISMS made a positive impact on the MFIs, microfinance beneficiaries, and the microfinance policy environment in Nigeria (see pages 8-10). However, USAID/Nigeria did not verify the microfinance data for FY 2006 activities included in its annual reporting to USAID/Washington, as required by its Mission Order. As a result, the Mission underreported on the Value of Loans indicator by $13.2 million (see pages 10-12).

This report includes three recommendations to assist USAID/Nigeria in managing its microfinance activities and annual reporting. First, we recommend that USAID/Nigeria develop guidance delineating the Mission's and partners' role and responsibilities in complying with Automated Directives System (ADS) 219 in its microenterprise programs (see page 8). Second, we recommend that USAID/Nigeria correct the results of its Value of Loans indicator and the related components reported in its annual reporting for FY 2006 activities and resubmit the results to USAID/Washington (see page 12). Third, we recommend that USAID/Nigeria expand the applicability of its Mission Order to expand beyond the normal annual reporting process to include data reported to USAID/Washington for formal program performance assessments and external reports (see page 12).

USAID/Nigeria concurred with the recommendations and based on actions taken by the Mission, Recommendation No. 2 has been closed and no further action is required. Management decisions have been reached for Recommendations Nos. 1 and 3 based on proposed actions. These recommendations will remain open until final actions are taken by USAID/Nigeria and coordinated with USAID's Audit Performance and Compliance Division within the Management Bureau's Office of the Chief Financial Officer (M/CFO/APC) (see page 13).

BACKGROUND

In many countries, microenterprises—small, informally organized commercial operations owned and operated mostly by the poor—constitute the majority of businesses. They account for a substantial share of total employment and gross domestic product, and they contribute significantly to poverty reduction.

Over the past three decades, support for microfinance development has been an important feature of U.S. foreign assistance. As the leading bilateral donor for microfinance development, USAID has advanced its vision of strengthening economic opportunities for poorer households to enable families to build assets, cope with the risks and vulnerability that accompany poverty, plan for better futures for their children, and contribute to key sectors of local, national and regional economies. As the predominant source of income and employment for hundreds of millions of people worldwide, the microfinance sector's influence on individuals, households, and national economies is clear and profound.

USAID's microenterprise development strategy seeks to address two pressing challenges:

- To link microenterprises to greater opportunities for growth, which includes integrating them on more favorable terms into the formal economies of their countries and connecting them to expanded information and resource networks.

- To bring the benefits of microfinance[1] and business development services to poorer people, ensuring that the positive impacts of microenterprise development programs reach those most in need.

In 2004, USAID/Nigeria awarded a $5.09 million contract to Chemonics for a 4-year microfinance development program called Promoting Improved Sustainable Microfinance Services (PRISMS). The activities under this contract directly supported the agriculture and economic growth objective under the Mission's Strategic Objective, Improved Livelihoods in Selected Areas, with the purpose of increasing access to critical financial services for micro and small enterprises in Nigeria. PRISMS worked directly with microfinance institutions (MFIs) and other institutions providing financial services to micro, small, and medium enterprises (MSMEs) to help them engage in best practices in productive and sustainable lending, savings mobilization, and other financial services. The intended beneficiaries were microfinance and other financial institutions and the entrepreneurs and enterprises they serve, with a particular focus on microenterprises and women.

In August 2006, PRISMS was merged with another program being implemented by Chemonics, called Maximizing Agricultural Revenue and Key Enterprises in Targeted Sites (MARKETS). MARKETS, which is under the same Strategic Objective as PRISMS, focuses on improving rural livelihood by expanding economic opportunities in

[1] Microfinance represents one component of microenterprise activities and refers to the provision of financial services adapted to the needs of low-income people, especially the provision of small loans, the acceptance of small savings deposits and simple payments services needed by microentrepreneurs and other poor people.

the agricultural subsector, especially for women and youth. Programmatically, the two projects complement each other: MARKETS generates the demand for financial services and PRISMS promotes access to the supply of financial services. To support the new microfinance activities under MARKETS, $1.3 million was de-obligated from the PRISMS contract and transferred to the MARKETS program.

AUDIT OBJECTIVES

This audit was conducted as part of a worldwide audit of USAID's microfinance activities included in the Office of Inspector General's fiscal year 2007 annual audit plan. The audit was conducted to answer the following questions:

Did USAID/Nigeria implement its microfinance activities efficiently?

Did USAID/Nigeria's microfinance activities achieve planned results?

Appendix I contains a discussion of the audit's scope and methodology.

AUDIT FINDINGS

Did USAID/Nigeria implement its microfinance activities efficiently?

For the most part, USAID/Nigeria implemented its microfinance activities in the Promoting Improved Sustainable Microfinance Services (PRISMS) program efficiently. The Mission complied with the requirements regarding efficiency and cost effectiveness in the Microenterprise Results and Accountability Act of 2004. We found increased efficiency in the operations of the primary microfinance institution (MFI) receiving technical assistance from PRISMS. Moreover, the Mission appropriately monitored the program to ensure that the implementing partner, Chemonics, performed its duties in accordance with the contract provisions, and the Mission took remedial action, when necessary, to ensure that the program achieved its intended results. However, USAID/Nigeria did not ensure that MFI eligibility conditions were met as referenced in Automated Directives Systems (ADS) 219, which includes USAID guidance pertaining to microenterprise development programs. Because of the wording of the guidance, USAID/Nigeria did not think the requirements were applicable to the Mission and instead thought that the partner was responsible for ensuring that requirements were met.

Although the PRISMS contract was awarded prior to the enactment of the Microenterprise Results and Accountability Act of 2004, USAID/Nigeria complied with the requirements of Section 3(b)(2)(C) pertaining to efficiency and cost-effectiveness. In evaluating proposals for awarding the contract, USAID/Nigeria considered the percentage of funds the bidders intended to expend on administrative costs, and Mission gave preference to proposals that were the most technically competitive and had a reasonable allocation to overhead and administrative costs, as was required by the Act. In addition, once the contract was awarded, the Mission closely monitored the program to ensure that Chemonics kept administrative costs as low as practicable to ensure that the maximum amount of funds were used (1) to directly assist microfinance and microenterprise clients, (2) to establish sustainable microfinance and microenterprise institutions, or (3) to advance the microenterprise development field.

Furthermore, the results of four financial indicators used to determine efficiency and productivity showed that the operational performance of the MFI, Lift Above Poverty Organization (LAPO), had improved. Efficiency and productivity indictors reflect how well an MFI uses its resources, particularly its assets and its personnel. LAPO's results related to its operating expense ratio, the number of borrowers per loan officer, the write-off ratio and the active clients per staff member showed a positive trend of increasing efficiency in its operations from 2005 to 2006. Furthermore, when compared with industry benchmarks, three of the four indicators indicated that LAPO was generally operating efficiently. However, despite a slight improvement from 2005 to 2006, LAPO's operating expense ratio of 38 percent remained significantly higher than the industry benchmark of 25 percent. See Table A-1 in Appendix III for the financial indicator results.

Additionally, USAID/Nigeria was responsible for ensuring that Chemonics performed in accordance with the contract provisions and for monitoring the program's progress. To fulfill these responsibilities, in addition to the cognizant technical officer (CTO) monitoring PRISMS, the Program Office conducted quarterly portfolio reviews of the program. A portfolio review conducted in August 2005 indicated that PRISMS was not achieving its intended results, and in November 2005, USAID/Nigeria issued a "Notice of Performance Delinquency and Required Remedy" to Chemonics. In the correspondence, the Mission expressed its concerns with Chemonics' failure to deliver results and required Chemonics to develop and submit a Recovery Plan and present its proposed execution. Once the Mission approved the Recovery Plan, the work plan and performance monitoring plan were modified accordingly. In the meantime, PRISMS began to achieve results, and although USAID/Nigeria acknowledged that the subsequent achievement could not be attributed solely to the Recovery Plan, the Mission took appropriate measures to ensure the achievement of intended results in the program.

Although USAID/Nigeria monitored PRISMS to ensure that Chemonics performed in accordance with the contract provisions and took steps to ensure that the program achieved its intended results, the Mission did not ensure that MFI eligibility requirements were met before agreements were signed with the MFIs.

ADS 219 Requirements Were Not Followed

Summary: ADS 219 describes certain conditions that must be met before an agreement is signed with an MFI for microfinance activities. USAID/Nigeria did not ensure that the MFI eligibility requirements were met before agreements were signed with the MFIs. This occurred because the Mission's interpretation of the ADS language led it to believe that the requirements were not applicable to the Mission or that the partner was responsible for ensuring that conditions were met. However, it is ultimately the responsibility for the Mission to safeguard the use of U.S. government funds. If the Mission does not fulfill this responsibility, it cannot be fully assured of meeting the intent of the ADS in terms of managing and implementing microfinance programs.

USAID's ADS 219 establishes policy directives and required procedures for USAID program efforts in the area of microenterprise development. For example, ADS 219.3.5, *Eligibility Conditions for USAID Assistance to Microfinance Institutions (MFIs)* requires the following conditions to be met among others before an agreement is signed with an MFI:

- MFI willingness and ability to set full-cost covering interest rates and fees.
- MFI commitment to attain full financial sustainability.
- MFI plan for attaining financial sustainability.
- MFI control over loan delinquency (the MFI's delinquency rate is below 10 percent and its loan loss rate is below 5 percent).

As part of our audit, we intended to determine the extent to which USAID/Nigeria complied with ADS 219, specifically the requirements pertaining to MFI eligibility conditions. We found that the Mission did not follow the ADS instructions related to eligibility requirements for MFIs because it interpreted the guidance too literally which led it to believe that some sections were not applicable to its program, or that compliance with those sections was the responsibility of the partner, not the Mission.

For example the Annex to ADS 219's internal mandatory reference, 'Microenterprise Development,' states that "USAID agreements involving *grant or loan assistance or loan guarantees* to any institution providing financial services to microenterprises…" (emphasis supplied). This Annex provides important guidance on the reporting and analysis of financial, operational, and analytic performance indicators. The Mission interpreted this guidance as not directly applicable to it because PRISMS provided only technical assistance to the MFIs, not direct monetary assistance in the form of grants, loan assistance, or loan guarantees.

Another example pertains to the requirement of MFIs' full financial sustainability contained in ADS 219.3.5.2, which includes the statement "Before the *Mission* signs an agreement to provide assistance to any microfinance institution…" (emphasis supplied). USAID/Nigeria staff literally interpreted this guidance as being applicable only to situations in which USAID has a direct agreement with MFIs, which was not the case with PRISMS. Although USAID/Nigeria had a contract with Chemonics for the PRISMS project, the memorandums of understanding (MOUs) with the MFIs were signed by Chemonics, not the Mission. The Mission did review the MOUs prior to the signing as part of its general oversight but not with the intent to ensure compliance with specific sections of the ADS. In fact, Mission staff indicated that they had intended for the partner to ensure that the eligibility requirements were met and they trusted in the partner's expertise.

Although the Mission did not comply with the ADS and ensure that the eligibility requirements were met, PRISMS staff did assess the operations of two MFIs—LAPO and DEC (Development Exchange Center)—before signing their MOUs. The assessments involved reviewing the MFIs' organizational structure and management, internal controls, products and services, loan portfolio and savings information, objectives and target clients, and financial information. These assessments covered several of the eligibility conditions cited in the ADS, but they did not fully address all of the eligibility conditions of ADS 219.3.5. As such, not all conditions were met before the MOUs were signed by PRISMS and the MFIs. However, we found that both LAPO and DEC met all of the eligibility conditions at the time of our audit fieldwork. For example:

- PRISMS reviewed the MFIs' interest rates during the assessments, but did not document whether the interest rates were full-cost covering. During our site visits, however, we discussed with both LAPO and DEC management their willingness and ability to set full-cost covering interest rates and fees, and we found that both MFIs set high enough interest rates to cover their costs. LAPO charges an interest rate of 36 percent on its loans and DEC charges 30 percent.

- PRISMS did not obtain written commitments to attain full financial sustainability from the MFIs. During our site visits, however, LAPO management said that it was already financially sustainable. This was confirmed by calculating its adjusted return on operations, the core measure used by USAID to assess the financial sustainability of an MFI. LAPO's adjusted return on operations was greater than one, which implies full financial sustainability. DEC management expressed their desire to achieve full financial sustainability, and has developed a strategy to attain this goal.

- PRISMS did not obtain the MFIs' plans for attaining financial sustainability. LAPO is already financially sustainable, however, and DEC included its strategy to attain financial sustainability in its business plan, which was developed as part of the technical assistance provided by PRISMS. DEC's Business Plan covers the years 2006-10, and details DEC's intended path to sustainability by 2010, at which point it will complete its transformation into a microfinance bank. This meets USAID's requirements that an MFI must attain full financial sustainability within no more than 7 years of the initial provision of USAID assistance.

- PRISMS reviewed loan delinquency rates during the assessments, but only one MFI met this eligibility condition. For example, LAPO's loan delinquency rate was 1 percent at the time of the assessment, but DEC's loan delinquency rate was 38 percent, substantially exceeding the 10 percent eligibility threshold. At the time of our audit, however, we found DEC's loan delinquency rate was approximately 10 percent. The decrease was attributable to the technical assistance provided by PRISMS. The MOU with DEC was designed to help DEC with its financial restructuring to better manage its at-risk portfolio and reduce its delinquency rate. The assessments indicated that PRISMS reviewed the amount of loans written off, but not the loan loss rates. We found that both MFIs had loan loss rates below the 5 percent threshold.

The Mission is fortunate that the partner performed some assessments of the MFIS and by the time of our audit, both MFIs met the eligibility conditions set out by the ADS. However, it is ultimately the responsibility of the Mission to safeguard U.S. Government funds and to ensure its own and its partners' compliance with ADS requirements. Failure to do this means the Mission cannot be fully assured of meeting the intent of the ADS in terms of managing and implementing microfinance programs. Therefore, to ensure that USAID/Nigeria fulfills its correct and appropriate responsibilities, the Office of Inspector General is making the following recommendation:

Recommendation No. 1: We recommend that USAID/Nigeria develop procedures and guidance delineating the Mission's and partners' roles and responsibilities in ensuring compliance with the requirements in the Automated Directives System 219 for its microenterprise programs.

Did USAID/Nigeria's microfinance activities achieve planned results?

Our review of reported results and project activities indicates that USAID/Nigeria's microfinance activities achieved planned results. The microfinance activities implemented through the PRISMS program met or exceeded the targets for almost all of its project indicators for FY 2006. In addition, the program made a positive impact on the MFIs with which it worked, their beneficiaries, and the microfinance policy environment in Nigeria.

PRISMS exceeded the targets for 9 of its 11 indicators in its annual workplan and met the targets for the remaining 2 indicators. For example, 13,819 loans were disbursed to MSMEs exceeding the target of 9,000 loans. The target related to the overall value of loans disbursed was exceeded as well, with 241 million naira disbursed through loans compared with the target of 90 million naira. In addition, three policies were approved or revised by the Central Bank of Nigeria (CBN) to support MSME finance, exceeding the planned target of having two policies adopted. See Table A-2 in Appendix III for more details on the planned and actual results achieved through this project in fiscal year 2006. In addition to the 11 project indicators in the PRISMS workplan, we reviewed seven financial indicators used to determine sustainability, profitability, and portfolio quality for LAPO. For six of the seven, the actual results in FY 2006 met or exceeded the targets, indicating that LAPO is achieving its planned results. See Table A-3 in Appendix III for these targets and results.

Other benefits were realized through the PRISMS program in addition to the achievement of planned results. For example, to counter the local commercial banks' skepticism about lending to MFIs, PRISMS helped the MFIs develop marketable business plans and linked them to specialized international microfinance investment and lending funds to secure hard currency loans. These hard currency loans were then deposited into local commercial banks to guarantee wholesale loans in naira, the local currency. In FY 2006, about 800,000 euros in hard currency loans from various international organizations were used to guarantee commercial bank loans of approximately 125 million naira.

The security of the wholesale loans provided MSMEs more access to financing, which translated to an increase in beneficiaries' income and improvement in their livelihood. We met with several beneficiaries who conveyed their satisfaction with the MFIs. Some expressed a desire to see the loan amounts increased from the current amounts, which would enable them to further increase their business capacities and further improve their lifestyle. During our site visit to one of LAPO's branches in Benin City, an area manager stated that LAPO had graduated some beneficiaries. These graduates no longer needed to borrow to operate and grow their businesses, but rather they were able to use their savings.

Photograph of one of LAPO's lending groups, Oromiyan Union, at its meeting location in Benin City (left)
Photograph of one of DEC's lending groups, Soyya, at its meeting location in Bauchi (right). LAPO and DEC lend only to groups as a form of social collateral. Credit officers meet with the groups weekly to collect the weekly loan payments and mandatory savings deposits. Both groups indicated that the loans provided by the MFIs have significantly enhanced the ability to grow their businesses.
Source: Photos were taken in Benin City and Bauchi by a Regional Inspector General/Dakar auditor in May 2007.

The program affected the financial sector policy environment in Nigeria. Before PRISMS no governmental policy regulated MFIs. PRISMS helped the CBN formulate the

Microfinance Banking Policy. The policy, which was launched in December 2005, requires MFIs to meet certain standards and convert to microfinance banks. PRISMS introduced risk-based supervision to the CBN as a method to monitor and supervise the microfinance banks more effectively and efficiently. The CBN is now converting to risk-based supervision throughout its banking system.

We also found that USAID/Nigeria effectively monitored the PRISMS program. The CTO was actively involved in and had thorough knowledge of the program activities. For example, the CTO maintained ongoing communication with Chemonics through weekly meetings, telephone conversations, and e-mail correspondence. Additionally, the CTO reviewed the program's quarterly progress reports, correspondence between Chemonics and the MFIs and commercial banks, and monthly invoices submitted by Chemonics. The CTO maintained telephone contact with the MFIs. Furthermore, USAID/Nigeria's monitoring and evaluation (M&E) contractor performed data quality assessments (DQAs) on the program's microfinance data included in the Mission's annual reporting for FY 2006 activities. Chemonics played an active role in monitoring the activities by maintaining frequent contact with the MFIs. Chemonics also performed in-depth reviews of quarterly reports submitted by the MFIs and made site visits to the field on a regular basis to verify data, review MFI operations, and observe activities.

We reviewed source documentation maintained by Chemonics supporting the results of the 11 project indicators reported in its final report to USAID/Nigeria, and found no discrepancies. We reviewed documentation supporting the FY 2006 data entered into the Microenterprise Results Reporting System[2] at the Mission and partner levels, and also found it to be accurate. We did, however, find errors in USAID/Nigeria's annual reporting for FY 2006 activities, which significantly misrepresented the Mission's accomplishments.

Data Submitted to Washington Needs to be Verified

Summary: USAID/Nigeria submitted erroneous data to Washington regarding the results of a key indicator which substantially misrepresented the value of loans disbursed through the program. This occurred because the Mission did not verify and cross-check the microfinance data reported to USAID/Washington in its annual reporting for FY 2006 activities, as required by its Mission Order. The Mission Order was not followed due to an oversight resulting from the different reporting process used and the lack of specific directions to verify the data before submission. Reporting of inaccurate results can lead to inappropriate programmatic decisions.

As discussed, USAID/Nigeria's M&E contractor conducted DQAs on the indicator data reported in the annual report table. Once the DQAs were complete, the M&E contractor gave the Mission separate data sheets for each indicator, which showed the allocation by partner and the grand total of the indicator result. The M&E contractor also provided the Mission with the final results in the form of a data table that listed each indicator and

[2] The Microenterprise Results Reporting (MRR) is USAID's official system for tracking its microenterprise investments.

its respective total result.

On three data sheets prepared by the M&E contractor, the last three digits were dropped when the figures provided were in the billions of naira. For example, the data sheet supporting the Total Value of Loans by USAID-assisted institutions showed a total of 1,903,709 naira, dropping the last three digits of the actual total of 1,903,709,980 naira. Compounding on this error is the fact that the Mission reported the amount as US dollars (US$), even though the data sheets identified the amounts as naira. As a result, USAID/Nigeria reported the value of its loans as US$1,903,709, rather than the correct amount of US$15,108,809[3], the equivalent of the 1,903,709,980 naira. Therefore, because the Mission did not verify the data before submitting it to USAID/Washington as required in its Mission Order, the Mission underreported on this indicator by more than US$13.2 million. We found similar errors on the data sheets for the three components of this indicator, with incorrect information reported to USAID/Washington:

- The data sheet for the value of loans to women showed a total of 1,814,398 Naira and was reported by the Mission as such in U. S. dollars. The correct amount however, was 1,814,398,266 naira, the equivalent of US$14,399,986. The Mission underreported on this indicator by US$12.6 million.

- The data sheet for the value of loans to other disadvantaged groups showed a total of 34,501,714 naira, and was reported by the Mission as such in U. S. dollars. The correct amount is US$273,823 USD. The Mission overreported on this indicator by US$34.2 million.

- The data sheet for the value of micro loans showed a total of 1,902,469 naira, and was reported by the Mission as such in U. S. dollars. The correct amount, however, was 1,902,469,980 naira, equivalent to US$15,098,968. The Mission underreported these program results by $13.2 million.

USAID/Nigeria's Mission Order 200-10 details the procedures for preparing the Mission's Annual Report. It states that the Program Office is responsible for sending out the complete annual report guidance to all Strategic Objective (SO) and support Team Leaders. SO and support Team Leaders will assign an individual to review the narrative and quantitative information contained in the relevant sections of the annual report and ascertain whether it matches the source documents, which includes cross-checking all information in the relevant sections of the annual report against source documents, and confirming that all quantitative calculations are correct. The individual is then required to sign a statement listing the indicators or data that have been verified, and the Team Leader will also sign the statement to confirm that the accuracy of the data has been verified. The Program Office will then enter data into the annual report application only if it is accompanied by a verification statement.

With the introduction of the Country Operational Plan[4] in the fall of 2006, USAID/Nigeria was not required to prepare the standard Annual Report as in previous years. In March 2007, USAID/Washington asked the Mission to submit the actual results for FY 2006 activities in the form of a table. The standard narrative section was not required.

[3] An exchange rate of 126 naira to US$1 was used.
[4] The Country Operational Plan is an integral tool of foreign assistance designed to link funding to activities and results.

Although the Program Office sent the draft results table to each of the SO Teams before submitting the data to Washington, the Program Office did not elaborate or specifically request verification of the data. Therefore, in light of the different reporting requirements and the lack of specific directions to verify the data, the SO Teams did not review and sign off on the data before the Program Office submitted it to Washington.

Data reported to USAID/Washington for formal program assessments or external reporting requirements should be verified before submission. Although the Mission did have a Mission Order describing procedures to verify data for the Annual Report, the Order did not specifically include other reporting mechanisms such as the new Country Operational Plan. The reporting errors that did occur caused the impact of USAID/Nigeria's microfinance program to be inaccurately reflected. It is important that reported results be reliable, especially in these times of increased budget scrutiny. Because performance information is used to influence program decisionmaking and resource allocation, this incorrect information could be used to make inappropriate programmatic decisions for future activities. The Office of Inspector General, therefore, is making the following recommendations:

Recommendation No. 2: We recommend that USAID/Nigeria correct the results of its Value of Loans indicator and the related components reported in its annual reporting for fiscal year 2006 activities and resubmit the results to USAID/Washington.

Recommendation No. 3: We recommend that USAID/Nigeria expand the applicability of its Mission Order 200-10 beyond the former annual reporting process to include data reported to USAID/Washington for formal program performance assessments and external reports, and communicate to Mission staff the importance of following the procedures in the revised Mission Order.

EVALUATION OF MANAGEMENT COMMENTS

USAID/Nigeria concurred with the findings and the recommendations in the draft audit report[5]. Final action has been taken on Recommendation No. 2 and no further action is required of the Mission related to that recommendation. Management decisions have been reached on Recommendations No. 1 and 3, which will remain open until final actions are taken by USAID/Nigeria and coordinated with USAID's Audit Performance and Compliance Division within the Management Bureau's Office of the Chief Financial Officer (M/CFO/APC). The Mission indicated that these actions will be completed within the next 6 months or sooner.

Recommendation No. 1 recommends that USAID/Nigeria develop procedures and guidance delineating the Mission's and partners' roles and responsibilities in ensuring compliance with the requirements in the Automated Directives System (ADS) 219 for its microenterprise programs. The Mission indicated that it is drafting a Mission Order to ensure compliance with the ADS regulation that will specify the roles and responsibilities for current and future microfinance activities. Based on this proposed action, a management decision has been reached but the recommendation will remain open until final action is completed by the Mission.

Recommendation No. 2 recommends that USAID/Nigeria correct the results of its Value of Loans indicator and the related components reported in its annual reporting for fiscal year 2006 activities and resubmit the results to USAID/Washington. The Mission submitted documentation showing a 'screen shot' of the corrected information in its reporting data base. Based on this final action, this recommendation is closed.

Recommendation No. 3 recommends that USAID/Nigeria expand the applicability of its Mission Order 200-10 beyond the former annual reporting process to include data reported to USAID/Washington for formal program performance assessments and external reports, and communicate to Mission staff the importance of following the procedures in the revised Mission Order. The Mission indicated that a revision of the Mission Order was underway and will stress its importance when disseminated to all Mission staff. Based on this proposed action, a management decision has been reached but the recommendation will remain open until final action is completed by the Mission.

Management's comments are included in their entirety (without attachments) in Appendix II.

---

[5] USAID/Nigeria's response refers to our preliminary report number 7-620-07-00X-P. However, it has been assigned a new number reflecting issuance in FY2008 (7-620-08-002-P).

(This page intentionally left blank)

SCOPE AND METHODOLOGY

Scope

The Regional Inspector General's office in Dakar, Senegal conducted this audit in accordance with generally accepted government auditing standards. This audit is part of a worldwide audit of USAID's microfinance activities. The audit was designed to determine whether (1) USAID/Nigeria implemented its microfinance activities efficiently and (2) USAID/Nigeria's microfinance activities achieved planned results.

According to USAID, microenterprise activities are comprised of four major components: microfinance, enterprise development, financial policy, and microenterprise development policy. The scope of this audit covers the microfinance component and encompasses USAID/Nigeria's fiscal year (FY) 2006 microfinance activities in the Promoting Improved Sustainable Microfinance Services (PRISMS) program implemented by Chemonics. In August 2006, PRISMS was merged with another program being implemented by Chemonics called Maximizing Agricultural Revenue and Key Enterprises in Targeted Sites (MARKETS). The audit focused on the two microfinance institutions (MFIs) that were integrated into MARKETS: Lift Above Poverty Organization (LAPO) and Development Exchange Center (DEC). We reviewed the results of the 11 project indicators reported in the PRISMS final program report.[6] USAID/Nigeria disbursed slightly less than $1 million for PRISMS activities conducted in FY 2006.

In planning and performing the audit, we reviewed and assessed the effectiveness of management control related to the microfinance activities. We identified management control as the Mission's annual self–assessment of management control as required by the Federal Managers' Financial Integrity Act Report, Mission policies and procedures, monitoring of activities, accurate and timely recording of transactions and events, and maintenance of documentation. The audit involved interviews with USAID/Nigeria, partner, and MFI staff; reviews of their records; site visits; and interviews with beneficiaries.

Audit fieldwork was conducted from May 8 through May 25, 2007, at USAID/Nigeria and the Chemonics/MARKETS office in Abuja. Site visits were conducted in Benin City and Bauchi at the headquarters office, a branch office, and a beneficiary group meeting location of the two MFIs.

Methodology

To answer the audit objectives, we obtained an understanding of the microfinance program by reviewing applicable laws, regulations, guidance, and program documents. We interviewed Mission, partner, and MFI staff regarding the microfinance activities being implemented, the achievement of results, their roles and responsibilities for monitoring of the activities, and data collection and reporting.

[6] The results only include data from LAPO's activities because PRISMS did not sign the memorandum of understanding with DEC until July 2006.

To evaluate efficiency, we determined compliance with Section 3(b)(2)(C) of Public Law 108-484: Microenterprise Results and Accountability Act of 2004, USAID's Automated Directives System (ADS) 219 – Microenterprise Development, and the provisions of the PRISMS contract. In addition, we reviewed the trends of the results of four financial indicators used in the microfinance industry to determine efficiency and productivity of LAPO.

We identified and selected the results of all 11 project indicators reported in the PRISMS final program report for in-depth review. We measured whether the selected indicators had been achieved by comparing the results with the targets. We also determined achievement by conducting site visits to observe activities first-hand. The following criteria were used to assist in answering the audit objective:

- If at least 90 percent of the selected planned results were achieved, the answer to the audit objective will be positive.

- If at least 80 percent, but less than 90 percent, of the selected planned results were achieved, the answer to the audit objective will be qualified.

- If less than 80 percent of the selected planned results were achieved, the answer to the audit objective will be negative.

While we have these threshold criteria, we also used auditor judgment to determine the applicability of the threshold percentages, taking into consideration other factors such as significance of the various outputs, environmental aspect, and timeliness of funds distribution.

In assessing achievement, we compared the results to the targets of seven financial indicators used in the microfinance industry to determine sustainability and profitability and portfolio quality for LAPO.

We verified the accuracy of the project indicator results by reviewing source documentation. We verified the accuracy of the data input into the Microenterprise Results Reporting System by USAID/Nigeria and Chemonics and the results of the two microfinance indicators reported in USAID/Nigeria's Annual Report Table. In assessing data quality, we used a materiality threshold of 5 percent for reporting accuracy.

We judgmentally selected a sample of sites for testing. For each MFI, we visited the headquarters office, a branch office, and a beneficiary group meeting location. During site visits, we interviewed MFI staff, reviewed documentation, and reviewed the MFIs' loan portfolio tracking and reporting systems. We also observed loan disbursement and collection activities and interviewed beneficiaries.

MANAGEMENT COMMENTS

USAID | NIGERIA
FROM THE AMERICAN PEOPLE

October 17, 2007

Nancy Toolan
Acting Regional Inspector General/Dakar
Office of Inspector General
Dakar, Senegal

Subject: Audit of USAID/Nigeria's Microfinance Activities

Dear Ms. Toolan,

USAID/Nigeria appreciates the assistance of RIG/Dakar and concurs with the findings as noted on the draft audit report, Audit of USAID/Nigeria's Microfinance Activities (Audit Report No. 7-620-07-00X-P.)

The following actions have been taken:

Recommendation No. 1:

> *"We recommend that USAID/Nigeria develop procedures and guidance delineating the Mission's and partners' roles and responsibilities in ensuring compliance with the requirements in the Automated Directives System 219 for its microenterprise programs."*

The Mission is drafting a Mission Order to ensure compliance of ADS 219 regulations that will specify roles and responsibilities for current and future microfinance activities.

Recommendation No. 2:

> *"We recommend that USAID/Nigeria correct the results of its Value of Loans indicator and the related components reported in its annual reporting for fiscal year 2006 activities and resubmit the results to USAID/Washington."*

The PART database correction has been completed. Attached are the "before" and "after" screen shots of the data base which reflect the change. We request the closure of this recommendation.

Recommendation No. 3:

> *"We recommend that USAID/Nigeria expand the applicability of its Mission Order 200-10 beyond the former annual reporting process to include data reported to USAID/Washington for formal program performance assessments and external reports, and communicate to Mission staff the importance of following the procedures in the revised Mission Order."*

To close this recommendation, the Mission is revising the current Mission Order to include all other data reported to USAID/Washington. The Mission will disseminate the revised Mission Order to all Mission staff to ensure compliance and stress its importance.

USAID/Nigeria will close the recommendations #1 and #3 within the next six months or sooner. As documentation is available, it will be forwarded to RIG for review and confirmation of closure.

USAID/Nigeria wishes to thank the auditors and appreciates their assistance.

Sincerely,

Sharon L. Cromer/s/
Mission Director

FINANCIAL AND PROJECT INDICATORS

Table A-1 – Efficiency and Productivity Financial Indicators

Indicator	2005	2006	Positive Trend Indication	Benchmark
Operating Expense Ratio	40%	38%	Downward	25%
Borrowers per Loan Officer	293	370	Upward	220
Write-off Ratio	0.1%	0.0%	Downward	0.4%
Active Clients per Staff Member	149	168	Upward	148

Note: Industry benchmarks were extracted from *Benchmarking African Microfinance 2005*, a report from the Microfinance Information eXchange, Inc

Table A-2 – Project Indicators

Indicator	2006 Target	2006 Actual	Achieved[a]
Value of loans disbursed to MSMEs[b] including repeat loans (in millions of Nigerian naira)	90.0	240.6	Yes - exceeded
Number of loans disbursed to MSMEs including repeat loans	9,000	13,819	Yes - exceeded
Value of wholesale loans to NBFIs[c] and retail loans to MSMEs disbursed (in millions of Nigerian naira)	90	179.1	Yes- exceeded
Number of wholesale loans to NBFIs and retail loans to MSMEs disbursed (in millions of Nigerian naira)	3	3	Yes
Number of new/existing financial products/guarantees introduced	2	3	Yes - exceeded
Value of retail loans to MSMEs by NBFIs including repeat loans (in millions of Nigerian naira)	90	240.6	Yes - exceeded
Number of retail loans to MSMEs by NBFIS including repeat loans	9,000	13,819	Yes - exceeded
Value of retail loans made to new clients by NBFIs	138,524	491,712	Yes - exceeded
Number of new clients served by NBFIs	6,973	25,202	Yes - exceeded
Number of new supervisory or planning tools/techniques introduced	1	1	Yes
Number of policies approved/revised to support MSME finance	2	3	Yes - exceeded

Notes:

[a] *We considered an indicator achieved when the actual results were 90 percent or more of the target*

[b] *Micro, small and medium enterprises (MSME)*

[c] *Non-bank financial institution (NBFI)*

Table A-3 – Sustainability, Profitability, and Portfolio Quality Financial Indicators

Indicator	2006 Target	2006 Actual	Achieved[a]
Active Portfolio	$8,629,976	$8,053,851	Yes
Active Clients	80,878	83,547	Yes
Write-off Ratio	0%	0%	Yes
Operational Self-Sufficiency Ratio	140%	137%	Yes
Return on Assets	8%	11%	No
Portfolio-at-Risk Ratio	0%	0%	Yes
Average Outstanding Loan Size	$104	$96	Yes

Notes:
[a] *We considered an indicator achieved when the actual results were 90 percent or more of the target*
[b] *Micro, small and medium enterprises (MSME)*
[c] *Non-bank financial institution (NBFI)*

U.S. Agency for International Development
Office of Inspector General
1300 Pennsylvania Ave, NW
Washington, DC 20523
Tel: (202) 712-1150
Fax: (202) 216-3047
www.usaid.gov/oig