

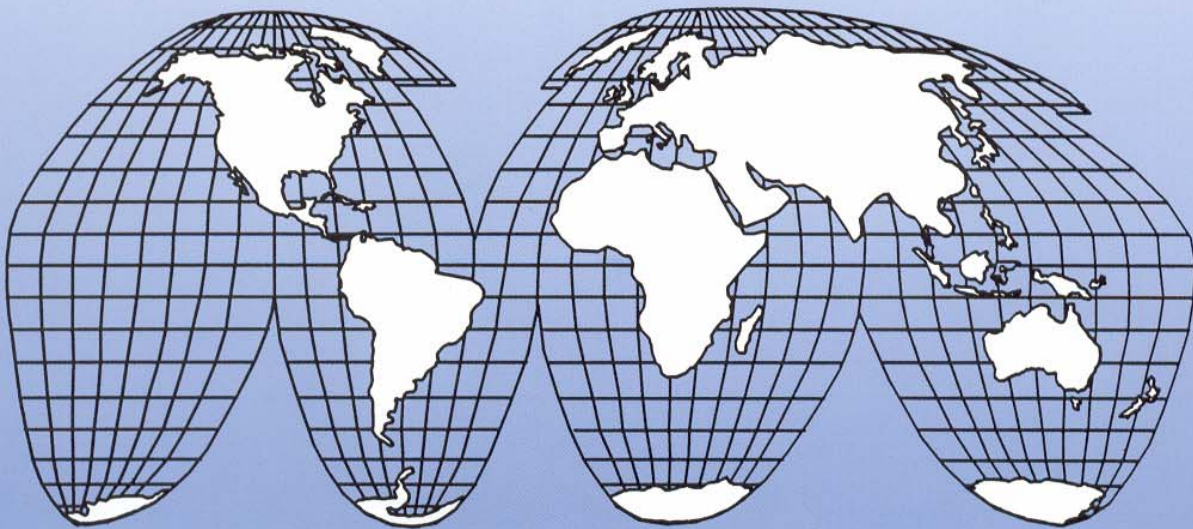
USAID

OFFICE OF INSPECTOR GENERAL

Audit of USAID/Jordan's Microfinance Activities

Audit Report No. 6-278-04-001-P

October 1, 2003



Cairo, Egypt

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October 1, 2003

MEMORANDUM

FOR: Director, USAID/Jordan, Anne Aarnes

FROM: RIG/Cairo, Darryl T. Burriss /s/

SUBJECT: Audit of USAID/Jordan's Microfinance Activities
(Report No. 6-278-04-001-P)

This is our final report on the subject audit. We reviewed your comments to our draft report and included them as Appendix II to this report.

The report recommends that USAID/Jordan (1) require that a data quality assessment of microfinance results be performed before using such results in the Mission's 2004 Annual Report, and (2) develop a procedure to verify that results included in the Mission's Annual Report have had data quality assessments.

Based on your comments to our draft report, we consider that a management decision has been made on Recommendation No. 1 and that final action has occurred on Recommendation No. 2. In regards to Recommendation No. 1, please notify the Bureau for Management's Office of Management Planning and Innovation when final action is complete.

I appreciate the cooperation and courtesy extended to my staff by USAID/Jordan and its microfinance institutions during the audit.

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Summary of Results

Regional Inspector General/Cairo audited USAID/Jordan's microfinance activities to determine if (1) the Mission administered the activities in accordance with applicable USAID guidance and (2) the activities had progressed towards their intended results. (See page 6.)

USAID/Jordan administered its microfinance activities in accordance with applicable USAID guidance, but three of four microfinance institutions did not focus on reaching poor people. We did not make a recommendation to address this issue because missions have flexibility in structuring their lending programs and the extent to which they target the poor. (See pages 7 – 9.)

In regards to intended results, USAID/Jordan's microfinance activities had mixed results for calendar year 2002. One indicator (number of borrowers) fell short of its target by 21 percent, but another indicator (number of repeat borrowers) exceeded its target by 2 percent. Mission officials were unaware that they had fallen short of their targeted number of borrowers because they had not assessed the quality of data reported to them by microfinance institutions. Consequently, they had inadvertently reported inaccurate microfinance results. (See pages 9 – 11.)

To address this issue, we recommended that (1) the Mission perform a data quality assessment of microfinance results before including such results in its 2004 Annual Report and (2) the Mission develop a procedure to verify that results included in the Mission's Annual Report have had data quality assessments. (See page 11.)

USAID/Jordan agreed with the two recommendations. Based on the Mission's response to our draft report, we determined that a management decision has been made to address Recommendation No. 1 and that final action has been taken on Recommendation No. 2. (See page 12.)

Background

In 1994, USAID launched a "Microenterprise Initiative" in partnership with the Congress. The initiative committed to expanding funding for microenterprise programs and set a goal that one-half of all microenterprise resources would support programs and institutions that provide credit to the poorest, with loans under \$300. In October 2000, the President signed the Microenterprise for Self-Reliance and International Anti-Corruption Act of 2000. The purposes of the Act included, among others, making microenterprise development an important element of United States foreign economic policy and assistance, and providing for the continuation and expansion of USAID's 1994 Microenterprise Initiative.

In support of USAID's microenterprise program, in January 1998 USAID/Jordan initiated an \$18.4 million microfinance initiative under its \$57 million Access to Microfinance and Improved Implementation of Policy Reform Program (AMIR 1.0). The initiative primarily involved four institutions and aimed to increase the sustainable delivery of financial services to microentrepreneurs, including small and medium enterprises and women entrepreneurs. The microfinance program ended on July 31, 2002, and cumulative microenterprise-related expenditures as of December 31, 2002, totaled \$18.4 million.

In August 2002, the Mission began a three-year \$59 million follow on program (AMIR 2.0) of which \$9 million was budgeted for microenterprise initiatives, including the development of microfinance institutions, microenterprise business development, and microenterprise innovation grants. Microenterprise-related expenditures under the follow on program totaled \$1.1 million as of December 31, 2002.

Our audit focused on calendar year 2002, and thus, covered the end of the initial microfinance program and the beginning of the follow on program. USAID/Jordan's strategic objective team for increased economic opportunities for Jordanians had responsibility for both programs.

Audit Objectives

As a carryover audit from our fiscal year 2002 audit plan, our audit aimed to answer the following two questions:

- Had USAID/Jordan administered microfinance activities in accordance with applicable USAID guidance?
- Had USAID/Jordan's microfinance activities progressed towards their intended results?

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

Audit Findings

Had USAID/Jordan administered microfinance activities in accordance with applicable USAID guidance?

USAID/Jordan administered microfinance activities in accordance with applicable USAID guidance, but three of four microfinance institutions did not focus on reaching poor people.

In accordance with USAID's Automated Directives System, Chapter 219, which provides policy on microenterprise development, USAID/Jordan's microfinance activities benefited women and poor people. In addition, three of four Mission-supported microfinance institutions had reached full financial sustainability¹. Further, the Mission had ensured that each of its microfinance institutions had annual audits of their financial statements. Some specific accomplishments for calendar year 2002 included the following²:

- 82 percent of the number of loans disbursed went to women, indicating that the Mission's activities were formally and effectively open to women in accordance with USAID policy. The percentage also indicated that the Mission's activities were targeting and reaching women.
- 44 percent of the number of loans disbursed went to poor people via poverty loans (i.e., loans of \$350 or less)³, indicating that the Mission's activities were benefiting poor people in accordance with USAID policy. USAID uses a proxy indicator to define the poor as individuals who received a poverty loan.
- 20,134 loans totaling 12.1 million Jordanian Dinar (\$17.3 million) were disbursed to microentrepreneurs. These statistics indicated that the Mission's activities had broad outreach as called for by USAID's Microenterprise Development Policy Paper.
- Three of four Mission-supported microfinance institutions had reached financial sustainability as of the end of calendar year 2002¹. Per USAID policy, microfinance institutions are supposed to be committed to achieving full financial sustainability.
- The Mission had ensured that all required financial audits of its microfinance institutions had, in accordance with Automated Directives System, Chapter 591, been performed.

¹ Based on unaudited financial information.

² Appendix I explains the methodology used to validate these accomplishments. Appendix III provides a breakdown of these statistics by microfinance institution.

³ Because poverty loans are issued in small amounts, poverty lending only represented 14 percent of the amount of loans disbursed during calendar year 2002.

Although 44 percent of the overall number of loans disbursed during calendar year 2002 went to poor people via poverty loans, two of the four microfinance institutions had not issued any poverty loans and a third institution had issued only a small percentage of loans as poverty loans. Hence, these three institutions did not focus on reaching the poor. This issue is discussed below.

Three Microfinance Institutions Did Not Focus On Poor People

U.S. law and USAID policy have a principal focus on reaching the poor with microenterprise development resources, but three of four USAID/Jordan-supported microfinance institutions had not focused their resources on reaching poor people. This occurred because USAID policy provides missions flexibility in structuring lending programs and the extent to which these programs target the poor. Consequently, although the three institutions were assisting entrepreneurs, they were not focused on assisting poor entrepreneurs.

The Microenterprise and Self Reliance Act of 2000 requires USAID to target 50 percent of all microenterprise resources to very poor entrepreneurs. USAID's Automated Directives System provides a \$350 poverty loan standard for loans made during 2002 in the Near East, and USAID uses this standard as an indicator to determine whether a loan was made to a poor person.

The Act's 50 percent funding target applies at the Agency level and not at the mission level. Therefore, USAID allows missions to choose the 50 percent target or a more or less stringent one. Per USAID's Office of Microenterprise Development, the extent to which a mission devotes its resources on poor entrepreneurs ideally needs to be made on technical grounds, considering a country's economic situation; the state of development of the country's microfinance sector; and the Mission's approach towards targeting by geographical, demographical, or sector means.

Although missions have flexibility with the 50 percent poverty lending target, two of four microfinance institutions that received funds from USAID/Jordan had not issued any poverty loans during calendar year 2002 and only 16 percent of a third institution's loans qualified as poverty loans. Although these three institutions were assisting microentrepreneurs, they were not focused on using USAID resources to benefit poor entrepreneurs, who are supposed to be a principal part of USAID's microenterprise development efforts.

USAID/Jordan officials explained that the Mission's microfinance strategy had a two-pronged approach: first, to support grassroots institutions that are capable of providing broad outreach in poverty lending and, second, to support bank-related institutions interested in deepening their outreach. They said that the Microfund for Women was the principal example of a grassroots program with an average loan size of \$200 and pointed out that their loan program represented over 80

percent of the number of loans disbursed by the Mission's microfinance institutions in calendar year 2002. They also explained that the Ahli Microcredit Company was an example of a bank-owned institution that had initiated microfinance activity and that its lending activities covered the gap between poverty loans and commercial loans needed by enterprises to grow their businesses.

Further, the Mission officials said that, although Ahli Microcredit Company's focus was not specifically in poverty lending, its role as a subsidiary of a commercial bank was creating a link between microentrepreneurs and the formal banking sector. Overall, the officials said these two reinforcing approaches were designed with the intent of creating a sustainable microfinance industry in Jordan that served the poor and met the needs of microentrepreneurs in Jordan.

Based on the Mission's explanation of its microfinance program and because, as previously stated, missions have flexibility in structuring their lending programs and the extent to which they target the poor, we did not make a recommendation on targeting more poor beneficiaries.

Had USAID/Jordan's microfinance activities progressed towards their intended results?

USAID/Jordan's microfinance activities had mixed results during calendar year 2002.

USAID/Jordan's strategic objective team for expanded economic opportunities had two primary performance indicators to track the performance of its microfinance activities: number of borrowers and the percentage of repeat borrowers. As illustrated in Table 1 below, USAID/Jordan's microfinance activities fell short of one of their 2002 targets, but exceeded the second.

Table 1. Comparison of Actual Accomplishments to Planned Targets

Performance Indicator	2002 Target	2002 Actual	Difference	Percentage Difference
Number of Borrowers	18,000	14,251	3,749	-21%
Percentage of Repeat Borrowers	54%	55%	1%	+2%

Mission officials reported that they had exceeded their 2002 target for the number of borrowers by 1,000 and thus, were not aware that they had actually fallen short of their target. They were not aware of the actual number of borrowers because

they had not verified lending results reported to them by four USAID-supported microfinance institutions. This issue is discussed below.

USAID/Jordan Needs To Perform Data Quality Assessments Of Reported Microfinance Results

Contrary to USAID policy, USAID/Jordan did not perform a data quality assessment of lending results reported by microfinance institutions. Consequently, the Mission included inaccurate microfinance statistics in its 2003 Annual Report. The error primarily occurred because strategic objective team officials were unaware of the requirement to perform data quality assessments of results reported to them by Mission-supported microfinance institutions.

Automated Directives System Chapter 203.3.5.2 discusses data quality assessments and states that data reported to USAID/Washington for reporting externally on Agency performance must have had a data quality assessment within the three years before submission. It also says that the purpose of a data quality assessment is to ensure that the operating unit and strategic objective team are aware of the strengths and weaknesses of the data being reported and are aware of the extent to which the data can be trusted to influence management decisions. Further, it explains that a data quality assessment involves applying the following five data quality standards to performance data: validity, integrity, precision, reliability, and timeliness.

Contrary to the above requirements, USAID/Jordan reported in its 2003 Annual Report microfinance lending statistics, which had not had data quality assessments. Consequently, the Mission reported inaccurate statistics for its microfinance activities.

For example, the 2003 Annual Report included the following statements:

- “The Mission’s four USAID-affiliated microfinance institutions had reached 19,128 microentrepreneurs, over 1,000 more people than the planned figure of 18,000.”; and
- “AMIR⁴ continues to support three microfinance providers within Jordan who have, on average, an 80 percent female client base.”

However, as shown in Table 2 below, the four microfinance institutions had 14,251 borrowers instead of 19,128, and the three AMIR-supported microfinance institutions had a female client base of 88 percent instead of 80 percent.

⁴ Achievement of Market-Friendly Initiatives and Results Program.

Table 2. Comparison of Reported vs. Verified Amounts

Performance Indicator	2002 Reported	2002 Per Audit	Difference	Percentage Difference
Number of Borrowers	19,128	14,251	4,877	-25%
Female Clients of Three AMIR-Supported Institutions	80%	88%	8%	+10%

The differences between the above results occurred because all four microfinance institutions had mistakenly reported on the number of loans they had issued instead of reporting on the number of borrowers. That is, because some borrowers had taken out more than one loan during the year, the number of loans issued during 2002 exceeded the number of borrowers. Hence, use of the number of loans issued instead of the number of borrowers caused the Mission to over report its number of borrowers and to miscalculate the percentage of loans made to females.

The errors in the results reported by the microfinance institutions were not detected by USAID/Jordan for two reasons. First, the Mission's strategic objective team officials were unaware of the requirement to assess the quality of data reported by the microfinance institutions, and second, USAID/Jordan did not have a management control to ensure that a data quality assessment of microfinance activity results had been performed before placing the statistics in the Mission's 2003 Annual Report. Had an assessment of the quality of data reported by the four microfinance institutions been performed, Mission officials likely would have discovered that the institutions had mistakenly reported on the number of loans disbursed instead of the number of borrowers and would have taken action to address it.

The reporting of unverified microfinance results could lead managers at USAID/Jordan and USAID/Washington, as well as decision makers outside of USAID, to make improper conclusions and programmatic decisions.

Recommendation No. 1: We recommend that the Director, USAID/Jordan perform a data quality assessment of microfinance results before using such results in the Mission's 2004 Annual Report.

Recommendation No. 2: We recommend that the Director, USAID/Jordan develop a procedure to verify that results included in the Mission's Annual Report have had data quality assessments.

**Management
Comments and
Our Evaluation**

In response to our draft report, USAID/Jordan agreed with the audit recommendations. Appendix II presents the response in its entirety.

In regards to Recommendation No. 1, the Mission said that it had issued an administrative notice, summarizing key references from the Automated Directives System on performance measurement quality, and requesting strategic objective teams to conduct data quality assessments for all indicators used in its annual report. In addition, the Mission said that it had initiated a data quality assessment for microfinance results. Based on the Mission's comments, a management decision has been made on Recommendation No. 1.

In regards to Recommendation No. 2, USAID/Jordan said that procedures for data quality assessments had been prepared and issued by the Mission. Based on our review of the procedures, we consider that final action on Recommendation No. 2 has occurred.

**Scope and
Methodology****Scope**

We performed our audit in accordance with generally accepted government auditing standards and assessed USAID/Jordan's compliance with Automated Directives System Chapter 219 titled "Microenterprise Development" and USAID's Microenterprise Development Policy Paper. The audit also assessed whether USAID/Jordan's microfinance development activities had progressed towards their intended results for calendar year 2002.

We performed our fieldwork at USAID/Jordan's office in Amman, Jordan and at four microfinance institutions located in Amman. We also performed site visits to the institutions' branch offices and borrowers in various cities including: Amman, Madaba, Kerak, Tafeela, Aqaba, Jerash, and Irbid, Jordan. Fieldwork was performed from January 21 to June 16, 2003.

The audit scope included:

- Controls over the issuance of loans made by four microfinance organizations.
- A universe of 20,134 loans totaling \$8.5 million in disbursements made during calendar year 2002.
- Tests of 84 loans with disbursements totaling \$226,416.
- Documentation supporting 84 microenterprise loans.
- Interviews with 69 borrowers.

Methodology

To determine the accuracy of USAID/Jordan's database of 20,134 loans, we chose a 90 percent confidence level and assumed an error rate of 5 percent. We then randomly selected 84 loans to test. To assist us with our testing, we hired an Independent Public Accounting firm.

Our tests included reviewing 84 loan applications to determine whether they had been signed by the borrower and a loan officer and approved by someone other than the loan officer. Our tests also compared information listed on the borrower's loan application, such as the borrower's name, gender, and loan amount, to that which was recorded in the microfinance organization's loan database. Further, we interviewed the 69 borrowers in our sample to determine whether (a) the amount of their loan matched the amount recorded in the microfinance organization's loan database, (b) they were a repeat borrower, and (c) they had 10 or fewer employees, which would qualify them for a microenterprise business loan.

Our tests revealed that 1 of the 84 sampled loans (1.2 percent) was invalid because the borrower had more than 10 employees, and thus did not qualify for a microenterprise loan. Given that the error rate in our statistical sample was less than

five percent, we concluded with a 90 percent confidence level that the error rate in the database of 20,134 loans was also less than five percent.

Since this error rate fell below our five percent materiality level, we also concluded that we could generate reliable microfinance lending statistics from the loan database. We then compared these statistics to USAID/Jordan's planned targets for 2002 to determine whether microfinance development activities had progressed towards their intended 2002 targets. We also used the statistics to determine the extent to which USAID/Jordan's microfinance activities were benefiting women and the poor.

Management Comments



OFFICE OF THE DIRECTOR

August 13, 2003

To: Darryl T. Burris, RIG/Cairo

From: David Barth, Acting Director, USAID Jordan /s/

Subject: Audit of USAID/Jordan's Microfinance Activities
(Report No. 6-XXX-03-XXX-P)

Thank you for the draft of the subject report. Our comments are as follows:

Recommendation No. 1: We recommend that the Director, USAID/Jordan, require Mission officials to perform a data quality assessment of the microfinance results before using such results in the Mission's 2004 Annual Report.

Action to be taken: Mission is in full agreement with this recommendation. The Mission has issued an administrative notice dated August 3, 2003 summarizing the key references on performance measurement quality found in various parts of the ADS and requested the SO teams to conduct data quality assessments for all indicators used in the annual report. The data assessments will be conducted by the Mission for all indicators to be used in the Annual Report in the first quarter of FY 2004. Additionally, we are initiating the data quality assessment for microfinance results forthwith as indicated in the attached memo.

Recommendation No. 2: We recommend that the Director, USAID/Jordan, require the Program Office to develop a procedure to verify that the results included in the Mission's annual report have had data quality assessments.

Action to be taken: Procedures for data quality assessments have already been prepared and issued by the Mission. We have included a copy of the Mission Notice for your information. Please show this recommendation as closed in your final report.

We wish to thank you and your staff for the excellent coordination and collaboration during this audit.

USAID / AMERICAN EMBASSY, P.O. BOX 354, AMMAN 11118, JORDAN, PHONE: 5920101, FAX: 5920143
USAID, UNIT 70206, APO AE 09892 - 0206

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Summary of USAID/Jordan's Microfinance Results for Calendar Year 2002

Microfinance Institution	Number of Loans	Amount Disbursed (\$1 = JD 0.7)	Number of Borrowers	Number of Male Borrowers	Number of Female Borrowers	Number of Repeat Borrowers	Number of Male Repeat Borrowers	Number of Female Repeat Borrowers	Number of Poverty Loans (under \$350)	Amount of Poverty Loans Disbursed (JD 0.7 = \$1)
AMC ¹	697	\$3,023,404	686	476	210	252	145	107	0	0
CHF ²	1,495	4,368,859	1,448	992	456	271	110	161	239	\$42,233
JMCC ³	1,618	3,345,750	1,522	1,096	426	932	656	276	0	0
MFW ⁴	16,324	6,608,071	10,595	0	10,595	6,400	0	6,400	8,562	\$2,301,643
Totals	20,134	\$17,346,084	14,251	2,564	11,687	7,855	911	6,944	8,801	\$2,343,876

¹ AHLI Microfinancing Company.

² Cooperative Housing Foundation.

³ Jordan Micro Credit Company.

⁴ Microfund for Women.