



OFFICE OF INSPECTOR GENERAL

AUDIT OF USAID/IRAQ'S IRAQ RAPID ASSISTANCE PROGRAM (IRAP)

AUDIT REPORT NO. E-267-09-005-P
August 16, 2009

BAGHDAD, IRAQ



Office of Inspector General

August 16, 2009

MEMORANDUM

TO: USAID/Iraq Acting Mission Director, Thomas R. Delaney

FROM: Director, Office of Inspector General, Iraq, Gerard M. Custer /s/

SUBJECT: Audit of USAID/Iraq's Iraq Rapid Assistance Program (IRAP)
(Report Number E-267-09-005-P)

This memorandum transmits our final report on the subject audit. In finalizing the report, we considered your comments on the draft report and modified the report language as appropriate. Your comments are included in their entirety as appendix II.

The report contains three recommendations for corrective action. On the basis of your written comments, in which you described actions already taken or initiated to address our concerns, we consider that final action has been taken on all three recommendations.

I want to express my sincere appreciation for the cooperation and courtesies extended to my staff during this audit.

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SUMMARY OF RESULTS

The Iraq Rapid Assistance Program (IRAP) is designed to provide provincial reconstruction teams (PRTs) in Iraq with a flexible mechanism to make funding available to support community-based leaders and local Iraqi organizations and institutions in their efforts to improve access to public services, education, and economic opportunities. Grants awarded under the program, ranging from \$25,000 to \$2 million, fund a variety of activities, with the overarching goal of strengthening ties between Iraqi citizens, civil society, and governmental bodies. USAID/Iraq awarded a \$200 million contract to its implementing partner, Development Alternatives, Inc., to manage the grants and to support the PRTs in developing grant proposals for new projects. The performance period for this contract covers September 28, 2007 to September 30, 2010. As of March 31, 2009, cumulative obligations and expenditures under the program totaled approximately \$165.0 million and \$64.2 million, respectively. USAID had awarded 566 grants, valued at \$75.9 million, as of this date. (See page 2.)

USAID's IRAP program was achieving its goal for the majority of the grants reviewed. Specifically, the audit found that at least 30 of the 40 sampled grants tested (75 percent) were contributing toward this goal and had either fully or substantially achieved their intended results, as specified in their grants. Some of the reviewed grants had not fully achieved their intended results, however, because of a host of problems that included design-related issues, lack of coordination with local authorities, poor performance by the implementing partner's subcontractors, and weak monitoring. (See pages 3 and 6.)

In addition, the audit identified a series of financial irregularities—involving at least 18 of the 40 grants reviewed (45 percent)—that underscore the need for improved oversight. An examination of available expense records disclosed evidence of fictitious invoices, possible cost manipulation, and other improper billing practices. Indications of possible fraud or abuse were further substantiated during the audit when allegations were received of a payroll scheme under one of the active grants. The scheme reportedly involved both the grantee and the implementing partner's subcontractor—the entity responsible for monitoring the grantee. These irregularities were immediately referred to the OIG/Iraq's Office of Investigations for further investigative review. (See page 13.)

In light of these problems, the audit report contains three recommendations to improve monitoring procedures and controls. Specifically, USAID/Iraq should require its implementing partner to (1) establish appropriate procedures for monitoring active grants to ensure that grant implementation problems are identified, addressed, and reported to USAID in a timely manner; (2) adhere to prescribed payroll procedures when administering payroll activities for grantees; and (3) establish improved procedures to ensure that invoices and other records supporting expense claims are reviewed more thoroughly so that irregularities are detected and addressed. (See pages 12 and 16.)

In response to our draft report, USAID/Iraq concurred with all three recommendations and outlined measures that its implementing partner had already initiated or proposed to carry out to ensure that appropriate procedures and controls were in place to address the auditors' concerns. On the basis of the actions, we consider that final action has been taken on all of the recommendations contained in the report. (See page 18.)

Management comments are included in their entirety in appendix II.

BACKGROUND

Provincial reconstruction teams (PRTs)¹ in Iraq support efforts by community-based leaders and local organizations and institutions to improve access to public services, education, and economic opportunities. In August 2007, the Department of State (DOS) established the Quick Response Fund (QRF) Program to offer a flexible mechanism to obtain funding for these efforts. Responsibility for the overall management of this program was assigned to the Office of Provincial Affairs (OPA) at the U.S. Embassy in Baghdad, Iraq (Embassy Baghdad), which oversees the program's two components. OPA manages the DOS component directly while USAID manages a second component referred to in this report as the Iraq Rapid Assistance Program (IRAP). This audit focused on the latter component and did not include a review of the DOS component.

Under IRAP, assistance is provided—generally in the form of grants—to support Iraqi organizations in their efforts to carry out an array of activities addressing different civil society, community, and socio-economic development needs. Entities receiving grants typically include nongovernmental organizations and local and provincial governments. IRAP grants are initiated by the PRTs, subject to the approval of two technical evaluation committees, and vary in size from \$25,000 to \$2 million, depending on the type of recipient involved. The grants fund a diverse range of activities, with the overarching goal of strengthening ties between Iraqi citizens, civil society, and governmental bodies.

In administering the program, USAID awarded a \$200 million contract to Development Alternatives, Inc., to manage and monitor all IRAP-funded grant activities as well as to support the PRTs in developing ideas and grant proposals for new projects. To assist in this effort, the contractor (implementing partner) uses two Iraqi subcontractors that are responsible for procuring the goods and services to be provided under each grant and for directly managing and monitoring all grant activities, providing weekly activity reports along with all pertinent expense records to the implementing partner. Oversight of grant activities is also provided by the PRTs, each of which is staffed with an onsite USAID PRT representative who serves as USAID's liaison with the PRT.

Funding for IRAP comes from two sources—\$135 million in Supplemental Economic Support Funds and \$30 million in USAID Civil Society and Conflict Mitigation Program funds. Of the total \$165 million approved to date, over half is applied toward program support costs. As of March 31, 2009, IRAP's cumulative obligations and expenditures totaled approximately \$165.0 million and \$64.2 million, respectively, and the program had awarded 566 grants, valued at \$75.9 million.

AUDIT OBJECTIVE

As part of its fiscal year 2009 annual audit plan, the Office of Inspector General/Iraq conducted this audit to answer the following question:

- Is USAID's Iraq Rapid Assistance Program achieving its main goal?

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

¹ In this report, "PRT" refers to provincial reconstruction teams and embedded provincial reconstruction teams collectively.

AUDIT FINDINGS

USAID's Iraq Rapid Assistance Program (IRAP) was found to be achieving its goal for the majority of the grants reviewed. The audit determined, however, that some grants had not fully achieved their intended results. The audit also identified financial irregularities, such as fictitious invoices and indications of improper billing practices, which underscored the need for improved oversight. These areas are discussed below.

Program Was Achieving Its Goal for Most of the Grants Reviewed

With respect to the grant activities that were reviewed, the program was, for the most part, achieving its objective of strengthening ties between Iraqi civilians, civil society, and governmental bodies. Specifically, a review of the sampled IRAP grants found that at least 30 of the 40 grants tested (75 percent) had contributed toward this objective in one way or another and had either fully or substantially achieved their intended results, as specified in their grants. Of the remaining 10 grants, 2 were still active. Examples of several of the successfully completed grants are highlighted below.

- **Voter Education Outreach Activities.** On January 31, 2009, Iraqi voters went to the polls to elect provincial councils in 14 of Iraq's 18 provinces. In preparation for this key election, in which voters faced a large number of candidates representing a range of goals and ideals, the program engaged in one of the largest grass-root voter education efforts ever conducted. This initiative was carried out in two phases through a series of IRAP-funded grants totaling approximately \$6.3 million. During the initial phase, train-the-trainer grants were awarded to provide instruction to Iraqi civil society organizations located around the country on how to conduct voter education sessions. This phase was immediately followed by a second round of grants, which sponsored the voter education sessions conducted by the civil society organizations that had participated in the first phase. The grants also funded other activities, such as printing voter education literature and posters and producing media broadcasts, flyers, and billboards to support the election awareness campaign. The campaign, which continued up to the day of the election, was touted as a success. Records show that over 300,000 people attended the IRAP-sponsored voter education sessions held around the country, exceeding the original targets. Through the grant-sponsored media and voter education activities, the program reached more than an estimated 4 million people—nearly one-third of the eligible voting population for this election.
- **TV Electrical Power Upgrade.** This \$137,000 grant supported one of the few independent, nonsectarian TV stations operating in Iraq. The project involved the purchase and installation of two large electrical generators at the station's two transmission facilities. Due to the daily, chronic power outages experienced in the cities, the TV station has relied on generators to produce the necessary power required to maintain daily uninterrupted broadcast operations. The provision of the new generators, which were being rotated with the older units to minimize future repairs, has allowed the station to continue its operations and provide an important independent voice within Iraq and regionally.



Among the many IRAP-funded billboards, this one shows a sample ballot, used as part of an election-awareness campaign in preparation for Iraq's provincial elections held in January 2009. (Photo by DAI.)

- Health Capacity Building Project.** The purpose of this grant was to improve pediatric health care services in the Kurdistan Region by providing medical care for children suffering from heart disease and by offering much-needed on-the-job training for local medical personnel in diagnosis and treatment. In this region, children reportedly suffer from a higher incidence of congenital heart disease, malformations, and other disorders that are associated with the long-term effects of chemical bombings in Kurdistan between 1987 and 1991. Under this \$200,000 grant, funds were spent to purchase surgical supplies used by a medical team from Italy, who made several trips to the region to perform a series of operations and provide postoperative care. Much of the remaining funding covered the airfare associated with these visits. Regional and national government ministries also contributed funding to cover other costs such as hospital expenses and lodging for the medical team. As a result of this project, numerous children—many coming from poor families—received urgently needed medical treatment, including life-saving operations, that would not have been possible otherwise because of the cost involved or the lack of skills and experience on the part of the local surgeons and cardiologists. Upon the project's completion, a total of 937 patients had been examined and 90 operations, including 41 heart operations, had been performed successfully. Local medical staff participating in these operations received valuable on-the-job training, while 73 physicians also received formal training on heart diseases and pediatric surgery.

- **Revitalization of Regional Statistics Office.** The purpose of this grant was to modernize a regional statistics office and strengthen its capacity to collect, store, and analyze data as part of a broader effort to promote the government’s transparency and effective delivery of services. Specifically, this \$199,500 grant provided desktop and laptop computers, scanners, and licenses for several information software systems to facilitate data collection and analysis. During a visit to the regional statistics office, officials expressed their appreciation for the computer equipment and software provided under the grant. The equipment, which “filled a huge gap,” would substantially improve the office’s capacity to gather, enter, and analyze data efficiently and effectively. For example, one official stated that by using the new software and scanners, his staff would be able to read data on a computer-generated form at a rate of 70 forms per minute. The official stated further that the statistics office was planning to use the computer equipment provided under the grant in the coming months to gather and compile data to calculate the region’s gross domestic product—the first time this had ever been attempted in the region.
- **Electrical Transformers.** This \$157,951 grant involved the purchase of nine electrical transformers to be installed by a municipality in nine local villages in order to expand the electrical distribution network in the area. During the audit team’s visit to one of the villages, residents expressed their appreciation for the transformer, which provided almost twice as much electricity as before. One villager said that it had improved their lives by giving more people access to electricity as well as increasing the level of electricity each household received.



One of the electrical transformers provided under an IRAP grant that has benefited residents in nine villages by increasing their access to electricity. (Photo by OIG.)

However, not all of the IRAP grants reviewed were successful in achieving their intended results, and some were found to have financial irregularities, indicating that the program was possibly being overcharged for costs as a result of improper billing practices.

Intended Results Were Not Always Fully Achieved

Summary. Although the audit found that the majority of the IRAP grants reviewed had been satisfactorily completed, the planned results in some grants had not been fully achieved as specified in the grant agreement. Contributing factors included design-related deficiencies, poor coordination with local government authorities, grantees' failure to provide their share of resources or facilitate the work to be done, and poor performance on the part of the implementing partner's subcontractors. Also, because of inconsistent monitoring by the implementing partner, some problems noted during the audit were not identified and addressed promptly, highlighting the need for greater oversight. By not fully achieving their intended results, these grants had a limited impact, and in some cases, funds were wasted on activities that produced little if any benefit. While some of the underlying causes involved were deemed to be beyond the control of USAID and the implementing partner, one area where improvements could and should be made is in the level of oversight provided to grant activities to ensure that problems arising during grant implementation are identified, addressed, and reported to USAID in a timely manner.

Planned activities under each IRAP grant—including objectives, planned inputs, and period of performance—are specified in the grant agreement, along with the grant's authorized budget. In carrying out these activities, USAID's implementing partner relies on its two subcontractors to work directly with the grantees, procuring any required equipment or supplies and monitoring and reporting on the status of activities. The subcontractors are also expected to provide the implementing partner with documentation such as weekly activity reports, photos to substantiate the performance of activities, and invoices and other pertinent records to support expense claims.

Although the audit found that the majority of the 40 grants reviewed had been completed satisfactorily, it also identified 8 grants (20 percent) that had not fully achieved their intended results. Examples include the following projects.

- **Market Renovation Project.** This project, funded under several USAID-funded programs and by Coalition Forces, involved the renovation of a large, unoccupied market in Baghdad in order to provide a safe environment where vendors could sell fresh fruit and vegetables. As part of this multiple-program effort, costing approximately \$2 million, IRAP awarded a \$205,940 grant to refurbish an administration building and public restrooms situated on the market grounds. Although the planned work under this grant was completed in July 2008, the market has been mired in controversy and, more than a year later, remains closed—with approximately 730 stalls sitting empty and waiting for vendors to occupy them. According to USAID officials, the local governor's office has been reluctant to open this market to the public, despite that office's assurances that it would provide the resources for the security and management of the market. In April 2009, all of the USAID-funded infrastructure at the market was turned over to the governorate. The situation remains at an impasse, however, with many fixtures now at risk of being stolen or damaged in the interim.
- **Fish Market Renovation Project.** Another market renovation project beset with problems involved a grant to renovate one of the main fish markets in Baghdad. Once a thriving fish and vegetable market, this market fell into disrepair during

the war and was shut down, forcing vendors to move to a temporary location. Under this \$195,000 grant, renovations were performed on some 40 fish stalls at the market. Each stall—including the fish tanks, floors, walls, and partitions—was renovated, and existing electrical and plumbing systems were repaired. The project was completed and hailed as a success by the media, with an opening ceremony held on February 9, 2009. However, the market remains empty to this day, with no vendors occupying any of the shops. According to one USAID PRT representative, shortly after the market opened, a departing brigade commander assigned to the local PRT ordered the placement of concrete barricades (“T-walls”) around the entire perimeter of the market in an effort to increase security, a move that effectively (though inadvertently) cut off access to the market. One section of the wall has a small opening to provide an access lane, but the lane is too narrow for vehicular traffic and, therefore, produce cannot be delivered to the vendors’ shops in the market. After viewing the setup, vendors declined to move in, despite the newly renovated stalls. Unfortunately, removing the walls may be difficult because the local Iraqi security forces reportedly want to keep them in place. In an attempt to resolve the issue, efforts are being made to negotiate the removal of certain sections of the wall in order to increase access. In the interim, however, the market remains empty and unused.



A fish market, shown before and after being refurbished under an IRAP grant (Photos above by DAI.). Following its opening, in February 2009, the market remained empty because a security wall installed around the market’s perimeter effectively denied access. (Photo below by USAID.)



- **Rail Yard Rehabilitation Project.** This project involved renovations and repairs to rehabilitate a rail yard, with the intention of making the complex functional in preparation for the eventual restoration of rail service in the region. The \$200,000 grant included plans to repair water tanks and pumps at the rail yard's water treatment plant, procure and install two new generators, refurbish the passenger terminal and office areas, and procure tools for the train maintenance workshop. The repairs and other work were completed, but because rail service in the region has not yet resumed, the benefits derived from this grant have been minimal. With no rail service, operations at the rail yard were limited, with little need at this time for some of the new equipment. Of the two electrical generators, for example, only one was installed and in use at the time of the audit team's visit; the other—costing \$35,500—was found in a storage area. Likewise, the rail yard has had no need for the maintenance tools and has placed them in storage—many still in their packages. Questions arose about the usefulness and suitability of these tools—intended for a rail yard maintenance workshop and costing some \$14,000—since the tools seemed more suitable for repairing an automobile than a train. Work done at the rail yard's water treatment plant also produced disappointing results. Although the planned work at the plant (e.g., new pumps installed and water tanks repaired) was completed, the rail yard has been unable to obtain sufficient supplies of chlorine to treat the water chemically before pumping it to the homes of the railway workers living in the area. At the time of the audit team's visit, in May 2009, the plant had been without chlorine for several months—with no further deliveries expected—and was pumping out untreated water, drawn directly from a nearby river. The quality of this water, according to one PRT engineer, was considered to be unhealthy because the lower-than-normal level of the river typically results in a higher concentration of contaminants.



One of two electrical generators, costing \$35,500 each, provided under an IRAP grant in connection with an Iraqi rail yard rehabilitation project. Since regional rail service has not yet resumed, operations at the rail yard have been so limited that only one of the two generators was needed; the second one was placed in storage, as shown here. (Photo by OIG.)

- Government Center Automation Project.** In May 2008, the program awarded a \$200,000 grant to one of the provincial governorates in support of its efforts to automate its operations (e.g., payroll and accounting) and improve transparency. The grant's planned activities included installing a local area network within the governorate's "government center" and providing computer equipment, printers, photocopying machines, and computer training. Although the grantee received the equipment procured under the grant, the overall objective of this grant was only partially achieved. During a visit to the provincial governorate, the audit team verified the installation of the network but found that it was not being used. According to one official at the site, the governorate unaccountably did not want the computers to be connected to the network. As a result, with no access to a shared network, employees could use their computers only as stand-alone units, and some had no direct access to a printer. These limitations partially defeated the purpose of the grant. In addition, although most of the computers were allocated to the governorate's different departments, some were placed in storage. Of the 55 computers provided, 10 to 15 were left in storage, where some were stolen or were damaged as a result of water exposure. During their visit, the audit team also noted that two photocopiers—costing \$3,300 each—were not being used. One sat in a box in a storeroom and the other, still wrapped in plastic, in an office. According to one official, no one at the governorate knew how to set up the copiers and use them. Although the grant included technical training for a systems administrator and help desk staff, officials stated that no one had yet been identified and assigned to these positions, indicating that this technical training had not taken place.



Two photocopiers provided under a grant to a provincial government center remained in their packaging, unused, because no one at the center knew how to operate them. (Photos by OIG.)

The projects cited above provide but a few examples of the problems and difficulties that have prevented some grants from fully achieving the results envisioned in the grant agreement. Although the underlying causes for these problems varied and were not always clear, the audit identified some contributing factors. For example, project specifications were sometimes vague or erroneous; the PRT staff did not coordinate activities with appropriate local authorities; grantees did not fulfill their responsibilities, thus preventing the grant from being implemented as planned; the implementing partner's subcontractors provided poor quality inputs; and the implementing partner provided inadequate monitoring. These factors are discussed in further detail below.

In several cases, results were not fully achieved because of design-related issues. During the early stages of the program, according to one PRT staff member, some grants were drafted by military and PRT staff who had little technical expertise in the areas covered by the grant. Consequently, the drafters could not provide the level of detail or the accurate specifications necessary to ensure that the work was done properly and that required inputs were provided. As a result, some grant agreements contained vague specifications, such as in the rail yard grant (see page 8) in which the agreement provided little detail on the types of maintenance tools to be procured. Several PRT staff members stated that although improvements have been made, and PRTs are now staffed with more technical experts, staffing is still a problem.

Implementation was also hampered by problems stemming from grants not being coordinated with the appropriate local authorities. One example involved a market renovation project (see page 8) in which the PRT unit overseeing the project initially coordinated the grant with a representative of the local municipality who, as the PRT later learned, did not have authority to make decisions concerning the market. An official from the governor's office pointed out that the local governorate had sole authority for such decisions. On the basis of discussions with this official and his assurances that the security and management of the market would be provided, the PRT elected to coordinate the remaining work through him, believing he was the appropriate official. This assumption proved to be incorrect and has had unfortunate consequences. After the renovation work was completed, the governor (who has since left) refused to permit the opening of the market, reportedly claiming that he had not been informed of the project. The primary reason for the governor's reluctance to open the market remains unclear; however, as a former USAID PRT representative for this project pointed out, one factor may be that the governorate—despite earlier assurances—did not have the capacity to provide for the security and management needs of the market. Regardless, this example illustrates the problems that can arise when projects are not coordinated at an early stage with the appropriate local authority or official.



An administrative building at a large market in Baghdad which was renovated under an IRAP grant as part of a larger effort to refurbish this market. Although the renovation work was completed in July 2008, the market remains vacant to this day because the local governorate has yet to open it. (Photo by USAID.)

Grant activities were also constrained when grantees failed to provide critical resources under the grant or their actions hampered its implementation. Examples include the Rail Yard Rehabilitation Project, in which the rail yard could not obtain sufficient chlorine to treat the river water pumped from its water treatment plant, and the Government Center Automation Project, in which efforts to automate the center were impeded by the governorate's refusal to allow the new computers to be connected to the newly installed network.

Another contributing factor was poor performance by the implementing partner's subcontractors. The audit team noted at least several projects in which the inputs provided by these entities were of questionable—if not substandard—quality. In one grant, involving training sessions conducted in connection with a small business development program, the local PRT found that the instructors and the curriculum developed for the project were of poor quality. Moreover, the students selected to attend these sessions were not considered appropriate for the nature of the training. Quality was also an issue in a second grant, which authorized approximately \$83,000 for the installation of two generators (not provided under the grant) to supply electricity for a university. As part of the installation work, the subcontractor was responsible for building a shelter, with a roof, to house each generator and protect it from the elements. A site visit by the PRT staff disclosed, however, that the work performed was incomplete and reflected substandard quality. A structure had been built for only one of the two generators, leaving the other exposed to the elements. Moreover, the structure was judged to be of very poor quality and not up to structural standards—it lacked even a roof, since this had blown off the structure a week before the visit.



One of two generators installed under an IRAP grant to provide electricity for a university. The grant specifications called for the building of a shelter for each generator to protect them from the elements. However, as this photo reveals, the construction work was not fully carried out, leaving this generator exposed. (Photo by USAID.)

Performance issues such as these were exacerbated by inconsistent monitoring by USAID's implementing partner, which prevented certain implementation problems from being identified, addressed, and reported to USAID/Iraq in a timely manner. The level of monitoring in one region was found to be especially weak, despite the large volume of grants—the second highest in Iraq—awarded in this region. Visits to selected grant activity sites in the region disclosed deficiencies that the implementing partner apparently did not know about. During a visit to the activity site for the Government Center Automation Project, for example, it was clear that the implementing partner's program development officer, who accompanied the audit team during their visit, was unaware of the problems noted (see page 9), although this activity took place at a facility located near the PRT unit where she was based.

Apparently, this was not an isolated incident. Staff assigned to this PRT informed the audit team of other instances in which grant implementation problems were identified by the PRT staff—not the implementing partner—although the latter had primary responsibility for administering and monitoring those grants, mostly through its subcontractors. One example was the small business development grant (see page 11) in which a USAID PRT representative, through her own monitoring and followup efforts, found that not only was the quality of the trainers and curriculum deficient, the participants selected to attend the training were not appropriate as well. Further review by this PRT representative revealed that one of the trainers hired for this activity was receiving duplicate salary payments, under both the grant and another USAID-funded activity, for teaching the same class. After she reported this problem, action was taken and the trainer was fired.

Because they did not fully achieve their intended results, some of these IRAP grant activities were much less helpful to the Iraqi organizations, institutions, and people the grants were designed to benefit than originally had been envisioned—an unfortunate outcome, given the amount of resources allocated in developing and implementing each grant activity. Although these grants represented only a portion of the total grants reviewed, the highlighted problems warrant consideration and, in some cases, further attention and improvements. Any “lessons learned” may then be applied to future grants—not only in Iraq but also in other countries where plans to initiate a similar program may be underway.

While many of the problems were attributed to factors beyond USAID’s control, we believe that the implementing partner should increase its level of monitoring to ensure that problems or issues arising during the implementation phase are identified, reported, and addressed in a timely manner. Such monitoring should also include controls to ensure that the quality of work performed under each grant (services rendered and goods provided), by the implementing partner’s subcontractors, is at an acceptable level that is consistent with the intent of the grant. Accordingly, we recommend the following:

Recommendation 1. *We recommend that USAID/Iraq require its implementing partner to establish appropriate procedures for monitoring active IRAP grants to ensure that (1) implementation problems are identified, addressed, and reported to both USAID/Iraq and the responsible USAID PRT representative in a timely manner and (2) the quality of the work performed and goods provided is acceptable and consistent with the intent of the grant.*

Financial Irregularities Were Identified

Summary. In reviewing the records supporting the expenses claimed under the sampled grants, the audit team identified a series of financial irregularities that provide evidence that the implementing partner's subcontractors may have been engaging in improper—and possibly fraudulent—billing practices at the program's expense. For example, payroll records that document salary payments to grantee staff were found to sometimes contain noticeably similar signatures for different staff, indicating that one individual may have signed for these employees to certify the receipt of their salary. Indications of possible abuse in this area were further substantiated during the audit when reports were received of an alleged payroll scheme that had been going on under the program's largest active grant, reportedly involving the grantee and one of the implementing partner's subcontractors. In addition to the payroll area, the audit team identified other irregularities involving bills for equipment and other items that were supported with invoices that were highly suspect and apparently fictitious. We believe that these examples—and the probability that many went undetected—demonstrate that USAID's implementing partner did not have adequate controls in place and did not provide sufficient oversight, particularly over its subcontractors, to deter and detect these irregularities. As a result, the subcontractors may have been systematically overcharging the USAID program under a number of grants. Since the irregularities identified by the audit warrant followup, they have been referred to OIG/Iraq's Office of Investigations for further review.

The Federal Acquisition Regulation (FAR) states that *“a contractor is responsible for accounting for costs appropriately and for maintaining records, including supporting documentation, adequate to demonstrate that costs claimed have been incurred, are allocable to the contract, and comply with applicable cost principles”* (FAR subpart 31.201-2(d)).

In addition, USAID/Iraq's contract with its implementing partner included a provision stipulating that *“contractors, subcontractors and any other agents acting under contracts awarded herein are expected to employ due diligence and have internal controls in place towards practicing good governance in execution of the contract. . . . Any one of these entities found to have engaged in illegal activity, improper behavior, or corrupt practices will be subject to corrective actions.”*

In reviewing supporting records relating to expenses claimed under the sampled grants, the audit identified a series of financial irregularities, involving at least 18 of the 40 grants reviewed (45 percent), which indicated that the implementing partner's subcontractors may have been engaging in improper—if not fraudulent—billing practices to overcharge the program. Examples of some of the identified irregularities include the following:

- **Possible Payroll Abuse.** A review of the payroll records submitted under selected grants revealed evidence of potential abuse in this area. In payroll records, which list the names of the staff along with their signatures to certify receipt of pay, signatures for different staff appeared noticeably similar, suggesting that one person may have signed all the signatures and that the staff members listed may not have been paid.

- **Reported Allegations of Payroll Scheme.** Indications of possible payroll abuse were further substantiated by allegations that were received during the audit. During their fieldwork, the audit team received reports of an alleged payroll scheme involving one of the program's largest active grants, a \$2.9 million agricultural project to support the development of an agricultural cooperative in one of Iraq's provinces. According to the PRT staff overseeing this project, interviews with farmers who were members of the cooperative disclosed that some were not receiving the full amount of their monthly salary, as specified in the grant budget, and were being deliberately underpaid. Further inquiry revealed evidence to suggest that both the implementing partner's subcontractor—the entity tasked with administering the grant and ensuring that it was being properly implemented—and a senior official of the grantee were engaged in a payroll scheme to defraud the program by cheating the members of the cooperative out of a large portion of their salaries. According to a source at the PRT, the subcontractor paid the farmers only a fraction of their authorized monthly salary by the subcontractor and then billed the program for the full amount of the monthly salaries, presumably retaining the difference (i.e., "skimming"). After several months of being underpaid, the farmers claimed that they finally had received the full amount of their monthly salary—most likely in response to inquiries by the PRT staff—only to be coerced into returning a large portion of it to an individual who was linked to the grantee's director, who was supposed to be supporting the development of the cooperative. After conferring with the PRT on this matter, the mission terminated this grant in late July 2009.
- **Costs Incurred Identical to Budgeted Amounts.** In reviewing the expense claims submitted by the implementing partner's subcontractors, the audit team noted that the actual cumulative expenses claimed under each grant often matched the amount of the grant's authorized budget. That the amounts were identical normally would be quite remarkable since these budgets are generally based on cost estimates. Such occurrences were not surprising, however, because the subcontractors' fee was based on a percentage of the expenses incurred under the grant, up to the budget ceiling—creating a financial incentive to maximize the costs incurred up to the amount budgeted. The audit team raised the issue with one of the subcontractors only to be told that these cases were not common and merely a coincidence. The audit results indicated otherwise, however, and disclosed that instances in which actual costs claimed totaled the amount budgeted occurred in approximately 35 percent of the grants reviewed. Far from a coincidence, this high percentage was viewed as an indication of possible price manipulation.
- **Fictitious Invoices.** The audit also identified expense claims supported by invoices that were intended to give the appearance of being issued by separate vendors but that displayed almost identical handwriting, offering compelling evidence that one person wrote all the invoices. In one grant, the audit team found a generic invoice—with no vendor name or address identified—used to document a \$733,000 expense for the purchase of 20 tractors. The generic invoice was supported by 10 invoices, each charging \$73,300 for the purchase of 2 tractors. The 10 invoices were meant to seem as if they had been issued by different vendors, because they were printed on different letterheads, but the handwriting on all 10 was clearly the same, making them highly suspect. Although the tractors were all procured and delivered, their actual cost is uncertain since the invoices were considered fictitious.



One of 20 tractors purchased for an agricultural cooperative under an IRAP grant. The actual cost claimed by the implementing partner's subcontractor for these tractors was suspect because of irregularities identified in the supporting vendor invoices. (Photo by DAI.)

Although these irregularities may not all have stemmed from fraudulent activities, their going unnoticed until now indicates weaknesses in the implementing partner's monitoring procedures. The partner needs to improve its oversight and control mechanisms to ensure that its subcontractors follow prescribed procedures and to detect any irregularities in a timely manner.

One example of an area requiring greater oversight is payroll. The implementing partner routinely relied on its subcontractors to administer and supervise the payment of grantee staff salaries, but the partner did not always monitor the process adequately to ensure that its subcontractors were, in fact, following proper procedures. This lack of oversight was evident in the case of the payroll allegations reported under the agricultural grant (see page 14), in which the subcontractor not only failed to follow prescribed payroll procedures but appeared to be directly involved in a payroll scheme, possibly in collusion with the grantee. The problem was eventually identified and reported to USAID/Iraq, primarily as the result of the monitoring and followup efforts of the PRT staff, rather than those of the implementing partner, although the latter had primary responsibility for monitoring and administering the grant. Without question, the implementing partner needs to adjust its oversight and controls to include greater supervision of its subcontractors to make sure they follow prescribed procedures and to minimize the likelihood of similar incidents recurring in the future.

The need for this additional coverage was further highlighted by the following example. During the audit, the audit team learned that the subcontractors—who were responsible for administering the grant monies on behalf of the grantees for control purposes—were being permitted to transfer funds to the grantees' bank accounts so that the latter could

administer the payroll for their own staff. When asked about this practice, an official with one of the subcontractors acknowledged that it was taking place, but he assured the audit team that a representative from his office was always present at the grant site to oversee the monthly payroll distribution. However, during a site visit to one of the grantees operating under this arrangement, the director at the site informed the audit team that no one from the subcontractor was ever present during the grantee's monthly payroll. Other sites apparently also lacked such supervision. At a PRT unit in another region, a PRT staff member stated that she had received similar reports of payroll activities routinely carried out by grantees in her region without the presence of the subcontractor's representative.

Early detection of irregularities is critical since they can often result in the diversion of grant monies to unauthorized purposes thus reduce the funds available for legitimate grant activities. Irregularities can also reduce the program's impact on the target population or entities the grants were meant to help.

Needless to say, the irregularities identified by the audit are a source of concern. The examples provide evidence that the implementing partner's subcontractors may have been engaging in improper billing practices in an intentional effort to overcharge USAID, thereby misusing the grant monies entrusted to them under the program. Of greater concern, however, is the possibility that these irregularities may represent part of a wider, systemic problem involving other grants funded under the program. Regardless of the scope, we believe the irregularities warrant additional followup; accordingly, this matter has been referred to OIG/Iraq's Office of Investigations for further review.

In the interim, the implementing partner needs to improve its oversight of this area and institute more effective controls in order to be able to detect and address irregularities indicating potential fraud or abuse. Therefore, we recommend the following:

Recommendation 2. We recommend that USAID/Iraq require its implementing partner to establish appropriate procedural controls to ensure that its subcontractors are adhering to prescribed procedures in administering grantee payroll activities.

Recommendation 3. We recommend that USAID/Iraq require its implementing partner to establish appropriate financial review procedures to ensure that invoices and other financial records supporting expense claims submitted by the partner's subcontractors are reviewed more thoroughly so that irregularities, such as those identified by the audit, are detected and addressed in a timely manner.

Other Matters

In addition to the audit findings already discussed, the audit team identified one area that needs additional policy guidance to improve the effectiveness of the program and strengthen the level of oversight provided by the PRTs. Since responsibility for the overall management of program activities rests with Embassy Baghdad's Office of Provincial Affairs (OPA)—not USAID/Iraq—we are not making a formal recommendation on this issue, but we would like to offer the following comments and suggestions.

- **Monitoring.** Discussions with staff assigned to the different PRT units showed that they had differing views (and uncertainty) regarding the extent to which they were responsible for monitoring IRAP grants; some believed that this was entirely the implementing partner's responsibility. As a result, the level of monitoring being performed appeared to vary considerably among the staff. One reason for this variance is the current lack of standard operating procedures in place outlining the PRT staff's role and responsibilities in monitoring IRAP grants. We believe that detailed policies and procedures are needed as a priority, given the large volume of grants awarded under the program as well as the shift in the nature of these grants to capacity-building objectives, which are inherently more complex and require more intensive monitoring. Specifically, these policies and procedures should outline and delineate the roles and responsibilities of the PRT staff, including the USAID PRT representative, in managing IRAP grants during both the design and implementation phases. Among other issues, consideration should be given to requiring that (1) USAID's onsite PRT representative have an opportunity to review and clear all IRAP grant proposals before the PRT submits the proposals for approval; (2) grantees provide the PRTs with monthly activity reports and a copy of their closeout report; and (3) the USAID PRT representative be designated as the primary liaison between the PRT and the implementing partner, particularly with regard to any grant implementation problems or issues.

EVALUATION OF MANAGEMENT COMMENTS

In its written comments on our draft report, USAID/Iraq concurred with the findings and recommendations and outlined specific actions that Development Alternatives, Inc. (DAI) had initiated or planned to implement to ensure that appropriate procedures and controls were in place to address our concerns and improve oversight.

To address our first recommendation relating to the need for improved monitoring over active IRAP grants, USAID/Iraq stated that DAI has (1) launched an internal review into the specific issues raised to identify areas where oversight can be strengthened; (2) planned to conduct training for its staff on specific monitoring functions and procedural controls, which would continue monthly through the program's completion, to ensure that staff are conversant with prescribed procedures; (3) started requiring its senior local staff to conduct surprise site visits, security permitting, to ensure that grants are progressing as planned; (4) planned to supplement its monitoring by hiring individuals capable of performing spot checks and visits to IRAP grant venues independent of DAI's local staff and that of its subcontractors; (5) required its staff to perform spot checks to independently verify the quality of goods and services provided and to inform USAID and the relevant provincial reconstruction team (PRT) representative of any issues or concerns related to grant implementation; and (6) taken steps to improve the reporting and line of communication between DAI and the PRTs, particularly with regard to the availability of status updates on all IRAP grant activities.

To address the second recommendation, concerning the need for effective controls to ensure that DAI's subcontractors were adhering to prescribed payroll procedures, USAID/Iraq stated that DAI has (1) instructed its subcontractors to desist from the practice of transferring payroll funds to grantees; (2) started requiring its expatriate grant managers to conduct surprise visits to the grant sites, as security permits, to ensure that salary payments are being distributed per prescribed procedures; (3) tasked one of its grants managers with reviewing grants involving salary payments to verify that these payments are made properly each month and are documented using a predesigned form, indicating the amount each employee is authorized to be paid and signed by the employee, the grantee, and subcontractor representative overseeing the distribution; and (4) expressed its commitment to ensure that its staff and that of the subcontractor undergo continuous training on DAI's financial procedures.

To address the third recommendation, concerning the need for more thorough review of the financial records, USAID/Iraq stated that DAI has (1) initiated an internal investigation to determine whether the irregularities identified are more widespread; (2) proposed having a grants manager responsible for performing a detailed review of the vouchers and supporting expense records provided to DAI by its subcontractors to ensure that receipts are allowable, allocable, reasonable, and valid; and (3) committed to having an internal auditor from DAI's U.S. home office come out to review existing systems and the subcontractors' expenses on a quarterly basis.

We believe that the actions described above address our concerns, and we consider that final action has been reached on all three of our audit recommendations. The mission's comments are included in their entirety as appendix II.

SCOPE AND METHODOLOGY

Scope

We conducted this audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides that reasonable basis.

The purpose of this audit was to determine whether the Iraq Rapid Assistance Program (IRAP) was achieving its stated goal. A total of \$165 million, consisting of \$135 million in supplemental Economic Support Funds and \$30 million in USAID Civil Society and Conflict Mitigation Program funds, was allocated to support this program. Of the \$165 million, over half was applied toward program support costs. As of March 31, 2009, cumulative obligations and expenditures totaled approximately \$165.0 million and \$64.2 million, respectively. To carry out the program, USAID/Iraq awarded a \$200 million contract to Development Alternatives, Inc. (the implementing partner), to manage and disburse the grant monies as well as to directly monitor grant-funded activities.

As of March 31, 2009, the program had awarded 566 grants—including 211 grants funded with Civil Society and Conflict Mitigation Program monies—totaling \$75.9 million. The scope of this audit was limited to a judgmental sample of 40 grants, valued at \$10.5 million, which represented 14 percent of the total dollar value of the audit universe. The sampled grants were selected from 3 of the 18 Iraqi provinces (Baghdad, Al Anbar, and Erbil), and these 3 represented over half of the total volume of grants awarded.

The audit covered grant activities since the inception of the program in October 2007 through March 31, 2009, but it took into account activities subsequent to this period with respect to several sampled grants that were still active as of March 31, 2009.

In planning and performing the audit, the audit team assessed relevant controls used by the mission to manage the program and ensure that its implementing partner was providing adequate oversight of grant activities. Specifically, these controls included (1) maintaining regular contact with the implementing partner's main office; (2) requiring the implementing partner to submit weekly and quarterly progress reports providing a narrative overview on the status of active grants in the different provinces, including any significant issues or notable developments; (3) obtaining a weekly spreadsheet from the implementing partner providing a comprehensive listing of all of the grants awarded for use in tracking the status of these grants; and (4) obtaining weekly reports from the USAID representatives at the provincial reconstruction team (PRT) units located throughout Iraq. Additionally, the auditors examined the mission's fiscal year 2008 annual self-assessment of management controls, which the mission is required to perform to comply with the Federal Managers' Financial Integrity Act of 1982.

Audit fieldwork was performed at the USAID/Iraq Mission and the implementing partner's main country office, both of which are located in the International Zone in Baghdad, Iraq, from March 18, 2009, through July 16, 2009. Also, site visits were made to two PRT units and the activity sites for 9 of the 40 sampled grants.

Methodology

To determine whether the program was achieving its intended goal, the audit team initially interviewed pertinent staff at USAID/Iraq's PRT Office and the implementing partner's main country office, via e-mail and in person, to gain an understanding of the program, all of the key players and their roles and responsibilities, and the reporting procedures and controls in place for monitoring the program. In answering the audit objective, the audit was limited to an overall assessment of whether the program's stated goal was being achieved with respect to the 40 sampled grants. This assessment was based on the audit team's review of these grants, which involved individual analyses focusing on determining whether (1) planned activities under each sampled grant appeared to contribute toward the program's goal; (2) planned inputs for the sampled grants were, in fact, provided as required; and (3) intended results were being achieved.

The audit team's analysis of the 40 sampled grants included a review of relevant grant documents on file with the implementing partner. These included the grant proposal; correspondence documenting the clearance and approval of the grant; and the grant agreement, expense reports, supporting invoices, inventory reports, photographs, receiving reports certifying the receipt of goods by the grantee, and any closeout reports. In addition, site visits were made to the activity sites for selected grants to perform a physical inspection to verify the provision of specific equipment. During these visits, interviews were held with grantee and PRT staffs to determine whether they were aware of any implementation problems and to solicit the staffs' views on whether intended results had been achieved. Interviews were also held with the field staffs for both the partner and its subcontractors.

Because the grants awarded under the program varied greatly in their activities, it was not possible to quantify their collective impact. Instead, the audit team assessed the impact of individual grants on the basis of the results (i.e., outputs) achieved under each.

In assessing whether the implementing partner was providing adequate oversight of its IRAP-funded grant activities, the audit team initially conducted interviews at the offices of the partner and its two subcontractors to gain an understanding of their procedures for monitoring grants. Discussions were also held with the USAID PRT representatives to assess the extent to which they were kept informed, by the implementing partner, of any implementation problems or issues within the PRT's area of responsibility. Additionally, the auditors examined selected grant records on file at the implementing partner's main country office, such as activity reports, as evidence of the information received and the extent of oversight provided by both the partner and its subcontractors.

In addition, the audit team reviewed applicable policies and procedures relating to the management of IRAP operations. These included policy guidance issued by Embassy Baghdad's Office of Provincial Affairs, USAID/Iraq, and the implementing partner.

In assessing the overall results of the auditors' analyses, the audit team established a materiality threshold of 75 percent. For example, if at least 75 percent of the sampled grants reviewed were found to have achieved their intended results, the auditors concluded that these grants were achieving the program's stated goal. Similarly, if at least 75 percent of the planned work under a grant was successfully completed, the auditors concluded that the work under the grant was substantially completed.

MANAGEMENT COMMENTS



August 12, 2009

MEMORANDUM

TO: Director, Office of Inspector General, Iraq – Gerard M. Custer

FROM: USAID/Iraq Acting Mission Director – Thomas R. Delaney /s/

SUBJECT: Management Comments to Draft Audit Report No. E-267-09-005-P

Thank you for affording the USAID/Iraq Mission an opportunity to respond to the draft audit of USAID/Iraq's Iraq Rapid Assistance Program (IRAP). The Mission concurs with the audit findings and recommendations and the Mission's comments on the overall report can be found below. Specifically we have responded to the three recommendations outlined in the draft OIG audit report, addressing actions taken or actions which are soon to be implemented.

Background

The Office of the Inspector General (OIG) draft audit report on the Iraq Rapid Assistance Program (IRAP) was provided to the Mission on July 20, 2009 and acknowledged that "the program was determined to be achieving its goal for the majority of the grants reviewed." USAID's IRAP program is a complex grants-under-contract mechanism in which the activities concept is developed at the Provincial Reconstruction Team (PRT) or embedded PRT (ePRT) level and elevated for review to a technical committee. The committee is chaired by the US Embassy in Iraq with USAID and other interagency participation. Once approved by the technical committee, final approval is granted by an interagency team in Washington. The OIG report cited a project success rate of at least 75% (excluding an additional 5% of active grants). This success rate should be viewed as an outstanding achievement considering the difficulties faced by the implementing partner while working in Iraq.

Each of the findings and recommendations has been examined to determine 1) whether the Mission is in agreement and 2) what actions would be undertaken in response to the audit. The Mission is in agreement with the findings and recommendations of the audit and has taken the actions described below in response to the audit. The Mission recognizes the value of this audit as a management tool.

After receipt of the audit report the USAID Mission met with DAI on July 21, 2009 to bring to their attention the issues identified in the report as they were significant enough to warrant immediate action by DAI in order to safeguard USAID resources under the contract. On July 27, 2009 the USAID Contracting Officer (CO) issued a formal letter

requiring DAI to take specified corrective measures and provide USAID with a plan of action and timeline for accomplishing the corrective measures identified no later than COB August 6, 2009. DAI met the deadline and their responses are incorporated under each recommendation. We believe that DAI is taking the findings and recommendations of the draft audit report seriously. After learning about the report findings, DAI's Chief Financial Officer from their home office in Maryland immediately flew out to Iraq to meet with the DAI team and initiate an internal audit/review. DAI also held an initial meeting with the OIG investigator with regards to the financial discrepancies identified in the report.

Below are the management decisions regarding the proposed audit recommendations:

Recommendation No. 1: We recommend that USAID/Iraq require its implementing partner to establish appropriate procedures for monitoring active IRAP grants to ensure that (1) implementation problems are identified, addressed, and reported to both USAID/Iraq and the responsible USAID PRT representative in a timely manner and (2) the quality of the work performed and goods provided are at an acceptable level that is consistent with the intent of the grant.

Management Decision:

In addressing USAID's concerns and the OIG draft audit report recommendation, DAI has agreed to the following actions:

1. DAI has already commenced an internal review and methodological examination into the specific issues raised by USAID. The scope of the review is not limited to the issues cited by the OIG. Rather, DAI will advise USAID of all relevant information regardless of whether identified by the OIG or not. DAI IRAP is committed to improving upon current efforts which provide oversight of grant activities in order to ensure that problems which arise during grant implementation are identified, addressed, reported and rectified in a timely and coherent fashion.
2. To ensure existing procedures and controls are entirely followed, DAI will conduct supplemental training on specific monitoring functions with the first training to occur not later than September 15, 2009. Additionally, the first training on appropriate procedural controls from the approved policies and procedures will occur no later than September 30, 2009. Both types of training will occur on a regular monthly basis thereafter in each DAI office and will include more in depth sessions at the up-coming strategy planning sessions and closeout. DAI Senior Management is tasking IRAP Financial Officers in each local office to review financial and procurement procedures. DAI IRAP Financial Director and DAI Internal Auditors will confirm training is completed and continues through program completion.
3. Starting immediately, DAI will ensure that senior local DAI staff will conduct periodic site visits to ensure implementation is running as planned. The documented spot checks and surprise visits will be conducted with the caveat that visits may be limited due to security reasons - especially regarding planned expatriate travel. DAI will visit the

grant locations to check on implementation, dependent upon security, at least once during each grant's implementation. These visits will be made in addition to visits made by the subcontractor RO.

4. DAI is planning within the approved budget to subcontract an augmented monitoring function capable of performing spot checks and visits to IRAP grant venues. This will supplement DAI's current site visits and monitoring efforts by using non DAI ROs and current local staff. DAI will supply individuals capable of making the spot checks independent of the RO's and regular DAI local staff. This additional review will serve as a supplemental layer of quality control over and above the anticipated management reporting system.
5. DAI will use DAI local staff, DAI expatriates staff (where possible), and (IRAP approved budget permitting) additional subcontractors to perform spot checks to independently verify the quality of goods and services provided. DAI will inform USAID and the PRTs of any issues/concerns related to grant implementation and present them to the PRT's and USAID representatives in a timely manner.
6. DAI will ensure that DAI's IRAP Senior Program Development Officers (SPDO) review and augment current communications and report to the PRTs. This will enhance lines of communication regarding the availability of reporting and status updates on all DAI IRAP activities. DAI IRAP will continue to provide documents to the PRT's and assist with facilitating accurate and timely reporting on all of DAI's IRAP project grant activities.
7. DAI IRAP Senior Grant Managers and IRAP Local Staff are proactively working with the PRTs to enhance efforts of DAI IRAP's project SPDOs to ensure that PRTs consult with DAI and all grant proposals are run past the USAID representatives prior to presenting grant proposals and budgets to QRF OPA/ETEC and USAID for approval.
8. DAI will conduct training on appropriate procedural controls from the approved policies and procedures. The first training will occur no later than September 30, 2009 and will occur on a regular monthly basis thereafter in each DAI office. Additionally, the up-coming DAI IRAP strategy planning sessions and closeout sessions will include more in-depth sessions.

Recommendation No. 2: We recommend that USAID/Iraq require its implementing partner to establish appropriate procedural controls to ensure its subcontractors are adhering to prescribed procedures in administering grantee payroll activities.

Management Decision:

In addressing USAID's concerns and the OIG draft audit report recommendation, DAI has agreed to the following actions:

1. Ensure that all DAI staff and Resource Organization staff members continually undergo training and refresher courses on DAI financial policies and procedures approved by USAID and established for the IRAP program.
2. Remind the ROs that failure to adhere to proper grantee salary payments may result in the termination of subcontracts for RO services to DAI. DAI will ensure all grants with salary payments are carried out according to approved and agreed amounts and are in accordance with the DAI IRAP financial/procurement policies. If there are instances where salaries are improperly paid DAI will immediately notify USAID and the relevant PRT Representative.
3. Strongly reiterate to the ROs that salary payments are not to be made using lump sum transfer to grantees, including grantees' bank accounts. DAI has informed the ROs that DAI may terminate subcontracts if the subcontractors are unable to justify salary payments or provide a field procurement in accordance with established DAI procedures. Where allowed by security, DAI expatriate grant managers will conduct surprise or spot checks to ensure payments are being conducted per the DAI policies and procedures governing salary payments.
4. Conduct its own review of all grants with pending salary payments and verify that all salary payments are made each month using a Grants Manager charged with supplemental voucher examination duties in accordance with established DAI policy, procedures and instructions. Employees are paid under approved IRAP grants using appropriately designed forms to document the payment of salaries. The forms including the employee's name, payroll period, amount each employee is authorized to be paid (in Arabic), and the signature of the employee, as well as signatures of the grantee representative, and Subcontractor/RO representative(s) overseeing the distribution.

Recommendation No. 3: We recommend that USAID/Iraq require its implementing partner to establish appropriate financial review procedures to ensure that invoices and other financial records supporting expense claims submitted by the partner's subcontractors are reviewed more thoroughly so that irregularities, such as those identified by the audit, are detected and addressed in a timely manner.

Management Decision:

In addressing USAID's concerns and the OIG draft audit report recommendation, DAI has agreed to the following actions:

1. DAI will propose to USAID to convert one IRAP SPDO position to a Grant Manager, who will perform detailed voucher examination and be dedicated to reviewing the receipts and vouchers provided to DAI by its Subcontractors. This position will be 100% devoted to the effort of ensuring that all receipts presented by the subcontractor ROs are complete, allowable, allocable, valid, accurate, reasonable, and are compliant with USAID and DAI policies and procedures. The invoices will be presented to the Grant Manager with this review in addition to the local DAI IRAP staff who also reviews the invoices

received. This Grant Manager will validate the financial documents before approval for payment. DAI will propose that this position be filled no later than October 1, 2009.

2. DAI commits to send a DAI/Home Office internal auditor to review DAI IRAP systems once per quarter until program conclusion on September 30, 2010. After visiting DAI IRAP during the week of July 31- August 6, DAI's Director of Internal Audit has committed to dedicating a DAI internal auditor to visit IRAP once per quarter. The DAI internal auditor will also audit expenses of the DAI subcontractors on a quarterly basis.
3. DAI will remind, reinforce and re-train all DAI IRAP staff; including local staff members that a DAI support mechanism exists in which staff can convey any acts of impropriety, fears, or perceived threats. Written materials detailing DAI's support mechanism are available in three languages. DAI maintains an international hotline for whatever issues DAI staff members might need, want or choose to disclose. This international DAI hotline is similar in nature to USAID's OIG Hotline, but is internal to DAI. DAI staff members worldwide may also reach out and communicate financial or other programmatic concerns through the hotline. DAI's internal ethics hotline allows staff members to anonymously identify any threats or acts of intimidation.
4. Having been informed of the identified financial irregularities, DAI immediately started investigation on whether issues of financial irregularity may exist on a more widespread basis.

In the "Other Matters" section the Draft Audit report also highlighted that there is confusion among non-USAID PRT staff as to their role when it comes to IRAP proposal development and oversight. USAID is working with OPA to further clarify non-USAID PRT staff role and responsibilities with regard to the IRAP program.

Based on the above, we believe that the actions taken by USAID/Iraq and DAI have adequately addressed the three audit recommendations and the auditors' concerns. We hope that these actions are sufficient to achieve final action on the recommendations.

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