



OFFICE OF INSPECTOR GENERAL

AUDIT OF USAID/PARAGUAY'S DEMOCRACY AND GOVERNANCE PROGRAM

AUDIT REPORT NO. 1-526-16-004-P
JANUARY 15, 2016, REISSUED JANUARY 21, 2016

SAN SALVADOR, EL SALVADOR



Office of Inspector General

January 21, 2016

MEMORANDUM

TO: USAID/Paraguay Mission Director, Fernando Cossich

FROM: Regional Inspector General/San Salvador, Jon Chasson /s/

SUBJECT: Reissuance of Audit of USAID/Paraguay's Democracy and Governance Program (Report No. 1-526-16-004-P)

This memorandum transmits the revised final report on the subject audit. In finalizing the audit report, we considered your comments on the draft report and included them in Appendix II. The original audit report has been revised to reflect that the mission's management decision on Recommendation 1 also represents final action. In addition, we updated the target completion dates for Recommendations 5 and 6 based on new information from the mission. These revisions do not impact the report's conclusions, recommendations, or the mission's management decisions thereon.

This report includes 14 recommendations to help improve USAID/Paraguay's implementation of its Democracy and Governance Program. After reviewing information provided in response to the draft report, we acknowledge management decisions on all 14 recommendations and final action on Recommendations 1 through 4, and 7 through 14. While we acknowledge the mission's management decision on Recommendation 1, we disagree with it. We further acknowledge that for Recommendation 5 the mission sustained \$8,064.61 in unallowable costs, and for Recommendation 6 sustained \$2,258.28 in unallowable costs. The mission issued bills of collection for these amounts. Please provide evidence of final action on the open recommendations to the Audit Performance and Compliance Division.

I want to thank you and your staff for the cooperation and assistance extended to us during this audit.

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Abbreviations

The following abbreviations appear in this report:

ADS	Automated Directives System
CDCS	Country Development Cooperation Strategy
MSI	Management Systems International
CFR	Code of Federal Regulations
NGO	nongovernmental organization
NUPAS	Non-U.S. Organization Preaward Survey
M&E	monitoring and evaluation
RIG	Regional Inspector General

SUMMARY OF RESULTS

USAID/Paraguay's Country Development Cooperation Strategy (CDCS) for 2014 through 2018 aims to support the creation of "a more prosperous, well governed democracy in Paraguay." The mission plans to achieve this goal by awarding 100 percent of its program funds through government entities or local organizations; doing so would exceed the Agency-wide target of 30 percent of funds awarded locally.

A key component of the mission's CDCS is strengthening the internal management and governance systems of select public institutions. To do that, effective October 1, 2013, USAID/Paraguay awarded a \$24.4 million, 5-year cooperative agreement to Centro de Estudios Ambientales y Sociales (Center for Environmental and Social Studies; the Center). As of December 31, 2014, USAID/Paraguay had obligated \$7.6 million and disbursed \$5 million for the Democracy and Governance Program.

The program planned activities in three areas:

1. Increasing institutional capacity of select public institutions.
2. Strengthening accountability and anticorruption efforts in select public institutions.
3. Advancing the legal and policy framework for effective governance.

The Regional Inspector General/San Salvador (RIG/San Salvador) conducted this audit to determine whether USAID/Paraguay's Democracy and Governance Program was achieving its main goal—which, like the CDCS's key component, is strengthening the internal management and governance systems of select public institutions. The audit team judgmentally selected 10 of the 14 public institutions the program is working with for review.

The audit reviewed the program's work plans and found that the Center successfully provided technical assistance in the 28 activities that began during the first year. Only one of these activities was behind schedule: the development of a merit-based recruitment system for the judiciary¹. As of December 31, 2014, the program had:

- Started implementing the civil service's computer system for human resource management. It had also launched a corresponding online portal, where all merit-based job openings in the civil service are posted.
- Improved and updated the tool used to measure how well the civil service manages human resources. Using the tool in the four public institutions—(1) Ministry of Finance (2) Ministry of Public Works and Communications, (3) Ministry of Public Health and Social Welfare, and (4) Ministry of Public Service—led to the development of improvement plans for those ministries.
- Integrated the national public procurement system with the Ministry of Health's new inventory system for better management of procurement and accurate tracking and management of medical supplies.

¹ Not part of the civil service.

- Introduced the Standard Internal Control Model for Public Institutions in three of the institutions. The Government of Paraguay developed the model in 2008 in carrying out the Financial Administration Act, one of many steps to reform procurement and reduce corruption. In addition, the program developed unified standards for how the two Paraguayan Government audit bodies, the Comptroller General and the Executive Audit Secretariat, would evaluate internal control in the ministries using the model.
- Developed and implemented a standard platform for e-government in two of the selected public institutions.
- Started implementing Open Government Platform and Open Data Catalogue² in three of the institutions following the passage of the Law on Free Access to Public Information and Governmental Transparency.

Despite these positive actions, auditors could not determine if the program was achieving its main goal because the monitoring and evaluation (M&E) plan initially developed by the project could not measure progress as required by USAID guidance. The data needed to track progress on many of the program's original performance measures or indicators were not available, some of the indicators were repetitive, and some indicators were not really measuring the expected results. Moreover, the Center, a first-time implementer, did not have the capacity or knowledge to gather and measure the results of the 25 indicators in the M&E plan.

At the time of audit fieldwork, USAID/Paraguay and the Center had already started overhauling the program's M&E plan. The mission was providing training on monitoring and evaluation and was helping the Center streamline the M&E plan, reduce the number of indicators by half, and focus on measuring impacts and results. Auditors reviewed the draft of the revised M&E plan and confirmed that the revisions meet USAID standards. Because the mission took these actions, the audit does not make recommendations to do so.

Still, the audit identified the following problems related to working with the Center:

- USAID/Paraguay did not fully assess, identify, or monitor the risk of using a local organization (page 5). In the preaward survey it completed for the Center, the mission did not appropriately assess risk. Furthermore, the mission did not include specific conditions in the agreement to address all of the weaknesses identified, nor did it adequately monitor to see if the Center had implemented the specific conditions.
- The implementer had weak controls in some areas (page 8). The audit disclosed weak management controls related to competition, conflicts of interest, and payroll.
- The implementer's hiring practices did not comply with USAID guidance (page 10). It filled positions with consultants whom it paid more than the rates budgeted for employees. It may also have violated local labor laws.
- The mission did not structure the award to promote sustainability (page 12). The mission awarded the agreement without indirect costs (overhead) and required the first-time local implementer to contribute toward the program's costs. The Center needed to have its overhead costs covered in order to expand its business and diversify funding sources.

² Online tools for sharing government data—action plans, activities, budgets and financial information—with the public.

To improve project management, we recommend that USAID/Paraguay:

1. Complete an analysis of the Center that meets the requirements for a Non-U.S. Organization Preaward Survey, assessing areas not covered by the preaward survey or this audit, which will also serve as a learning experience on how to conduct a Non-U.S. Organization Preaward Survey (page 6).
2. Determine whether to add specific conditions to the award and whether to extend timelines for specific conditions and have the agreement officer modify the award as necessary (page 7).
3. Develop a formal plan for monitoring and facilitating progress by the Center on specific conditions to improve the program's financial and administrative control environment, or terminate the agreement (page 7).
4. Instruct the Center in writing to revise its procurement practices to meet requirements for competition, including proper advertising and unbiased selection of vendors (page 9).
5. Determine the allowability of \$406,910 in ineligible questioned costs related to the lack of competitive bidding, and recover from the Center the amount determined to be unallowable (page 10).
6. In coordination with the Center, mitigate the conflict of interest, calculate the fair value of office space funded by USAID for the Democracy and Governance Program that the subcontracted consulting firm occupied rent-free, have the agreement officer determine the allowability of the calculated amount, and recover from the Center any amounts determined to be unallowable (page 10).
7. Work with the Center to revise its payroll process to track payroll hours for employees not fully dedicated to the program (page 10).
8. In coordination with the Center, review the subaward between Management Systems International (MSI) and the Center, document and calculate the costs of any subaward requirements that MSI did not meet, have the agreement officer determine the allowability of the calculated amount, and recover from the Center any amount determined to be unallowable (page 10).
9. Develop a formal plan for monitoring and supporting the Center that provides appropriate oversight through coaching and regular financial reviews to ensure proper accountability for funds provided to the organization (page 10).
10. Instruct the Center, in writing, to pay employees at the rates in the award budget (page 11).
11. Work with the Center to determine and document the most cost-effective method for staffing program positions that complies with local labor laws (page 11).
12. Have the agreement officer amend the Democracy and Governance Program agreement to include the latest mandatory standard provisions for non-U.S. nongovernmental organizations (NGOs) as noted in A Mandatory Reference to Automated Directives System (ADS) 303, "Standard Provisions for Non-U.S. Nongovernmental Organizations" (page 12).

13. Have the agreement officer amend the award for the Democracy and Governance Program to cover the Center's indirect costs or require the Center to seek new funding sources so that costs associated with doing so would become direct costs (page 13).
14. Evaluate and document whether to adjust the Center's cost-share percentage in accordance with the organization's particular circumstances, and have the agreement officer modify the award as necessary (page 13).

Detailed findings appear in the following section. The scope and methodology are described in Appendix I. Management comments appear in their entirety in Appendix II, and our evaluation of management comments begins on page 14.

AUDIT FINDINGS

USAID Did Not Fully Assess, Identify, or Monitor the Risk of Using a Local Organization

Under the Local Solutions initiative, USAID “embraces new models for public-private partnerships and increased investment directly to partner governments and local organizations.” However, USAID recognizes that there is a higher risk involved in working directly with these new partners. Therefore, in 2012, USAID revised its processes and procedures for awarding funds directly to local NGOs.³

Under the new procedures, before making an award to a local NGO, USAID must conduct a risk assessment to confirm that the applicant meets USAID’s requirements. ADS 303, “Grants and Cooperative Agreements to Non-Governmental Organizations,” provides two options for conducting the risk assessment. The first is to use the “Non-U.S. Organization Pre-Award Survey [NUPAS] Guidelines and Support”⁴ (NUPAS Guidelines), and the second is to conduct a detailed analysis with the same objectives as a NUPAS, to:

- (1) determine whether the organization has sufficient financial and managerial capacity to manage USAID funds in accordance with U.S. Government and USAID requirements,*
- (2) determine the most appropriate method of financing to use under the potential USAID award, and*
- (3) determine the degree of support and oversight necessary to ensure proper accountability for funds provided to the organization.*

The second option is familiar to many USAID staff members because it is used for U.S. NGOs.

After the risk assessment is completed, USAID is required to include specific conditions⁵ in the award to mitigate risks identified during the assessment. USAID also is required to implement a monitoring plan to ensure that the recipient corrects the noted deficiencies, thereby satisfying the specific conditions in the time allotted.

However, the audit identified areas where the mission did not follow this guidance.

USAID’s Risk Assessment Did Not Meet NUPAS Requirements. A NUPAS risk assessment includes 29 evaluation elements, the items most critical to determine risk before an award is given to a local NGO. USAID/Paraguay chose not to use NUPAS guidelines, relying instead on

³ ADS 303.3.9.1, “Preaward Survey,” and its mandatory reference ADS 303mab, “Standard Provisions for Non-U.S. Nongovernmental Organizations” (Standard Provisions).

⁴ ADS 303sam.

⁵ The Office of Management and Budget’s final guidance on 2 CFR 200, “Reducing Administrative Burden and Waste, Fraud, and Abuse,” Subsection 8, “Strengthening Oversight,” requires agencies to impose “specific conditions where necessary to mitigate potential risks of waste, fraud, and abuse, before the money is spent.”

the more familiar preaward survey methodology used to evaluate risks of U.S.-based organizations. However, this preaward survey did not achieve the same objectives as a NUPAS.

Specifically, the preaward survey the mission conducted for the Center did not address 14 of the 29 areas listed in NUPAS. Most critically, the mission did not evaluate the Center's policies, procedures, and capabilities in the following areas: compliance with legal requirements, management of bank accounts, internal controls over direct and indirect costs, the price reasonableness of procurement actions, maintenance of financial records, and project management. Because of these limitations, the mission's assessment of the Center did not identify numerous weaknesses. An evaluation of the Center's ability to comply with procurement policies and procedures might have revealed that the organization lacked proper procedures to hire consultants and meet Paraguay employment requirements, a weakness addressed later in this report. Similarly, a thorough review of the Center's internal control systems might have revealed that the organization had weak financial controls, as discussed later in this report.

According to USAID/Paraguay officials, the preaward survey did not meet all of the NUPAS objectives because mission personnel did not understand the new process and believed the preaward survey they had conducted provided the agreement officer with sufficient information to determine the level of risk.

By not conducting a risk assessment that met the objectives of a NUPAS, the mission put \$24.4 million at risk. The local NGO that received the agreement did not have sufficient financial and managerial capacity to manage USAID funds, assess results, or track program progress.

Therefore, we make the following recommendation.

Recommendation 1. *We recommend that USAID/Paraguay complete an analysis of Centro de Estudios Ambientales y Sociales that meets the requirements for a Non-U.S. Organization Preaward Survey, assessing areas not covered by the preaward survey or this audit, which will also serve as a learning experience on how to conduct a Non-U.S. Organization Preaward Survey.*

USAID Did Not Include Specific Conditions for All Identified Risk Areas. According to ADS 303.3.9.2, when a risk assessment determines that a local NGO is high-risk, the award may still be made as long as it includes specific conditions designed to mitigate the identified risk. These conditions may be of limited duration or cover the entire period of the award, and the mission must develop and carry out a plan for monitoring them.

While limited in scope as noted above, the mission's preaward survey found the Center to be high risk because of numerous weaknesses with its policies and procedures, accounting system, and administrative and financial processes. However, while the mission formulated two specific conditions to mitigate risks, it did not include conditions in the award to address all of the identified risk areas. For example, while the preaward survey concluded that the Center's lack of internal controls made paying them with advances versus cost reimbursement a high-risk payment method, the award did not include a specific condition to address this risk. Similarly, the preaward survey indicated the Center would need to reassess its policies regarding segregation of duties and financial matters, but the mission inserted no conditions to address them.

Mission officials explained that they did not understand that they needed to add recommendations or specific conditions for all the risk areas they identified. By not having

sufficient specific conditions in the award, the mission could not improve the financial and managerial capacity of the local NGO or ensure proper accountability for funds.

Therefore, we make the following recommendation.

Recommendation 2. *We recommend that USAID/Paraguay determine whether to add specific conditions to the award for the Democracy and Governance Program and whether to extend timelines for specific conditions already imposed, and have the agreement officer modify the award as necessary.*

USAID/Paraguay Did Not Monitor Implementation of Specific Conditions. The preaward survey noted that USAID/Paraguay should perform at least two financial reviews in the program's first year (at the 2- and 6-month marks) to assess the implementation of specific conditions. Additionally, the agreement stated that the conditions would be addressed within 6 months, and that noncompliance with the conditions would result in termination of the agreement.

However, the mission completed just one financial review after the program had been operating for 9 months. At that time, the mission found that the Center had not fully implemented the conditions in the award. For example, while the Center had upgraded its accounting system, the new system generated financial reports in a format that could be easily changed or manipulated. Similarly, while the Center had developed policies and manuals for key areas as required, the mission's review found problems with those related to personnel, procurement, and travel. Although the Center did not comply with the conditions added to the agreement, the mission did not enforce the termination clause for noncompliance. The mission concluded that the Center should retain its high-risk status until all recommendations and specific conditions were closed.

Mission officials said they followed up through weekly meetings and phone calls but did not perform another financial review. Many of the problems identified during the review remained at the time of the audit, 17 months into the award. This inadequate monitoring and follow-up occurred because the mission was understaffed⁶ and did not have a formal, detailed monitoring plan. Additionally, the expectation that the Center would complete the specific conditions just 6 months after signing the agreement seemed too ambitious. The mission believed that the award could serve as the plan, but not all the conditions made it into the award.

By not monitoring the implementation of the specific conditions in the award, the mission will not know whether the local NGO's financial and managerial capacity has improved, and cannot ensure the proper accountability for funds.

Recommendation 3. *We recommend that USAID/Paraguay develop a formal plan for facilitating and monitoring progress by Centro de Estudios Ambientales y Sociales on specific conditions to improve the program's financial and administrative control environment, or terminate the agreement with Centro de Estudios Ambientales y Sociales.*

⁶ The mission had been scheduled to close, and staff were reduced in preparation for that. Then the mission decided to emphasize local solutions, and remained open.

Implementer Had Weak Controls in Some Areas

According to USAID's NUPAS Guidelines, local organizations seeking USAID awards must have sufficient financial and managerial capacity to manage USAID funds. Having that capacity means being able to comply with standard provisions⁷—that the recipient “determine the most economical and practical means by which to accomplish program objectives,” “avoid conflicts of interest, including bias and unfair competitive advantage,” enforce competition, and determine the reasonableness of costs.

The preaward survey done by USAID/Paraguay concluded that the Center's financial and administrative capacity was inadequate to manage USAID funds. The survey noted that the Center was a small local NGO accustomed to managing a \$250,000 budget per year and that it would not be able to handle \$5 million per year, the expected annual increase from the award. Additionally, the preaward survey concluded that the Center would require a great deal of monitoring and coaching from USAID/Paraguay's financial and technical offices. The survey therefore recommended that the local NGO hire a subcontractor to help with management.

In response, the Center hired Management Systems International (MSI), a U.S. organization with experience implementing USAID awards, to provide (1) program management to build the capacity of its team and manage the program effectively, efficiently, and based on USAID and U.S. Government regulations and (2) expert technical assistance for the three components of the program. MSI's subcontract to perform these services was for \$3.6 million.

Despite the subcontract with MSI, USAID/Paraguay's first financial review revealed that the Center still lacked the administrative capacity to manage USAID funds. The financial review identified numerous problems, such as an inadequate accounting system, manuals needing further revision, unenforced internal controls, and noncompetitive procurements. In particular, the financial review identified \$574,000 in questioned costs related to procurement, noting the “lack of evidence of a competitive process” in 13 of 16 transactions tested. While the mission obtained an explanation for the questioned costs from the Center, the mission did not require the Center to adopt improved internal controls to prevent problems from recurring.

Our audit, conducted 6 months after the mission's financial review, found that the Center continued to operate with weak financial controls related to competition, conflicts of interest, and payroll:

Lack of Competition for Procurement Actions. The standard provisions state that procurements must ensure fair and unbiased competition. However, audit tests of a sample of 16 out of 92 procurements for consulting services (17 percent) totaling \$406,910 out of \$1,822,840 (22 percent) disclosed deficiencies with the competitive process. None of the 16 procurement actions was subject to open competition: 12 were sole-source procurements, and 4 were by invitation only. Only 1 of the 16 procurement actions was advertised openly, but only on the Center's Web site and only for a short time. For 2 of the 16 transactions, the rates the Center paid exceeded the market value documented in the files the Center maintained, and it could not provide justification.

⁷ A Mandatory Reference to ADS 303, “Standard Provisions for Non-U.S. Nongovernmental Organizations,” Section RAA4, “Indirect Costs—Charged as a Fixed Amount (Nonprofit) (June 2012).”

Conflicts of Interest. According to the standard provisions, recipients “must avoid conflicts of interest, including bias and unfair competitive advantage.” Recipients of 11 of the 16 tested transactions were individuals who had previously helped the Center prepare its winning proposal for USAID-funding. For one of the transactions, the Center selected a consulting firm partially owned by the Democracy and Governance Program’s chief of party. Furthermore, the Center was sharing the program’s USAID-funded office space with the consulting firm owned by the chief of party but not charging it rent. This arrangement, though approved by the agreement officer’s representative, appears to violate the requirement to avoid conflicts of interest. Although the Center indicated it had reduced the consulting firm’s rates by the cost of rent, the subcontract showed no evidence of this reduction.

Weak Payroll Controls. The Code of Federal Regulations (2 CFR 200.430 (i)(1)(vii)) states:

Charges to Federal awards for salaries and wages must be based on records that accurately reflect the work performed. These records must . . . [s]upport the distribution of the employee’s salary or wages among specific activities or cost objectives if the employee works on . . . a Federal award and non-Federal award.

Contrary to this guidance, the Center was not tracking the hours of one employee partly dedicated to the program. The president of the Center charged 75 percent of her time to the program but did not track the work done for the program as required.

This problem occurred because USAID/Paraguay did not provide the Center the level of monitoring and coaching that the preaward survey prescribed to ensure proper accountability for funds. In addition, after bringing in MSI, USAID/Paraguay did not provide appropriate oversight to ensure that it was working effectively with the Center to correct identified problems. For example, the financial review conducted by USAID found that the policy and procedures manual that MSI developed for the Center did not focus on the Center’s institutional requirements and organizational needs. The review also concluded that the Center was not following all internal control steps outlined in the manual, and that Center staff needed additional training. Finally, MSI had high staff turnover, which limited the effectiveness of the capacity-building effort; for example, three times during the first year MSI headquarters replaced the financial and administrative specialists assigned to the Center.

Given the results of the mission’s financial review, MSI and the Center agreed to modify MSI’s responsibilities, which had previously been limited to financial and administrative control. MSI’s new role is more of an all-purpose adviser, providing technical assistance in any program area, and the Center relies on a new internal specialist for financial and administrative support. However, the Center had not modified the subagreement or budget to reflect this change.

This weak financial and managerial environment has led to \$406,910 in ineligible questioned costs for procurement actions by the Center and in a \$3.6 million subaward that is not being used as intended. Unless these weaknesses are corrected, the program remains at risk of using taxpayer funds inefficiently, ineffectively, and contrary to guidelines.

Therefore, we make the following recommendations.

Recommendation 4. We recommend that USAID/Paraguay instruct Centro de Estudios Ambientales y Sociales in writing to revise its procurement practices to meet requirements for competition, including proper advertising and unbiased selection of vendors.

Recommendation 5. We recommend that USAID/Paraguay determine the allowability of \$406,910 in ineligible questioned costs related to the lack of competitive bidding and recover from Centro de Estudios Ambientales y Sociales the amount determined to be unallowable.

Recommendation 6. We recommend that USAID/Paraguay, in coordination with Centro de Estudios Ambientales y Sociales, mitigate the impact of the conflict of interest, calculate the fair value of office space funded by USAID for the Democracy and Governance Program that the subcontracted consulting firm occupied rent-free, have the agreement officer determine the allowability of the calculated amount, and recover from Centro de Estudios Ambientales y Sociales any amount determined to be unallowable.

Recommendation 7. We recommend that USAID/Paraguay work with Centro de Estudios Ambientales y Sociales to revise its payroll process to track payroll hours for employees not fully dedicated to the program.

Recommendation 8. We recommend that USAID/Paraguay, in coordination with Centro de Estudios Ambientales y Sociales, review the subaward between Management Systems International and Centro de Estudios Ambientales y Sociales, document and calculate the costs of any subaward requirements that Management Systems International did not meet and have the agreement officer determine the allowability of the calculated amount, and recover from Centro de Estudios Ambientales y Sociales any amount determined to be unallowable.

Recommendation 9. We recommend that USAID/Paraguay develop a formal plan for monitoring and supporting Centro de Estudios Ambientales y Sociales that provides appropriate oversight through coaching and regular financial reviews to ensure proper accountability for funds provided to the organization.

Implementer's Hiring Practices Did Not Comply With USAID Guidance

USAID's standard provisions,⁸ which implement 2 CFR 200.459(b)(6), state that in determining whether the cost of using consultants is allowable, the implementer should evaluate "whether [a] service can be performed more economically by direct employment rather than contracting."

The Center did not follow this guidance. During its budget negotiations with USAID/Paraguay at the outset of the program, the Center identified numerous key positions, including the chief of party, monitoring and evaluation specialist, gender specialist, contract specialist, and information technology specialist, as direct labor. However, the Center filled all of these positions with consultants instead of direct-hire employees and in many cases paid consultants much more than the salaries proposed in the budget.⁹ The following table shows the difference between the direct labor rates proposed by the Center and the consultant rates actually paid.

⁸ According to ADS 303, parts of 2 CFR 200 apply indirectly through ADS 303mab.

⁹ Although the chief of party was converted to an employee in August 2014, the other positions were still held by consultants.

Consulting Positions Exceeding USAID-Approved Budget Amounts (Audited)

Position	Daily Rate Agreed per Budget (\$)	Daily Rate Paid (\$)	Amount Over Budget (\$)
Gender specialist	70	207	137
Contract specialist	100	119	19
Information technology specialist*	180	213	33
Monitoring and evaluation specialist	70	75	5

* USAID approved the job positions listed for employees paid at USAID-approved rates, except for the information technology specialist, which the mission approved as a consultant.

Furthermore, the Center may have violated Paraguayan labor law. According to Law 213, employees work under the direction of an employer and are entitled to benefits including social security. Consultants, on the other hand, normally work under their own direction with their own resources to produce specified deliverables and are not entitled to the same benefits as employees. The Center’s consultants appeared to meet the definition of employees. For example, the Center managers directed the consultants in their work, and the consultants maintained a regular work schedule at the Center’s program office. However, because the Center hired these employees as consultants, they did not receive benefits, and the Center did not pay employee taxes or social security for them.

These problems occurred for two reasons:

- Center officials said they were not aware of these requirements. The standard provisions document was updated after the award. The Center, being a new implementer, did not know the standard provisions, and MSI did not provide input regarding these hires.
- USAID/Paraguay did not closely monitor the Center’s financial and managerial decisions or provide appropriate training and oversight. Furthermore, the mission had not modified the agreement to include updated standard provisions.

As a result of these hiring practices, program funds were not being used in the most efficient and effective way. These practices led to \$406,910 in ineligible questioned costs for procurement actions by the Center (addressed in the previous finding) and may have violated local labor law.

Therefore, we make the following recommendations.

Recommendation 10. *We recommend that USAID/Paraguay instruct Centro de Estudios Ambientales y Sociales, in writing, to pay employees at the rates in the award budget.*

Recommendation 11. *We recommend that USAID/Paraguay work with Centro de Estudios Ambientales y Sociales to determine and document the most cost-effective method for staffing program positions that complies with local labor law.*

Recommendation 12. *We recommend that USAID/Paraguay have the agreement officer amend the Democracy and Governance Program agreement to include the latest mandatory standard provisions for non-U.S. nongovernmental organizations as noted in the mandatory reference to Automated Directives System 303, “Standard Provisions for Non-U.S. Nongovernmental Organizations.”*

Mission Did Not Structure the Award to Promote Sustainability

USAID expects project outcomes to be sustainable, meaning that they “evolve under their own momentum or actions, without continued donor intervention” (ADS 201.3.16.3 (c)). To that end, ADS requires missions to do a sustainability analysis of every project or program during the planning stage. The analysis should include

a review of the financial implications of project sustainability. For any organization to be sustained following completion of the project . . . a recurrent cost analysis must be undertaken that estimates the costs . . . of continuing expected functions at the end of the project and estimated sources of revenue.

Although USAID/Paraguay did a sustainability analysis for the Democracy and Governance Program, its analysis did not adequately consider the Center’s costs to continue or its estimated sources of revenue. The cooperative agreement USAID/Paraguay awarded to the Center does not reimburse it for indirect costs, and it imposes burdensome cost-sharing requirements.

According to the standard provisions, indirect costs (overhead) charged as a fixed amount of direct costs are allowable for local NGOs that have not negotiated an indirect cost rate. This guidance took effect June 18, 2012,¹⁰ making it applicable to the Center. Yet USAID/Paraguay did not reimburse the Center for indirect costs. Reimbursement for these costs, along with coverage of operating expenses, would improve the Center’s chances of sustainability. The Center could pay staff to write grant proposals, bid on contracts, and do other fund raising to diversify revenue sources. At present, the Center receives all its funds from USAID/Paraguay.

ADS Chapter 303, which defines cost sharing as “resources a recipient contributes to the total cost of an agreement” (ADS 303.3.10), advises that “USAID should use cost sharing after considering whether it is appropriate for the recipient organization in the particular circumstances” (ADS 303.3.10.1). Yet USAID/Paraguay seems not to have considered the Center’s circumstances, because it required the Center to contribute 15 percent of the total award, or \$3.7 million. This cost-share requirement burdens the Center, which has (1) poor financial and managerial capacity, (2) only one funding source, (3) no coverage of its indirect costs, and (4) no experience with cost sharing. As of June 30, 2014, the Center had contributed only \$47,589, or 1.3 percent of the total budget.

The mission did not reimburse the Center for indirect costs because USAID/Paraguay officials were unaware of the new indirect cost rate policies at the time the award was signed; the mission had relied on a cooperative agreement template for local NGO awards that was out-of-date (prepared before June 2012) and did not include indirect costs. As for the cost share, mission officials believed that a 15 percent contribution was appropriate because other local

¹⁰ A Mandatory Reference to ADS 303, “Standard Provisions for Non-U.S. Nongovernmental Organizations,” Section RAA4., “Indirect Costs – Charged as a Fixed Amount (Nonprofit), June 2012.

NGOs had managed it on their awards. However, those awards were much smaller than the \$24.4 million award with the Center and required a much smaller total contribution.

Local NGOs need to have diverse funding sources and not be saddled with burdensome cost-sharing requirements if they are to survive past the life of this award. Therefore, we make the following recommendations.

Recommendation 13. *We recommend that USAID/Paraguay have the agreement officer amend the award for the Democracy and Governance Program to cover the indirect costs of the Centro de Estudios Ambientales y Sociales or require Centro de Estudios Ambientales y Sociales to seek new funding sources so that costs associated with doing so would become direct costs.*

Recommendation 14. *We recommend that USAID/Paraguay evaluate and document whether to adjust the cost-share percentage for the Centro de Estudios Ambientales y Sociales in light of its circumstances, and have the agreement officer modify the award as necessary.*

EVALUATION OF MANAGEMENT COMMENTS

The mission agreed with 10 of 14 recommendations. We acknowledge management decisions on all 14 recommendations and final action on Recommendations 1 through 4, and 7 through 14. Our evaluation of management comments follows.

Recommendation 1. The mission disagreed with the recommendation to conduct an analysis of the Center to address the areas of a NUPAS not previously covered. Mission officials feel that the preaward survey they originally conducted met the objectives of NUPAS. They also believe that since the program is over 2 years old, there is no additional benefit to conducting a NUPAS of the Center.

While we acknowledge the mission's management decision and final action, we disagree with it. As explained in our finding on page 6, the preaward survey conducted by the mission of the Center was not a NUPAS, nor did it meet the objectives of one. Rather it was the preaward survey used to evaluate risks of U.S.-based organizations. We reviewed a gap analysis that the mission believed showed that the preaward survey met the objectives of a NUPAS, but we did not find it sufficient.

While the mission may not see any benefit from conducting a NUPAS of the Center at this point in the program, we do. USAID/Paraguay asserts that it is a pilot mission for Local Solutions, yet it has never done a NUPAS. We feel it is important for mission staff to gain experience with this process.

Recommendation 2. The mission agreed with this recommendation and reviewed the existing specific conditions against findings from both the recipient-contracted audit and USAID/Paraguay's financial reviews. Mission officials determined that no new conditions were needed and pledged to work with the Center to lift the remaining conditions. We acknowledge the mission's management decision and final action.

Recommendation 3. The mission agreed with this recommendation and developed a plan for monitoring and facilitating progress on specific conditions in the award. The plan includes enhanced financial and administrative oversight, as well as technical assistance to improve the Center's internal control environment. We acknowledge the mission's management decision and final action.

Recommendation 4. The mission agreed with this recommendation and instructed the Center to revise its internal control manuals. We acknowledge the mission's management decision and final action.

Recommendation 5. The mission agreed with this recommendation and reviewed the questioned costs. Officials determined that \$8,064.61 paid to a member of the Center's board for consulting services was unallowable and unsupported, and issued a bill of collection. The mission anticipated receiving the refund by January 28, 2016. We acknowledge the mission's management decision.

Recommendation 6. The mission agreed with this recommendation and had the subcontracted consulting firm vacate the Center's office space on June 1, 2015. The mission issued a bill of collection for \$2,258.28 to the Center for this unallowed cost and anticipated receiving this refund by January 28, 2016. We acknowledge the mission's management decision.

Recommendation 7. The mission agreed with this recommendation and worked with the Center to revise its payroll process. The Center now has a payroll tracking procedure that requires supporting payroll documentation for staff not fully dedicated to the program. We acknowledge the mission's management decision and final action.

Recommendation 8. The mission agreed with this recommendation and reviewed the subaward between the Center and MSI. Officials determined that the costs related to products and services received thus far were allowable. Accordingly, we acknowledge the mission's management decision and final action on this recommendation. The mission also determined that the current arrangement presents a potential for conflict of interest. Thus, the mission will adjust the subaward and issue a new award for technical assistance; this new award will be managed directly by USAID/Paraguay.

Recommendation 9. The mission agreed and developed a plan for monitoring and supporting the Center's internal control. We acknowledge the mission's management decision and final action.

Recommendation 10. The mission disagreed with instructing the Center to pay employees the rates agreed to in the award budget, noting that these rates were just estimates. However, the mission did instruct the Center that it must justify any variance in salary rates from the negotiated budgeted amounts and obtain approval from the mission. We acknowledge the mission's management decision and final action.

Recommendation 11. The mission agreed with this recommendation and instructed the Center to implement it. The Center worked with a local labor law attorney to revise its human resources manual, bringing its practices into compliance. We acknowledge the mission's management decision and final action.

Recommendation 12. The mission agreed with this recommendation and included the July 22, 2015, standard mandatory provisions for non-U.S. nongovernmental organizations in Modification 7, signed on September 21, 2015. We acknowledge the mission's management decision and final action.

Recommendation 13. The mission disagreed with amending the award to cover indirect costs or allow the Center to seek new funding sources as a valid activity. However, the mission amended the award to allow the Center to include activities aimed at identifying new funding and business opportunities to ensure the financial sustainability of the organization. We acknowledge the mission's management decision and final action.

Recommendation 14. The mission disagreed, saying the cost-share percentage did not need to be adjusted since the Center's September 2015 financial report shows it met 40 percent of its cost-share requirement with 3 years to go. We acknowledge the mission's management decision and final action.

SCOPE AND METHODOLOGY

Scope

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

The purpose of this audit was to determine whether USAID/Paraguay's Democracy and Governance Program was achieving its main goal of strengthening the internal management and governance systems in select public institutions.

On October 1, 2013, USAID/Paraguay signed a \$24.4 million cooperative agreement with a local NGO, Centro de Estudios Ambientales y Sociales, to implement a 5-year program. As of December 31, 2014, USAID/Paraguay had obligated \$7.6 million and disbursed \$5 million for the program. The latter represents the amount tested.

In planning and performing the audit, the audit team assessed significant management controls the mission used to manage the project and provided adequate oversight. These included quarterly and annual performance reports, performance management plans, and annual work plans. In addition, the auditors examined the mission's portfolio review notes and its fiscal year 2014 self-assessment of management controls, which is required by the Federal Managers' Financial Integrity Act, to determine whether the assessment cited any relevant weaknesses.

We also reviewed award documents; tested reporting systems; conducted site visits; and interviewed USAID/Paraguay staff, Paraguayan Government officials, Center staff, and beneficiaries. We reviewed reported results for accuracy and made note of any potential issues identified. We conducted fieldwork in Paraguay from February 9 through 27, 2015. We visited 10 of the 14 government institutions the program is working with and reviewed technical assistance being provided to improve their institutional capacity, accountability, anticorruption efforts; and legal and policy frameworks for effective governance.

Methodology

To answer the audit objective, we reviewed program documentation and conducted interviews and site visits. We evaluated the mission's management and oversight of the program, the performance of the Center, and the effectiveness of its activities. We met with officials from USAID/Paraguay and the program's partners. We also interviewed beneficiaries and Paraguayan Government officials.

Through these interviews and the review of the program's documentation, the audit team obtained an understanding of (1) the program's goals, (2) how USAID established performance indicators, targets, and baseline data to measure progress, (3) how the mission verified the quality of the data the contractor reported, (4) how the mission monitored program activities, and (5) whether the mission was aware of any allegations of fraud or other potential illegal acts or noncompliance with laws, regulations, or agreement terms.

In addition, we performed the following audit tests:

- Reviewed and tested all the work plan activities for their progress and results to determine their reported accuracy.
- Reviewed and tested procedures the mission established to monitor and confirm the accuracy of the program's reported results.
- Documented and tested compliance with award requirements for sustainability, gender analysis, stopping human trafficking, and branding and marking.

To determine the progress made and answer the audit objective, we relied on computer-processed data contained in quarterly and annual progress reports prepared by the implementing partners. We assessed the reliability of this data by judgmentally selecting accomplishments, focusing on those that contributed most to project goals, and taking into account the geographic location and accessibility of activity sites we could visit to check source documents for accomplishments. We then evaluated the data in these reports and verified them against supporting documentation. In addition, we conducted interviews to gather support to answer the audit objective. These tests and interviews led us to conclude the data were sufficiently reliable to be used in answering the audit objective.

To verify the status of activities completed, we examined documentation maintained at the contractor's office in Asuncion. In addition, we judgmentally selected 10 of the 14 public institutions the program is working with and reviewed the technical assistance provided to improve their institutional capacity, accountability and anticorruption efforts, and legal and policy frameworks. We based our sample selection on factors including availability of government personnel and diversity of institutions.

The public institutions we contacted were the Ministry of Education, Ministry of Civil Service, Ministry of Information Technologies and Communication Technologies, Auditor General of the Executive Branch, Controller General, Public Procurement Agency, Ministry of Planning, Supreme Court, Anticorruption Secretariat, and Ministry of Health. We met with officials representing these ten to validate reported results to the extent possible.

Because the testing and site selections were based on judgmental samples, the results and conclusions related to the analysis are limited to the items and areas tested, and cannot be projected to all program data. We believe our substantive testing was sufficient to support the audit's findings.

MANAGEMENT COMMENTS



USAID | PARAGUAY
DEL PUEBLO DE LOS ESTADOS
UNIDOS DE AMÉRICA

December 17, 2015

TO: Jon Chasson, Regional Inspector General/San Salvador

FROM: Fernando Cossich, Mission Director, USAID/Paraguay /s/

SUBJECT: Comments on the Draft Report of the Audit of USAID/Paraguay's Democracy and Governance Program (Report No. 1-526-15-XXX-P)

Thank you for providing us with the opportunity to respond to the draft report on the Performance Audit of USAID/Paraguay's Democracy and Governance Program. We reviewed it carefully and offer the following comments:

This audit report is a clear reflection of the challenges and internal resistance USAID faces as we modify the way we do business, particularly with respect to strengthening and sustaining local systems. The performance audit report focuses on and amplifies risks taken by the Mission, pointing out important issues. Unfortunately, the report does not address whether our Program is strengthening the local system as a whole and is producing the desired development outcomes.

Viewed from a development outcome perspective, USAID/Paraguay's Democracy and Governance Program is an unqualified success. In a very short period of time, our local partner, the Centro de Estudios Ambientales y Sociales (CEAMSO), achieved dramatic, positive changes within Paraguay:

- **Access to Information Law.** Thanks to this award, Paraguay now has a viable anti-corruption strategy and an Access to Information Law through which citizens actively communicate with government officials and report corruption cases. Citizen oversight of government data, facilitated by web-based platforms developed under the Program, unearthed multiple cases of corruption. Because of these platforms, several high-profile congressmen lost their immunity and are under investigation. Moreover, as a result of disclosures made possible through this Program, the Comptroller General and his deputy resigned after initiation of impeachment procedures for allegations of corruption. Multiple cases of nepotism and graft were uncovered at the National University, and 53 employees of the Electoral Court have been formally charged on multiple corruption charges. None of these outcomes would have been possible without USAID's and CEAMSO's efforts.
- **Greater Transparency.** Through this award, CEAMSO established an on-line system to file asset and financial disclosure statements for all government officials and installed transparent and streamlined merit-based hiring procedures for civil servants.

- **Standardization of Internal Controls.** The standardized model for internal controls installed and implemented under this award in Executive Branch ministries and the Supreme Court have led to clear, uniform evaluation criteria, safeguarded public assets and reduced corruption.
- **Improved Public Procurement:** With CEAMSO's support, the National Procurement Agency implemented a web-based application that allows citizens to track and challenge the legality of the government's contract award process. All procurement related information is now available around the clock and free of charge, allowing bidders and citizens to track the status of any procurement action and file protests. The program is also developing a risk management system for contracts under the control of the Ministry of Public Works, minimizing corruption and fraud in large infrastructure projects. The Program synchronized the Ministry of Health's inventory system with the national procurement system so the Ministry could reduce re-supply times and track purchases and availability of medicines and medical supplies. These reforms have the potential to save millions of dollars in public funds and ensure the delivery of higher quality goods and services to the public.

Thanks to CEAMSO, the Program is achieving its primary goal of supporting the creation of a more prosperous, well governed democracy in Paraguay. The aforementioned results are just a small sampling of the Program's successes.

Through the procurement process, USAID/Paraguay came across an organization with sound technical capability and in-depth understanding of the local development challenges and interrelationships of local actors. CEAMSO's proposal showed its potential to make USAID's program a catalyzer for broad-based social change in Paraguay. Even though CEAMSO had the capacity to properly manage the funding levels it administered before the USAID award, the Mission's pre-award survey revealed that CEAMSO was a high risk organization based on several deficiencies, and that it needed to build its capacity to meet the considerable increase in funding levels and USAID requirements.

USAID/Paraguay anticipated and attempted to mitigate this risk through the adoption of several measures. We therefore disagree with the report's comment that by not using the standard Non-U.S. Organization Pre-Award Survey (NUPAS) format during the pre-award survey, the Mission put \$24.4 million at risk. The pre-award survey met NUPAS objectives and provided the Agreement Officer with sufficient information to determine the level of risk.

USAID/Paraguay's decision to award this cooperative agreement to CEAMSO was not made randomly; it was based on sound information provided by the pre-award survey. Having extensively and successfully worked with local partners in the past, we knew exactly what the challenges and critical issues would be as we moved forward. This is, without a doubt, the sort of calculated risk we as an Agency must take on if we truly strive to work with local partners and build local capacity. The special award conditions built into the award were designed to be broad enough to give our partner room to maneuver and move forward with implementation, while also giving USAID the needed flexibility to take corrective actions as required. Special award conditions included areas that needed to be addressed immediately, such as the development of institutional manuals, an upgrade of the accounting system, and the hiring of an internal auditor.

To mitigate the inherent risk of working with a local partner, CEAMSO's proposal included an innovative approach whereby it would issue a sub-award to a seasoned international

development firm, Management Systems International (MSI), to provide it with administrative, financial, and management support. In a further effort to mitigate risk, the Agreement Officer made the determination during award negotiations to include a permanent Resident Advisor position from MSI to work within CEAMSO during the first three years of implementation. The purpose of this position was to work with CEAMSO to comply with special award conditions, ensure compliance with USAID regulations, and provide technical assistance to strengthen CEAMSO's project management capacity.

The Mission also put in place a risk management plan that included the following:

- Workshops and coaching sessions provided by our technical and financial teams;
- An Organizational Capacity Assessment (OCA), carried out by CEAMSO, to identify institutional gaps that needed to be addressed;
- Financial reviews;
- Internal and external audits; and
- Weekly meetings with the technical and administrative teams to assess progress.

In addition to the above, USAID/Paraguay planned for and hired a Local Capacity Development Specialist to ensure that the organization is brought up to speed with USAID requirements and programmatic challenges, and to ensure the sustainability of the actions undertaken by the program. As we moved forward with implementation and prior to the RIG audit, the Mission's internal financial reviews identified critical issues and deficiencies. These issues and deficiencies were subsequently incorporated into the subject RIG audit findings, but they were already being addressed by the Mission at the time the audit took place.

Challenges are continuous when working with Local Solutions. Nevertheless, our experience shows that it is the most sustainable way of doing sound development work. USAID/Paraguay's experience in this arena demonstrates that Local Solutions have made USAID development efforts more effective, more enduring and less costly. This Mission has chosen to be at the forefront of the Agency's efforts in Local Solutions work, and through this approach we are achieving impressive results. Most recent examples of local organizations that we helped to become sustainable and key players in the local development environment include the Centro de Información y Recursos para el Desarrollo, Semillas para la Democracia, Fundación Saraki, and A Todo Pulmón. We believe that, with support from USAID, CEAMSO has the opportunity to be a similar success story.

Comments on recommendations:

***Recommendation 1.** We recommend that USAID/Paraguay complete an analysis of Centro de Estudios Ambientales y Sociales that meets the requirements for a Non-U.S. Organization Pre-award Survey, assessing areas not covered by the pre-award survey or this audit, which will also serve as a learning experience on how to conduct a Non-U.S. Organization Pre-award Survey.*

We do not concur with the recommendation.

The Mission conducted a thorough pre-award survey which met the NUPAS objectives described in ADS Chapter 303 and adequately served to provide the Agreement Officer with the necessary and sufficient information to determine the level of risk and design appropriate special award conditions. Our position is strongly supported by a gap analysis performed to identify any differences between each of the required elements of a NUPAS and those

assessed under our completed pre-award survey. This analysis concluded that no significant deviations existed, and that all evaluation elements of a NUPAS were satisfactorily covered by the Mission's evaluation team prior to the award.

The areas assessed during the pre-award survey included:

- Legal structure of the entity, including governance and control environment;
- Financial management and internal control systems, including a comprehensive revision of the partner's bank accounts, accounting system, financial statements, payments, segregation of duties protocol, financial records management, funding sources, financial reporting, audits, and financial management personnel experience;
- Procurement systems, including policies and procedures;
- Human resources systems;
- Project management; and
- Organizational Sustainability, where applicable.

The results of this analysis led to the Mission's overall determination of CEAMSO's level of risk prior to award.

The Mission believes that at this point in time, over two years into the program, no additional benefits will be obtained by conducting a NUPAS. As further described in ADS reference document 303sam, a NUPAS precedes an award and is used to inform the selection process. The Mission's pre-award assessment and resulting conclusion that CEAMSO was a high risk organization led the Mission to adopt several risk mitigating and capacity building measures before finalizing the award, thus safeguarding USAID's \$24.4 million investment. Additionally, since performing the original pre-award assessment, the Mission carried out numerous re-assessments and systems strengthening exercises in the form of interim financial reviews, a recent recipient contracted audit, and periodic spot checks.

Based on the above, we request closure of this recommendation.

Recommendation 2. *We recommend that USAID/Paraguay determine whether to add specific conditions to the award for the Democracy and Governance Program and whether to extend timelines for specific conditions, and have the agreement officer modify the award as necessary.*

We concur with the recommendation.

The Mission thoroughly reviewed existing special award conditions against findings from the recipient contracted audits and USAID/Paraguay's financial reviews. It determined that no new special award conditions were required, although the Mission continues to work with CEAMSO on lifting the remaining special conditions. CEAMSO satisfied the special condition related to contracting an internal auditor, therefore it has been lifted.

Based on the above, we request closure of this recommendation.

Recommendation 3. *We recommend that USAID/Paraguay develop a formal plan for monitoring and facilitating progress by Centro de Estudios Ambientales y Sociales on any specific conditions to improve the program's financial and administrative control environment, or terminate the agreement with Centro de Estudios Ambientales y Sociales.*

We concur with the recommendation.

The Mission developed an updated plan for monitoring and facilitating progress on special award conditions. This includes enhanced financial and administrative oversight, as well as support from the Mission through direct technical assistance.

The Mission, in coordination with CEAMSO's Chief of Party, established and implemented a monitoring plan for identifying and correcting significant financial and administrative internal control weaknesses that could adversely affect CEAMSO's ability to meet its program objectives. An assessment by a consulting firm identified the following systems in need of improvement:

- Consulting services;
- Acquisitions;
- Travel and per-diem;
- Human resources;
- Costs allocation;
- Payments to suppliers; and
- Sub-grants and cost sharing.

For each system identified, CEAMSO developed a Risk Matrix with a corresponding Risk Mitigation Plan and assigned corrective actions. Periodic monitoring by the Mission will provide assurances that identified improvements have been addressed.

The Mission's monitoring plan will enable CEAMSO to improve its internal control environment. This plan utilizes various procedures to monitor indicators and control techniques in order to ensure progress towards set targets. It places an increased emphasis on monitoring the work plan of CEAMSO's internal auditor, spot checks, and interim financial reviews. Implementing timely corrective actions is a key component of the Mission's oversight plan.

Based on the above, we request closure of this recommendation.

Recommendation 4. We recommend that USAID/Paraguay instruct Centro de Estudios Ambientales y Sociales in writing to revise its procurement practices to meet requirements for competition, including proper advertising and unbiased selection of vendors.

We concur with the recommendation.

The Mission identified this deficiency during the July 2014 financial review of CEAMSO, prior to the RIG audit. Subsequently, the Mission instructed CEAMSO in writing, to revise its procurement manuals.

Based on the above, we request closure of this recommendation.

Recommendation 5. We recommend that USAID/Paraguay determine the allowability of \$406,910 in ineligible questioned costs related to the lack of competitive bidding and recover from Centro de Estudios Ambientales y Sociales the amount determined to be unallowable.

We concur with the recommendation.

The Mission conducted a thorough and detailed evaluation of the \$406,910 in questioned costs. For each questioned cost, CEAMSO provided additional supporting documentation that justified each procurement. CEAMSO properly justified instances where there was a lack of competition. The Mission determined that of these instances the amount of \$8,064.61 claimed for consulting services provided by a member of CEAMSO's board is unallowable and unsupported. Therefore, USAID issued a Bill of Collection to CEAMSO requesting the refund of these costs. (See Annex 1.)

Based on its review, the Mission determined that the remaining balance of \$398,845.25 is allowable.

Recommendation 6. *We recommend that USAID/Paraguay, in coordination with Centro de Estudios Ambientales y Sociales, mitigate the impact of the conflict of interest, calculate the fair value of office space funded by USAID for the Democracy and Governance Program that the subcontracted consulting firm occupied rent-free, have the agreement officer determine the allowability of the calculated amount, and recover from Centro de Estudios Ambientales y Sociales any amount determined to be unallowable.*

We concur with the recommendation.

The subcontracted consulting firm vacated the CEAMSO office space on June 1, 2015. The Mission issued a Bill of Collection in the amount of \$2,258.28 to CEAMSO requesting a refund for this disallowed cost. (See Annex 2.)

Recommendation 7. *We recommend that USAID/Paraguay work with Centro de Estudios Ambientales y Sociales to revise its payroll process to track payroll hours for employees not fully dedicated to the program.*

We concur with this recommendation.

The only permanent staff not fully dedicated to the program is CEAMSO's Executive Director. CEAMSO has now included a payroll tracking procedure that requires supporting payroll documentation for staff not fully dedicated. The Mission will continue to monitor and assess the effectiveness of this procedure during its monitoring of the program.

Based on the above, we request closure of this recommendation.

Recommendation 8. *We recommend that USAID/Paraguay, in coordination with Centro de Estudios Ambientales y Sociales, review the sub-award between Management Systems International and Centro de Estudios Ambientales y Sociales, document and calculate the costs of the sub-award requirements that Management Systems International did not meet and have the agreement officer determine the allowability of the calculated amount, and recover from Centro de Estudios Ambientales y Sociales any amount determined to be unallowable.*

We concur with this recommendation.

USAID/Paraguay and CEAMSO, under the Agreement Officer's leadership, reviewed the sub-agreement with MSI and determined that the corresponding products and services were received. Thus, payments under this sub-agreement were deemed allowable.

Furthermore, for more cost-effective and efficient management of the Program, the Mission decided to de-scope the portion of the Technical Assistance (TA) component contained in CEAMSO's technical and cost application that allows CEAMSO to directly manage the sub-agreement with its TA provider. The Mission decided that this reporting structure presents a potential conflict of interest, as the TA provider is employed by the prime, CEAMSO, but often times needs to make suggestions that could be critical of the prime. To mitigate this risk and remove any potential conflict, the Mission intends to directly issue an award to a TA provider that will work with CEAMSO, but report to USAID/Paraguay. This approach will provide greater flexibility to the Mission and result in concrete recommendations that will strengthen CEAMSO.

Based on the above, we request closure of this recommendation.

Recommendation 9. We recommend that USAID/Paraguay develop a formal plan for monitoring and supporting Centro de Estudios Ambientales y Sociales that provides appropriate oversight through coaching and regular financial reviews to ensure proper accountability for funds provided to the organization.

We concur with the recommendation.

Please refer to our response to Recommendation Number 3 and 8 above. Specifically, the revised monitoring and reporting plan for improved internal controls will ensure proper accountability of funds by providing reasonable assurance that noncompliance with applicable policies and regulations will be prevented or detected.

Based on the above, we request closure of this recommendation.

Recommendation 10. We recommend that USAID/Paraguay instruct Centro de Estudios Ambientales y Sociales, in writing, to pay employees at the rates in the award budget.

We do not concur with the recommendation.

The amounts stated in the cost application are estimates. The market value of the position to be filled determines the final cost.

Nevertheless, moving forward, the Agreement Officer instructed CEAMSO in writing that whenever the resultant employee salary rate is above the negotiated budgeted amount, CEAMSO must justify the variance in salary costs in writing and obtain prior approval from the Agreement Officer.

Based on the above, we request closure of this recommendation.

Recommendation 11. We recommend that USAID/Paraguay work with Centro de Estudios Ambientales y Sociales to determine and document the most cost-effective method for staffing program positions that complies with local labor laws.

We concur with the recommendation.

The Mission communicated this concern to CEAMSO. In response, CEAMSO presented its revised Human Resources Manual and contracted a local labor law attorney to assist in its compliance with Paraguayan labor law. The process now in place includes clearly defined

parameters to define the contractual relationships CEAMSO will pursue with its staff.

Based on the above, we request closure of this recommendation.

Recommendation 12. *We recommend that USAID/Paraguay have the agreement officer amend the Democracy and Governance Program agreement to include the latest mandatory standard provisions for non-U.S. nongovernmental organizations as noted in the mandatory reference to Automated Directives System 303, "Standard Provisions for Non-U.S. Nongovernmental Organizations."*

We concur with the recommendation.

Standard mandatory provisions for non-U.S. nongovernmental organizations dated July 22, 2015, were included in Modification Number Seven signed on September 21, 2015.

Based on the above, we request closure of this recommendation.

Recommendation 13. *We recommend that USAID/Paraguay have the agreement officer amend the award for the Democracy and Governance Program to cover the indirect costs of the Centro de Estudios Ambientales y Sociales or require Centro de Estudios Ambientales y Sociales to seek new funding sources so that costs associated with doing so would become direct costs.*

We do not concur with the recommendation.

When the Cooperative Agreement was awarded in September 2013, CEAMSO did not have a Negotiated Indirect Cost Rate Agreement (NICRA). Therefore, all costs included in the agreement were direct costs. The Standard Provision which allows local recipients to include a "De Minimis" 10 percent, under 2 CFR 200-414(f), did not come into effect until December 2014, fourteen months after the agreement was awarded.

CEAMSO's agreement was revised under Modification Number Six to include a new component specially tailored to address sustainability issues. Component Four allows CEAMSO to identify and seek new funding and business opportunities to ensure the financial sustainability of the organization.

Based on the above, we request closure of this recommendation.

Recommendation 14. *We recommend that USAID/Paraguay evaluate and document whether to adjust the cost-share percentage for the Centro de Estudios Ambientales y Sociales in light of its circumstances, and have the agreement officer modify the award as necessary.*

We do not concur with the recommendation.

The Mission considers that the applicable cost-share percentage is realistic. Per CEAMSO's latest financial report, as of September 2015 and two years into this five year agreement, CEAMSO reported a total of \$1,472,503 in cost-share contributions. This amount represents 40 percent of the total cost-share required under the Agreement.

Based on the above, we request closure of this recommendation.

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