USAID
FROM THE AMERICAN PEOPLE

Office of Inspector General

December 29, 2006

MEMORANDUM

To: USAID/Ghana Director, Sharon Cromer

From: Acting RIG/Dakar, Abdoulaye Gueye

Subject: Close-out Audit of the USAID/Ghana Resources Managed by MOLTENO, under Cooperative Agreement No. 641-A-00-04-00048 for the Period December 17, 2003 to September 30, 2004 (Audit Report No. 7-641-07-001-D)

Attached for your information and use is the Defense Contract Audit Agency's (DCAA) audit report No. 2191-2006U17900003. This report presents the result of a financial audit of the USAID/Ghana resources managed by MOLTENO, under Cooperative Agreement # 641-A-00-04-00048 for the period December 17, 2003 to September 30, 2004. DCAA's European branch office performed the audit in accordance with U.S. Government Auditing Standards.

MOLTENO is a non-governmental, not-for-profit organization incorporated in South Africa. The primary purpose of the organization is to facilitate the acquisition of fundamental reading and writing skills through a literacy instructional methodology (BTL) which is based on the Language Experience Approach.

On December 17, 2003, the Ghana Mission of the United States Agency for International Development (USAID/Ghana) approved a $447,967 Cooperative Agreement to MOLTENO, with a completion date of September 30, 2004. The purpose of the agreement was to support the provision of technical assistance to the Ghana Education Service to conduct a pilot of the BTL instructional approach in 50 selected primary schools in four districts of Ghana. In September 2004, the agreement was modified to increase the total estimated amount to $623,553 for the purchase of additional BTL materials for a roll-out of the pilot to 107 additional schools.

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

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During the period December 17, 2003 to September 30, 2004, MOLTENO reported total costs incurred of $481,842 in USAID funds.

The objectives of the audit were to: 1) express an opinion on the fund accountability statement; 2) evaluate and obtain a sufficient understanding of MOLTENO's internal control, assess control risk, and identify reportable conditions; 3) perform tests to determine whether MOLTENO complied with agreement terms including cost sharing and applicable laws and regulations related to USAID/Ghana - funded programs; 4) determine whether cost-sharing contributions were provided and accounted for by MOLTENO in accordance with the terms of the agreements; express an opinion on MOLTENO's general purpose financial statements; 5) perform an audit of overhead costs to determine the actual rate that should have been used to charge overhead costs; and 6) determine if MOLTENO has taken adequate corrective action on prior audit report recommendations.

Results of the DCAA Audit

Fund Accountability Statement

DCAA found that except for questioned costs of $119,487, MOLTENO's fund accountability statements for the period December 17, 2003 through September 30, 2004 presented fairly, in all material respects, costs financed by USAID/Ghana, in conformity with generally accepted accounting principles. The questioned costs were comprised of $84,984 in ineligible costs, and $34,503 in unsupported costs. The ineligible costs represent unallowable employee allowances, travel and per diem expenses incurred in excess of allowable per diem rates, and Value Added Taxes (VAT) paid. The unsupported costs represent labor costs that could not be supported due to lack of an adequate timekeeping system and travel costs that could not be supported due to MOLTENO's failure to maintain adequate supporting documentation for costs incurred under the agreement.

Cost Sharing

In reviewing MOLTENO's cost sharing schedule, DCAA found that MOLTENO was not able to provide adequate supporting documentation for its total claimed cost sharing contribution. As a result, DCAA determined cost sharing questioned costs in the amount of $57,413. The questioned costs were comprised of $20,542 in ineligible costs, and $36,871 in unsupported costs. Exhibit B (pages 21-24) of the attached draft report gives further details on these questioned costs.

Internal Control Structure

DCAA noted four reportable conditions regarding MOLTENO's internal control structure, including inadequate timekeeping system, inadequate segregation of duties in finance and administration departments, inadequate training of financial department employees, and failure to identify and segregate unallowable costs. These conditions are further developed in Exhibit C (page 25-27) of the attached draft report.

Compliance with Grant Agreement Terms and Applicable Laws and Regulations

In testing MOLTENO's compliance with grant agreement terms and applicable laws and regulations, DCAA found seven instances of noncompliance related to MOLTENO's failure to: establish an adequate timekeeping system; exclude unallowable salary allowances; comply with travel policies and procedures regarding per diem; comply with procurement policies and procedures to ensure open and free competition; identify and segregate unallowable costs; retain adequate supporting documentation for costs incurred on the cooperative agreement; and adequately document and comply with cost sharing requirements. In DCAA's report on the fund accountability statement, the impact of these instances of non-compliance is considered to be ineligible or unsupported costs. These noncompliance conditions are further described in Exhibit D (pages 28-34) of the attached draft report.

Follow-up on Prior Audit Findings

DCAA found that MOLTENO took corrective actions to adequately address the conditions identified in recommendations made during two prior financial audits. The results of this follow-up review are detailed in Exhibit E (page 35) of the attached draft report.

In its comments on the draft report, MOLTENO agreed on $5,889 of the questioned costs, arguing that they are not subject to OMB requirements governing indirect costs and that additional documentation supporting some of the questioned costs have been located. DCAA maintained their position on the basis that MOLTENO did not adequately respond to their findings. Regarding the cost sharing contributions, MOLTENO did not specifically address the questioned cost sharing amounts by element. Rather, they stated that additional eligible cost sharing amounts have been identified, and that the analysis is available for review. Regarding internal controls and compliance, MOLTENO agreed with DCAA's findings and recommendations and stated that it would take corrective actions.

Based on our review of the DCAA report, we are making the following recommendations for inclusion in USAID's Consolidated Audit Tracking System.

> *Recommendation No. 1: We recommend that USAID/Ghana: 1) make a management decision with regard to the questioned costs of $119,487; and 2) recover from MOLTENO the amounts determined to be unallowable.*

Recommendation No. 1 is considered to be without a management decision until USAID/Ghana advises RIG/Dakar of its official management decision to sustain or not sustain the questioned costs. For the amounts determined to be sustained, USAID/Ghana is required to take final action by recovering such amount and forwarding all documentation supporting its action to the Audit Performance and Compliance Division within the Management Bureau's Office of the Chief Financial Officer (M/CFO/APC).

> *Recommendation No. 2: We recommend that USAID/Ghana: 1) make a management decision with regard to the questioned costs of $57,413 in cost sharing; and 2) recover the amounts determined to be MOLTENO's cost sharing contribution.*

Recommendation No. 2 is considered to be without a management decision until USAID/Ghana advises RIG/Dakar of its official management decision to sustain or not sustain the questioned cost. For the amounts determined to be sustained, USAID/Ghana is required to take final action by recovering such amount and forwarding all documentation supporting its action to the Audit Performance and Compliance Division within the Management Bureau's Office of the Chief Financial Officer (M/CFO/APC).

This report is being transmitted to you for your action. Please advise my office within 30 days of actions planned or taken regarding the recommendations. If you have any questions related to this report, please contact Abdoulaye Gueye, Audit Manager, or Cheikh Talla, Financial Audit Coordinator, at RIG/Dakar.

DEFENSE CONTRACT AUDIT AGENCY

AUDIT REPORT NO. 2191– 2006U17900003

November 9, 2006

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SUBJECT: Report on Audit of USAID Resources Managed by Recipient
December 17, 2003 to September 30, 2004

REFERENCES: Cooperative Agreement No. 641-A-00-04-00048
USAID Activity Number 641-0129
Relevant Dates: See Page 42

RECIPIENT: The Molteno Project
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REPORT RELEASE RESTRICTIONS: See Page 43

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SUBJECT OF AUDIT

In response to a USAID/Ghana request, dated January 4, 2006, we examined the USAID resources managed by The Molteno Project (Molteno) under Cooperative Agreement No. 641-A-00-04-00048 for the period December 17, 2003 to September 30, 2004. The purpose of the examination was to:

- express an opinion on whether the fund accountability statements for the USAID/Ghana-funded programs present fairly, in all material respects, revenues received, costs incurred, and commodities/technical assistance directly procured by USAID for the period reviewed in conformity with the terms of the agreement and generally accepted accounting principles or other comprehensive basis of accounting, including the cash receipts and disbursements basis and modifications of the cash basis;
- obtain a sufficient understanding of the recipient's internal controls related to the USAID/ Ghana-funded programs being audited, assess control risk, and identify reportable conditions, including material internal control weaknesses;
- perform tests to determine whether the recipient complied, in all material respects, with agreement terms and applicable laws and regulations related to USAID/Ghana funded programs;
- perform an audit of the indirect cost rate if the recipient has been authorized to charge indirect costs to USAID using provisional rates and USAID has not yet negotiated final rates with the recipient;
- determine if the recipient has taken adequate corrective action on prior audit report recommendations;
- determine whether cost-sharing contributions were provided and accounted for by the recipient in accordance with the terms of the agreements; and
- perform a financial audit of the recipient's general-purpose financial statements on an organization-wide basis, if the recipient has been authorized to charge indirect costs, or if the mission specifically requests such an audit.

Molteno is responsible for preparing the fund accountability statements (FAS) to comply with the requirements in USAID "Guidelines for Financial Audits Contracted by Foreign Recipients." Molteno is also responsible for establishing and maintaining an adequate internal control structure, and for compliance with the requirements of the laws, regulations, contracts, and grants applicable to the USAID funded programs. Our responsibility is to express an opinion on the fund accountability statements, test their related internal controls and obtain reasonable assurance on whether these statements are free of material misstatement and compliant with applicable laws, regulations and grant provisions based on our examination.

SCOPE OF AUDIT

We conducted our examination in accordance with generally accepted government auditing standards and Office of Management and Budget (OMB) Circular A-122. Those standards require that we obtain a sufficient understanding of the recipient's internal controls related to the USAID cooperative agreement and to plan and perform the examination to obtain reasonable assurance about whether the data and records reviewed are free of material misstatement. An examination includes:

- evaluating the recipient's internal controls, assessing control risk, and determining the extent of audit testing needed based on the control risk assessment;
- examining, on a test basis, evidence supporting the amounts and disclosures in the data and records reviewed;
- assessing the accounting principles used and significant estimates made by the recipient; and
- evaluating the overall data and records presentation.

We evaluated Molteno's fund accountability statement, the internal controls related to the USAID funds being audited, and compliance with agreement terms, applicable laws, and regulations using the requirements contained in the:

- OMB Circular A-122, "Cost Principles for Nonprofit Organizations";
- Cooperative Agreement No. 641-A-00-04-00048 between USAID and Molteno; and
- USAID "Guidelines for Financial Audits Contracted by Foreign Recipients".

Specific procedures performed during the period February 27, 2006, to March 10, 2006, included, but were not limited to:

- examining the fund accountability statement and cost sharing schedule submitted by Molteno for the period December 17, 2003 to September 30, 2004;
- reviewing accounting records, general ledgers and project ledgers for the USAID/Ghana-funded program to determine whether costs incurred were properly recorded;
- determining the cooperative agreement recipient's ability to record, process, summarize and report financial data consistent with the assertions embodied in each account of the fund accountability statement;
- evaluating the effectiveness of internal controls for each significant assertion in the fund accountability statement;
- determining, through interviews with program management personnel and reviews of existing procedures, agreements, laws and regulations and prior audit findings, whether the control environment is effective;

- evaluating whether project management has complied with agreement terms, laws, regulations, contracts and binding policies and procedures, and determining the extent of noncompliance or unallowable expenses;
- identifying costs which are not supported with adequate documentation or are not in accordance with the applicable laws, regulations and agreement terms; and
- following up on material findings and recommendations from prior audits.

Our assessment of control risk reflects that we did not perform an examination of Molteno's internal control structure related to (i) the control environment, (ii) the accounting system, or (iii) the related internal controls in effect during the period that costs were incurred. The scope of our examination reflects our assessment of control risk and includes tests of compliance with applicable laws and regulations that we believe provide a reasonable basis for our opinion.

RESULTS OF AUDIT

Fund Accountability Statements

a. Direct Costs. In our opinion, Molteno's fund accountability statement for the period December 17, 2003 through September 30, 2004, as adjusted by our examination, presents fairly, in all material respects, the financial position of costs financed by USAID/Ghana, in conformity with the basis of accounting described in Note 1, page 7. Our examination disclosed $65,004 of ineligible direct costs, and $34,503 of unsupported costs. The ineligible costs represent unallowable employee allowances, unallowable travel and per diem expenses incurred in excess of allowable per diem rates, and unallowable Value Added Taxes (VAT) paid. The unsupported costs represent labor that could not be supported due to lack of an adequate timekeeping system and travel costs that could not be supported due Molteno's failure to maintain adequate supporting documentation for costs incurred on the agreement. The ineligible and unsupported costs are summarized as follows:

Cost Element	Ineligible	Unsupported	Total
Salary	$39,859	$21,907	$61,766
Fringe Benefits	14,382		14,382
Travel	10,706	12,048	22,754
Other Direct Costs	57	548	605
Total	$65,004	$34,503	$99,507

b. Indirect Costs. Molteno's budgeted labor costs included an overhead allocation rate of 40.5 percent that was applied to direct salaries. As discussed in exhibit A, note 6, page 14, of this report, the recipient's actual overhead rate for the period is 14.23 percent. Application of this rate to direct salary and fringe benefit costs disclosed a difference of $19,980 between the claimed overhead costs and the actual overhead costs allocable to this cooperative agreement. We question this amount as ineligible (see exhibit A, page 7).

A draft of this report was provided to Molteno by USAID/Ghana. The recipient requested many extensions of USAID/Ghana in order to respond to the draft report. USAID granted these extensions, and Molteno's comments on the draft report were received October 10, 2006. The recipient's complete written response is included as an appendix on page 44. Please refer to exhibit A, page 7, of this audit report for the fund accountability statement and the notes to the statement.

Cost Sharing

In planning and performing our review of Molteno's cost sharing schedule, we reviewed the cooperative agreement to determine if cost sharing contributions were provided and accounted for by the recipient in accordance with the terms of the agreement. According to the agreement, the recipient agreed to expend an amount not less than $47,800 of the total activity costs. Molteno was able to provide adequate supporting documentation for $26,082 in cost sharing contributions. For further details, see exhibit B, Cost Sharing, page 22 of this report.

Internal Control Structure

In planning and performing our examination, we obtained an understanding of the design of relevant internal control policies and procedures and determined whether they have been placed in operation. We assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the fund accountability statement and not to provide an opinion on internal controls. Accordingly, we do not express an opinion on Molteno's system of internal controls taken as a whole.

We noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions requiring corrective action. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect Molteno's ability to record, process, summarize and report financial data consistent with the assertions of management in the fund accountability statement. The identified reportable conditions are summarized as follows:

- lack of an adequate timekeeping system;
- inadequate segregation of duties in finance and administration departments;
- inadequate training of financial department employees; and
- failure to identify and segregate unallowable costs.

We consider lack of an adequate timekeeping system to be a material weakness. A material weakness is a reportable condition in which the design or operation of one or more of the internal control elements does not reduce to a relatively low level the risk that errors or fraud in amounts that would be material in relation to the fund accountability statement and the cost-sharing schedule may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

See exhibit C, page 27 of this report, for details on the reportable internal control deficiencies identified during the course of our audit.

Our consideration of internal controls would not necessarily disclose all matters in internal controls that might be reportable and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above.

Compliance with Grant Agreement Terms and Applicable Laws and Regulations

As part of obtaining reasonable assurance that the fund accountability statement is free of material misstatements, we performed tests of Molteno's compliance with certain provisions of agreement terms, laws, regulations, and policies and procedures. Noncompliance with any of these provisions could have a direct and material effect on the determination of the fund accountability statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. Nevertheless, our tests disclosed the following instances of noncompliance. We reported the effects of these instances as ineligible and unsupported costs in the fund accountability statement.

- failure to establish an adequate timekeeping system;
- failure to exclude unallowable salary allowances;
- failure to comply with travel policies and procedures regarding per diem;
- failure to comply with procurement policies and procedures to ensure open and free competition;
- failure to identify and segregate unallowable costs;
- failure to retain adequate supporting documentation for costs incurred on the cooperative agreement; and
- failure to adequately document and comply with cost sharing requirements.

We detailed these noncompliance conditions under exhibit D, page 31 of this report.

Follow-up on Prior Audit Findings

During our examination we obtained copies of the financial statements for FY 2004 and FY 2003 audited by BDO Spencer Steward (Johannesburg) Inc., Chartered Accountants (South Africa), dated April 25, 2005 and May 2, 2004 respectively. We performed a follow-up review to determine the status of the conditions identified in the two reports. As discussed in exhibit E, page 39 of this report, we determined that the recipient's revised policies and procedures adequately address the identified conditions. The results of our follow-up review are detailed in exhibit E, page 39 of this report.

Financial Statements

USAID requested that an audit of the recipient's organization-wide financial statements be performed if the recipient had been authorized to charge indirect costs. During our examination we obtained a copy of the financial statements for FY 2004 performed by BDO Spencer Steward (Johannesburg) Inc., Chartered Accountants (South Africa), dated April 25, 2005. As discussed in exhibit F, page 40 of this report, the chartered accountants issued a qualified opinion in that report because they did not observe the counting of the physical inventories at year end. Because Molteno's records did not permit the application of adequate alternative auditing procedures regarding this inventory, the external auditors did not obtain all the information and explanations considered necessary to satisfy themselves as to the existence and valuation of inventory. Except for the effect on the financial statement of those qualifications regarding inventory, the auditors determined that the financial statements fairly presented, in all material respects, the financial position of the company at December 31, 2004 and the results of operations and cash flows for the year then ended.

We discussed audit findings with Molteno representatives Mr. Masennya P. Dikotla, Chief Executive Officer, Mr. Velile Mqhum, Finance and Administrative Manager, Ms. Paula Gains, National Training and Research and Development Manager and with Mr. Emmanuel Qua-Enoo, Auditor, from the USAID South Africa Office of the Inspector General in an exit conference held March 10, 2006. A draft of this report was provided to Molteno by USAID/Ghana. The recipient requested many extensions of USAID/Ghana in order to respond to the draft report. USAID granted these extensions, and Molteno's comments on the draft report were received October 10, 2006. The recipient's complete written response is included as an appendix on page 44. Please refer to exhibit A, page 7, of this audit report for the fund accountability statement and the notes to the statement.

THE FUND ACCOUNTABILITY STATEMENT

We consider $84,984 to be ineligible costs and $34,503 to be unsupported costs based on our examination of costs incurred under the cooperative agreement no. 641-A-00-04-0048 for the period December 17, 2003 through September 30, 2004. The following schedule details the ineligible and unsupported costs by element.

The Molteno Project
Cooperative Agreement No. 641-A-00-04-00048
Fund Accountability Statement by Cost Element (Note 1)
And Results of Audit
December 17, 2003 to September 31, 2004

FUND ACCOUNTABILITY STATEMENT
December 17, 2003 to September 31, 2004

	BUDGET	ACTUAL	QUESTIONED COSTS			NOTES
		(Note 2)	INELIGIBLE	UNSUPPORTED	TOTAL	
REVENUE						
Total Revenue (USD)	$623,553	$481,842				3
COSTS INCURRED						
Personnel						
Salary	$68,101	$61,766	$39,859	$21,907	$61,766	4
Fringe Benefits	21,815	27,857	14,382		14,382	5
Overhead Allocation	27,581	25,015	19,980		19,980	6
Travel	74,100	71,946	10,706	12,048	22,754	7
Equipment	415,106	289,881				8
Supplies	11,610	1,123				8
Contractual	3,240	1,163				8
Other Direct Costs	2,000	3,091	57	548	605	9
Total Costs Incurred	$623,553	$481,842	$84,984	$34,503	$119,487	

NOTES TO FUND ACCOUNTABILITY STATEMENT

1. Accounting Principles

The fund accountability statement of The Molteno Project for Cooperative Agreement No. 641-A-00-04-00042 funded by USAID was prepared on an accrual basis in accordance with generally accepted accounting principles. The statement is presented by cost element, in accordance with the requirements of USAID and budgeted amounts.

2. Actual Costs

The amounts included as actual costs in the recipient's fund accountability statement are based on the five invoices submitted to USAID from March 10, 2004 through October 12, 2004 for reimbursement under the cooperative agreement. As discussed in the notes below, salary and related fringe and overhead costs were calculated using budgeted rates and actual labor hours. The remaining costs were based on actual costs incurred. Unless a specific exchange rate was provided in the recipient's calculations, we used the exchange rate of 6.45 South African rands per dollar obtained from Global Insight (GI) economic indices. The GI exchange rate of 6.45 is the average rate for 2004.

3. Total Revenue

   a. Summary of Conclusions:

We reconciled Molteno's reimbursements to the accounting books and to USAID's records. USAID/Ghana's fund distribution schedule includes $3,489 that has not been included in Molteno's books and records. Molteno should be required to explain where these funds were used, since they are not included in the total claimed revenue amount of $481,842.

   b. Basis of the Recipient's Revenue:

The recipient's claimed revenue is based on reimbursements received for five invoices submitted to USAID that represent total claimed cost on the cooperative agreement.

   c. Audit Evaluation:

We compared USAID/Ghana's schedule of funds dispersed to the amounts recorded in Molteno general ledger account number 2110.118, Income, USAID/Ghana. We verified that the amounts received for reimbursement based on the five submitted invoices was properly recorded. There is a difference of $3,489 between USAID/Ghana's claimed distribution of $485,331 and Molteno's recorded revenue of $481,842. We were not able to determine the reason for the difference.

4. Salary

   a. Summary of Conclusions:

We questioned salary costs of $39,859, since we determined these costs to be ineligible under the cooperative agreement. These costs represent the difference between the recipient's claimed direct salary costs and the recorded direct salary costs for the cooperative agreement. We questioned the remaining salary costs as unsupported, since the recipient does not have an adequate timekeeping system as required by OMB Circular A-122.

b. Basis of the Recipient's Costs:

The recipient's claimed salary costs were submitted to USAID in five invoices that represent total claimed cost. Molteno based its claimed costs on the budgeted labor rates for each employee multiplied by the claimed labor hours for each employee. The budgeted labor rates were the same as the ones proposed in Molteno's budget prepared for the cooperative agreement.

c. Audit Evaluation:

We determined that claimed salary costs (based on the budgeted rates) were significantly higher than actual salary costs incurred. The recipient also claimed salary costs for each day that employees were on trips to Ghana, including weekends and other days when the employees were not actually working.

Using information extracted from the recipient's payroll records, we calculated the actual daily base salary rate for each employee for whom salary costs were claimed. Our calculations assumed 21.66 workdays per month (52 weeks × 5 days per week ÷ 12 months). We multiplied our audit-determined daily salary rate by the number of audit-determined work days charged to the cooperative agreement to compute total salary costs for each employee. The audit-determined daily salary rate does not include fringe costs. The computation of questioned salary cost is shown below:

Questioned salary costs	Amount
Invoiced Costs (a)	$61,766
Actual Costs Per Payroll Records (b)	$32,430
Less Management and Administravie Salaries (c)	10,523
Direct Costs Incurred (d) = (b) - (c)	$21,907
Questioned Invoiced Costs (e) = (a) - (d)	$39,859

Molteno's invoiced labor costs include direct employees (trainers and research personnel who worked in Ghana), and management and administrative support staff. Molteno does not require its management and administrative staff to prepare timesheets in sufficient detail to allow us to determine labor hours allocable to this cooperative agreement. In addition, all salary and fringe benefit costs for management and administrative staff are included in Molteno's home office accounts in its General Ledger. As discussed in note 6, page 14 of this report, home office costs are included in the overhead allocation. Therefore, in order to preclude duplicate recovery of these costs, we have questioned the invoiced administrative and management salaries of $10,523 as unallowable. Since the administrative and management salaries are already recovered through the overhead rates, they should not be claimed as a separate cost under this agreement.

The recipient did not have written timekeeping policies as required by OMB Circular A-122, attachment B, section 8, Compensation for Personal Services – Support of Salary. Direct labor costs were not supported by personnel activity reports. Because the direct labor costs were not supported by timesheets, we were unable to verify the nature of the work performed or the actual hours worked. Accordingly, we have questioned the direct labor costs as unsupported. Since the recipient did not have timesheets in support of the claimed direct labor, we used an alternative method to determine the schedule followed by direct employees during each trip. Based on the "Progress Report", we determined the number of days each employee worked on the cooperative agreement. We allowed one working day for each day the employee was conducting a workshop or orientation, and additional days as necessary for travel.

d. Recipient's Reaction:

In their undated response to Mr. James Athanas, USAID Senior Contracting Officer, (received by DCAA on October 10, 2006) Molteno agrees that $4,020 of personnel cost is ineligible. However, Molteno's written response regarding questioned costs is predicated on the conclusion that it is not subject to OMB Circular A-122 regulations governing indirect costs. Molteno argues that nowhere in the cooperative agreement is there any mention of overhead rates, indirect cost rates, negotiated indirect cost rates, etc. Further, they argue that the cooperative agreement budget includes seven cost elements (personnel, fringe benefits, travel, equipment, supplies, and contractual). Molteno asserts that since overhead is not included as one of these cost elements, it is not proper to question costs associated with overhead. Molteno's complete written response is included as an appendix on page 44.

e. Auditor's Response:

Molteno's fund accountably statement (FAS) submission received from Velile Mqhum, Molteno Finance/Administrative Manager, on February 28, 2006 clearly shows personnel costs made up of salary, fringe benefits, and overhead allocation. Except for concurring to $4,020 of ineligible personnel costs, Molteno essentially disagrees with the remaining questioned costs. The recipient states that overhead costs should not be questioned for reasons discussed above; however, since Molteno's FAS submission includes these costs, it is their responsibility to support the costs as claimed. The time to do this was during audit fieldwork performed February 25 through March 10, 2006. Since Molteno's response does not address the questioned costs as presented in the FAS or our audit report, we offer no additional comments.

5. <u>Fringe Benefit Costs</u>

a. Summary of Conclusions:

We questioned fringe benefit costs of $14,382 due to the difference between the fringe benefit costs claimed by the recipient, and allowable actual costs incurred as determined by our audit.

b. Basis of Recipient's Cost:

In its budget for the cooperative agreement, Molteno applied a fringe benefit rate of 32.1 percent to base salary costs to which an overhead allocation of 40.5 percent had already been applied. Therefore, the fringe benefit rate was apparently applied to an overstated allocation base. We noted that salary bonus, medical aid, pension, insurance, regional service and skills development levy costs were included in both the base salary costs, and in the applied fringe benefit pool costs included in the budgeted fringe benefit rates.

c. Audit Evaluation:

We determined that claimed fringe benefit costs were significantly higher than actual costs incurred. The claimed fringe benefit costs are based on the budgeted rate, applied to an overstated allocation base as discussed in note 5.b above.

Further, we determined that claimed fringe benefit costs included unallowable costs for housing, travel and subsistence and travel allowance. Additionally, claimed fringe benefit costs include costs for indirect employees working in the home office. As discussed in note 6, page 14 of this report, home office costs have already been included in the overhead allocation. Therefore, the claimed fringe benefit costs for indirect employees represent a duplicate recovery of these costs.

Using the recipient's payroll records, we calculated the actual fringe benefit costs for all employees for whom fringe benefit costs were claimed. From this amount we deducted fringe benefits applicable to management and administrative employees, as well as unallowable fringe benefit costs as discussed above. Our computation of questioned fringe benefit costs is summarized below:

Molteno fringe benefit costs	Amount		Notes
Invoiced Costs (a)		$27,857	
Actual Costs Per Payroll Records (b)		$23,408	
Less: Management and Administrative Fringe (c)		7,517	(1)
Less: Unallowable Costs for Direct Employees			
Housing Allowance	$626		(2)
Travel Allowance	1,243		(3)
Subsistence and Travel Allowance	547		(4)
Total Unallowable Costs (d)		2,416	
Allowable Actual Costs (e) = (b) - (c) - (d)		$13,475	
Questioned Invoiced Costs (f) = (a) - (e)		$14,382	

Notes

(1) Administrative and Management Fringe Benefits

We determined that $7,517 of the actual fringe benefit costs relate to management and administrative staff. As such, these fringe benefit costs are properly recovered through the overhead allocation as discussed in note 6, page 14, as direct costs on the cooperative agreement. Therefore, these costs are deducted from the actual costs per the payroll records.

(2) Housing Allowance

Molteno provides specific employees a housing allowance of 550 rands per month to help defray bond (mortgage) costs. Actual costs incurred for this benefit are included in the general and payroll ledger for the period.

We questioned $784 of The Molteno Project's housing allowance costs. Management and administrative employee costs comprise $158 of the total questioned costs. As discussed in note 5.c above, we determined that these costs are included in the overhead rate and have therefore questioned their inclusion as direct costs on the cooperative agreement.

The remaining questioned costs of $626 ($784 - $158) are costs incurred by direct (training and research) personnel. These costs are unallowable costs per OMB Circular A-22, attachment B, paragraph 20, Housing and Personal Living Expenses, which states:

> *Costs of housing (e.g., depreciation, maintenance, utilities, furnishings, rent, etc.), housing allowances and personal living expenses for/of the organization's officers are unallowable as fringe benefit or indirect costs regardless of whether the cost is reported as taxable income to the employees. The term "officers" includes current and past officers and employees.*

Using information extracted from the recipient's payroll ledger, we calculated the monthly housing allowance for eligible trainers and research staff. We calculated a daily unallowable housing allowance cost for each employee assuming 21.66 workdays per month (52 weeks × 5 days per week ÷ 12 months). We then multiplied this daily rate by the number of audit-determined work days charged to the cooperative agreement to determine the total unallowable cost for each employee.

(3) Travel Allowance

Molteno employees having authorization to use Molteno corporate vehicles are required to maintain travel logs that document miles traveled for personal use and miles traveled for Molteno business and expenses incurred. The recipient's claimed costs include total costs for fuel and oil and insurance costs paid on the vehicle.

Using the recipient's payroll ledger, we computed questioned travel allowance cost for all Molteno employees (direct, administrative, and management) of $2,451. Of this amount, $1,208 relates to travel allowance costs for Molteno administrative and management staff. The questioned travel costs of $1,243 is the difference between total questioned travel allowance costs ($2,451) and the questioned costs applicable to administrative and management staff ($1,208). These questioned costs relate to training and research (direct) employees for personal use of company vehicles. These costs are unallowable costs per OMB Circular A-22, Attachment B, Paragraph 8, Compensation for Personal Services which states:

> *That portion of the cost of organization-furnished automobiles that relates to personal use by employees (including transportation to and from work) is unallowable as fringe benefit or indirect costs regardless of whether the cost is reported as taxable income to the employees.*

Using the travel logs for each of the training and research employees, we calculated the personal use portion of each employee's travel allowance included in the recipient's payroll ledger. We calculated a daily unallowable travel allowance cost for each employee assuming 21.66 workdays per month (52 weeks × 5 days per week ÷ 12 months). We then multiplied this daily rate by the number of audit-determined work days charged to the cooperative agreement to determine the total unallowable cost for each employee.

(4) Subsistence and Travel Allowance (S&T)

Per The Molteno Project's policies and procedures, for those trips involving overnight travel away from home, each employee may either receive an allowance to arrange private accommodation and other incidental expenses, or claim actual costs by arranging accommodation at a hospitality institution approved by Molteno. Claimed costs represent actual costs incurred for the period.

Using information provided in the recipient's payroll ledger, we calculated the monthly S&T allowance for eligible employees. We calculated a daily S&T allowance cost for each employee assuming 21.66 workdays per month. We then multiplied this daily rate by the number of audit-determined work days charged to the cooperative agreement to determine the total unallowable cost for each employee.

We questioned $547 of The Molteno Project's subsistence and travel allowance (S&T) costs. The questioned costs are costs incurred by training and research personnel that have been charged to the cooperative agreement as direct travel costs on invoices presented to USAID/Ghana and included in the Fund Accountability Statements as travel costs. In order to preclude duplicate charges to the Government, we have questioned as ineligible all S&T costs claimed as fringe benefit costs.

d. Recipient's Reaction:

Molteno's written response (appendix on page 44) does not specifically address questioned fringe benefit costs. See page 10, note 4.d, for additional information.

e. Auditor's Response:

Since Molteno's response does not address the questioned costs as presented in the FAS or our audit report, we offer no additional comments. See page 10, note 4.e, for additional comments.

6. Overhead Allocations

a. Summary of Conclusions:

We questioned $19,980 of the claimed overhead costs as ineligible. Questioned costs represent the difference between the claimed overhead costs and the overhead costs computed by applying the audit-determined overhead rate of 14.23 percent to the audit-determined salary and fringe benefit costs.

b. Basis of Recipient's Costs:

In its budget prepared for the cooperative agreement, Molteno included an overhead rate of 40.45 percent, which was applied to the calculated base salary costs. The base salary costs exclude fringe benefits. The notes to the budget indicate that the rate was developed using Molteno's 2002 audited costs. Our review of Molteno's 2002 financial statements disclosed that the notes specifically refer to these costs as unaudited. Additionally, Molteno finance personnel were unable to reconcile these costs to its books and records.

c. Audit Evaluation:

Because the recipient was unable to provide support for the proposed overhead rate, we reviewed costs in Molteno's general ledger to develop an audit-determined overhead rate. Audit-determined overhead pool costs include home office related expenses in the general ledger with the suffix ".100". Audit-determined overhead base costs include all direct labor and related fringe costs on Molteno's various projects. We traced costs in accounts that we considered significant in amount to invoices and payroll documents. We noted no differences between the costs included in the general ledger and the supporting documentation. Details of the audit-determined overhead rate, including questioned costs identified in the overhead pool, are summarized on the following schedule and accompanying notes:

Overhead Pool

Cost Element	Actual Cost Incurred	Ineligible Costs	Notes
Professional Services	$27,234		
Bank Charges	$4,832	$112	(1)
Salaries	$155,254		
Fringe Benefits and Taxes	$111,799		
Office Costs	$90,228		
Miscellaneous Costs	$19,909		
Housing Allowance	$4,775	4,775	(2)
Interest on Vehicle Financing	$15,868	15,868	(1)
Training Expenses	$8,518		
Travel Expenses	$8,219	1,020	(3)
Total	$446,636	$21,775	

Overhead Base

Cost Element	Actual Cost Incurred
Direct Salaries	$2,864,257
Direct Fringe Benefits and Taxes	121,460
Total	$2,985,717
Overhead Rate Before Exclusion of Ineligible Costs	14.96%
Audit Adjusted Overhead Rate	14.23%

Notes

(1) Interest

We questioned as ineligible $15,980 of interest costs included in Molteno's overhead pool. The recipient's costs are based on actual monthly costs incurred as recorded in its books and records and supported by invoices.

Our review of costs included in the overhead pool disclosed $112 in account number 1030.100 (Bank Charges) incurred as interest charged on credit cards. Additionally, account number 1097.100 (Interest on Vehicle Financing) included costs of $15,868 incurred as interest for vehicle financing. Total questioned costs are therefore $112 + $15,868 = $15,980.

OMB Circular A-122, attachment B, paragraph 23 states, "Costs incurred for interest on borrowed capital, temporary use of endowment funds, or the use of the non-profit organization's own funds, however represented, are unallowable." Accordingly, we have questioned those costs as ineligible costs on the cooperative agreement.

(2) Housing Allowance

The Molteno Project provides specific employees a housing allowance of 550 rands per month (approximately $86) to help defray bond (mortgage) costs. Actual costs incurred for this benefit are included in the general and payroll ledger for the period.

Our review of costs included in the overhead pool disclosed $4,775 in account 1095.100, General Housing Subsidy, incurred as housing allowance costs.

OMB Circular A-122, attachment B, paragraph 20, Housing and Personal Living Expenses states:

> *Costs of housing (e.g., depreciation, maintenance, utilities, furnishings, rent, etc.), housing allowances and personal living expenses for/of the organization's officers are unallowable as fringe benefit or indirect costs regardless of whether the cost is reported as taxable income to the employees. ... The term "officers" includes current and past officers and employees.*

Accordingly, we have questioned all housing allowance costs included in the overhead pool as costs ineligible costs under the cooperative agreement.

(3) Travel Expenses

Molteno employees having authorization to use Molteno corporate vehicles are required to maintain travel logs that document miles traveled for personal use and miles traveled for Molteno business and expenses incurred. The recipient's claimed costs include total costs (business and personal use) for fuel and oil and insurance costs paid on the vehicle.

We questioned $1,020 of The Molteno Project's travel expense costs included in its overhead pool. The questioned costs represent costs incurred by administrative and management personnel for personal use of company vehicles. These costs are unallowable costs per OMB Circular A-122, attachment B, paragraph 8, Compensation for Personal Services which states:

> *That portion of the cost of organization-furnished automobiles that relates to personal use by employees (including transportation to and from work) is unallowable as fringe benefit or indirect costs regardless of whether the cost is reported as taxable income to the employees.*

Accordingly, we have questioned these costs included in the overhead pool as costs ineligible to be charged to the cooperative agreement.

Audit-determined overhead costs were computed using the audit-adjusted overhead rate, and applying it to the audit-determined salary and fringe benefit costs. The audit-determined overhead costs were then deducted from the claimed overhead costs to compute questioned overhead costs. This computation is summarized in the following table:

Molteno overhead costs	Amount	Reference
Claimed Overhead Costs (a)	$25,015	
Audit-Determined Overhead Base Costs		
Audit-Determined Salary Costs (b)	$21,907	*Exh. A, Note 4*
Audit-Determined Fringe Benefit Costs (c)	13,475	*Exh. A, Note 5*
Total (d) = (b) + (c)	$35,382	
Audit-Determined Overhead Rate (e)	14.23%	
Audit-Determined Overhead (f) = (d) × (e)	$5,035	
Questioned Overhead Costs (g) = (a) - (f)	$19,980	

d. Recipient's Reaction:

Molteno's written response (appendix on page 44) does not specifically address questioned overhead costs. In fact, Molteno disagrees that they are subject to the OMB Circular A-122 requirements governing indirect costs. See page 10, note 4.d, for additional information.

e. Auditor's Response:

Molteno's fund accountably statement (FAS) submission received from Velile Mqhum, Molteno Finance/Administrative Manager on February 28, 2006 clearly shows personnel costs made up of salary, fringe benefits, and overhead allocation. Since Molteno's response does not address the specific computations or factual matters regarding questioned overhead costs as presented in the FAS or our audit report, we offer no additional comments. See page 10, note 4.e, for additional comments.

7. Travel

a. Summary of Conclusions:

We questioned travel costs of $10,706 as ineligible, and travel costs of $12,048 as unsupported. Ineligible costs include costs for Value Added Taxes (VAT), charges for meals that should have been included in per diem charges, and differences between the claimed costs and the recipient's post-workshop reports. Unsupported costs of $12,048 relate to inadequate documentation in support of the accommodations and per diem costs claimed on the first two invoices submitted to USAID.

b. Basis of Recipient's Cost:

Travel costs consist of airfares, visas, travel insurance, required preventive medicine, accommodations and per diem. According to the recipient's policies and procedures, the not-to-exceed accommodation rate for locations within Accra is $102, and $50 for locations outside of Accra. Molteno's policies and procedures require employees to submit receipts for reimbursement of accommodation costs. The per diem rate for Molteno employees working in Accra is $54 and $32 outside of Accra. Per diem is a flat rate per day and receipts are not required.

c. Audit Evaluation:

We examined each of the invoices submitted by Molteno under the cooperative agreement. We examined all available supporting documentation for each invoice. The recipient did not have travel reconciliation sheets for each trip taken by the employees. We used an alternative method to determine the schedule followed by each employee during each trip. The recipient provided two progress reports that describe the project work performed from January through September 2004. These include dates of workshops, and the participants from Molteno. Based on the progress reports, we determined the number of days that employees were working in Accra or outside of Accra to compute the allowable accommodation and per diem rates.

A summary of the questioned travel costs, by element, including explanation for each element questioned, is included in the following schedule:

			Questioned Costs	
Description	Invoiced Cost	Allowable Costs	Ineligible Costs	Unsupported Costs
Airfares	$35,362	$33,882	$1,480	
Accomodations & Per Diem	34,141	25,247	8,894	$12,048
Visas & Med.	2,111	2,111		
VAT	332		332	
Total	$71,946	$61,240	$10,706	$12,048

No receipts were available for the days that accommodation costs were claimed for invoices one and two. Therefore, we used an average of the claimed costs that were adequately supported on subsequent invoices. We calculated accommodation and per diem costs of $12,048 for the first two invoices. However, since these costs were not substantiated by receipts and other documentation, we questioned them as unsupported.

Questioned airfare costs include the difference between claimed and actual airfares, and the airfare costs for a trip that was cancelled.

We questioned claimed costs for accommodations and per diem as ineligible, because the days claimed did not agree with the "Progress Report" schedule. Further, the recipient included separate charges for meals which were already recovered through allowable per diem costs.

VAT costs are an unallowable expense in accordance with OMB Circular A-122 attachment B, paragraph 47, Taxes, which states:

> *In general, taxes which the organization is required to pay and which are paid or accrued in accordance with GAAP, and payments made to local governments in lieu of taxes which are commensurate with the local government services received are allowable, except for (i) taxes from which exemptions are available to the organization directly or which are available to the organization based on an exemption afforded the Federal Government and in the latter case when the awarding agency makes available the necessary exemption certificates.*

A VAT exemption was available to The Molteno Project.

We converted questioned South African rands to the U.S. dollar amount using the same exchange rate that Molteno used in their cost reimbursement claims to USAID under the cooperative agreement. The exchange rate used by the recipient is comparable to the exchange rate reported in Global Insight for the period of performance.

d. Recipient's Reaction:

Molteno concurs with questioned airfare and VAT costs of $1,480 and $332, respectively. The recipient states that additional supporting documentation has been located to support the remaining questioned costs. Molteno's complete written response is included as an appendix on page 44.

e. Auditor's Response:

Our audit fieldwork was performed February 25 through March 10, 2006. Molteno had ample opportunity to provide any and all supporting documentation during our audit and prior to completion of the draft report in April 2006. If additional supporting documentation can be provided to USAID for analysis, this may impact the final conclusions regarding these costs. However, we do not have the resources available at this time to review addition documentation. Therefore, we offer no additional comments.

8. Equipment, Supplies, Contractual Costs

a. Summary of Conclusions:

We take no exception to the recipient's claimed costs of $289,881, $1,123, and $1,163 for equipment, supplies and contractual costs respectively.

b. Basis of Recipient's Costs

Equipment costs consisted of materials purchased from Molteno's contracted supplier, Maskew, Miller, Longman, to be used in its Ghanaian workshops. Costs recorded in Molteno's books and records were supported by invoices from the contracted supplier.

Supply costs consisted of miscellaneous office supplies and photocopying costs for materials to be used in Ghanaian workshops. Costs recorded in Molteno's books and records were generally supported by invoices.

Contractual costs were incurred for artwork used in the development of the pilot materials, and were recorded in Molteno's books and records.

c. Audit Evaluation:

We examined each of the invoices used by the recipient to claim costs under the cooperative agreement. We examined all available supporting documentation for each invoice. We traced selected costs to the recipient's books and records. We take no exception to the recipient's claimed amounts for these items.

9. <u>Other Direct Costs</u>

a. Summary of Conclusions:

We questioned $605 of the claimed other direct cost of $3,091. Molteno failed to provide adequate documentation in supporting $454 of claimed excess baggage. We also questioned $151 for car rental charges of which $57 was due to VAT charges, and the remaining due to the difference between the claimed amount and the amount supported by adequate documentation. VAT is an unallowable expense in accordance with OMB Circular A-122, attachment B, paragraph 47.

b. Basis of Recipient's Costs:

The recipient's claimed cost was submitted to the government in five invoices that represent total claimed cost. The recipient's costs were based on actual cost from its books and records for the period December 17, 2003 to September 30, 2004.

Claimed other direct costs consist of rental car expenses, excess baggage, freight and telephone/fax services. Costs were supported by invoices and costs recorded in Molteno's books and records.

c. Audit Evaluation:

We examined each of the invoices used by the recipient to claim costs under the cooperative agreement. We examined all available supporting documentation for each invoice. We traced selected costs to the recipient's books and records. We questioned a total of $605 of the recipient's claimed costs; $454 for unsupported excess baggage costs, and $151 for unsupported car rental charges (of which $57 was for VAT). With respect to the VAT charges, OMB Circular A-122, attachment B, paragraph 47, states:

> *In general, taxes which the organization is required to pay and which are paid or accrued in accordance with GAAP, and payments made to local governments in lieu of taxes which are commensurate with the local government services received are allowable, except for (i) taxes from which exemptions are available to the organization directly or which are available to the organization based on an exemption afforded the Federal Government and in the latter case when the awarding agency makes available the necessary exemption certificates.*

A VAT exemption was available to The Molteno Project.

d. Recipient's Reaction:

Molteno concurs with questioned VAT costs of $57. The recipient states that additional supporting documentation has been located to support the remaining questioned costs. Molteno's complete written response is included as an appendix on page 44.

e. Auditor's Response:

As stated previously, our audit fieldwork was performed February 25 through March 10, 2006, with the draft report completed in April 2006. In order to perform audits that are effective, efficient, and meaningful, we require supporting documentation to be provided at the time of fieldwork. We make a diligent effort in each audit to request and/or obtain necessary documentation before or during field work. If additional supporting documentation can be provided to USAID for analysis, this may impact the final conclusions regarding these costs. However, we do not have the resources available at this time to review addition documentation. Therefore, we offer no additional comments.

COST SHARING

	ACTUAL (Note 1)	QUESTIONED COSTS (Note 2) INELIGIBLE	UNSUPPORTED	TOTAL	Notes
CASH					
IN-KIND					
Preparation Costs	$2,480	$2,480		$2,480	3
Travel and Recovery Costs	49,848	17,686	$6,696	24,382	4
Support Provided by Ghanaian Officials	8,599		8,599	8,599	5
Material development and Translation Costs	22,568	376	21,576	21,952	6
Total	$83,495	$20,542	$36,871	$57,413	

EXPLANATORY NOTES

1. Actual Costs

Under section A.8 of cooperative agreement no. 641-A-00-04-00048, Molteno agreed to expend no less than $47,800 as eligible cost sharing expenses. The recipient provided a schedule that reflects its claimed cost sharing amounts. Our review disclosed that Molteno was able to provide adequate supporting documentation for only $26,082 ($83,495 claimed less $57,413 total questioned) for cost sharing purposes. Of the questioned costs, $20,542 relates to cost determined to be ineligible under the cooperative agreement, and $36,871 relate to unsupported costs.

2. Exchange Rate

The recipient's claimed costs were calculated in U.S. dollars. Our calculation of costs incurred was based on the recipient's books and records which accumulate costs in South African rands. In order to perform a comparative analysis we used a conversion factor of 6.45 rands per dollar obtained from Global Insight (GI) economic indices. The GI conversion factor is the average rate for 2004.

3. Preparation Costs

a. Summary of Conclusions:

In its schedule of cost sharing contributions, Molteno included $2,480 for materials preparation. The costs were incurred under a different USAID cooperative agreement (641-A-00-04-00004) and are therefore not eligible to be claimed as cost sharing contributions under this agreement.

b. Basis of Recipient's Costs:

The recipient claimed cost sharing amounts for three Molteno employees for preparation and workshop costs related to a workshop presented from October 14 through October 21, 2003.

c. Audit Evaluation:

Our review of supporting documents provided by the recipient disclosed that the claimed costs were included on Molteno invoice no. 118/GHA/0002, dated October 28, 2003, submitted to USAID/Ghana under fixed price cooperative agreement 641-A-00-04-00004. Paragraph C.19 of the audited cooperative agreement (641-A-00-04-00048) stipulates that costs considered to be cost sharing must be incurred as project costs. Since the costs were not incurred for the audited cooperative agreement, we have determined them to be ineligible as cost sharing.

d. Recipient's Reaction:

Molteno does not specifically address our questioned cost sharing amounts by element. Rather, they state that additional eligible cost sharing amounts have been identified and that the analysis is available for review. Molteno's complete written response is included as an appendix on page 44.

e. Auditor's Response:

As stated previously, our audit fieldwork was performed February 25 through March 10, 2006, with the draft report completed in April 2006. In order to perform audits that are effective, efficient, and meaningful, we require supporting documentation to be provided at the time of fieldwork. We make a diligent effort in each audit to request and/or obtain necessary documentation before or during field work. If additional supporting documentation can be provided to USAID for analysis, this may impact the final conclusions regarding these costs. However, we do not have the resources available at this time to review addition documentation. Therefore, we offer no additional comments.

4. <u>Travel and Recovery Day Costs:</u>

a. Summary of Conclusions:

We questioned $17,686 of claimed travel and recovery day costs as ineligible, due to claimed amounts exceeding actual costs. Also, we questioned $6,696 of claimed travel and recovery day costs as unsupported, since Molteno could not provide adequate support for these costs.

b. Basis of Recipient's Costs:

Molteno's written policies and procedures provide one day of compensatory leave for any weekend day during which an employee is required to work or to be away from home. One day of compensatory leave is also provided each time an employee is required to spend more than four nights away from home on Molteno business. This compensatory time off is termed "recovery days."

Molteno also included compensatory travel days for employee travel to and from Johannesburg from the employees' home prior to departure for Ghana workshops.

For its cost sharing contribution, Molteno claimed 145 recovery days and 56 travel days at a rate of $248 per day.

c. Audit Evaluation:

We reviewed the recipient's records to verify that the costs for the claimed recovery and travel days were not already included in invoiced costs under the cooperative agreement.

We calculated the number of travel and recovery days that were supported by travel documentation, principally airfare receipts and post workshop reports. We noted that Molteno used a labor rate of $248 for each recovery and travel day rather than the actual costs incurred. We calculated the actual cost incurred for each employee using the audit-determined fully burdened labor rate for the period in which the travel occurred. The questioned costs identified as ineligible in the above schedule represent the difference between the actual costs incurred, and the claimed costs.

Our audit disclosed that adequate documentation was not available for $6,696 of the claimed travel and recovery day costs. Therefore, we have classified these costs as unsupported.

d. Recipient's Reaction:

Molteno does not specifically address our questioned cost sharing amounts by element. Rather, they state that additional eligible cost sharing amounts have been identified and that the analysis is available for review. Molteno's complete written response is included as an appendix on page 44.

e. Auditor's Response:

See page 23, note 3.e, for our response.

5. Support Provided by Ghanaian Officials

a. Summary of Conclusions:

We set aside as unsupported Molteno's claimed cost sharing contributions of $8,599 for support received from Ghanaian officials at workshops presented by Molteno trainers.

b. Basis of Recipient's Costs:

The recipient provided a schedule of costs based on a total of 555 days attendance by Ghanaian officials at workshops conducted by The Molteno Project. The claimed costs were based on the officials' annual salaries.

c. Audit Evaluation:

In addition to the schedule of claimed cost sharing contributions, the recipient provided two documents: "Breakthrough to Literacy and Bridge to English – Progress Report on the Pilot Implementation – January to August 2004" and "Breakthrough to Literacy and Bridge to English – Report on the Pilot Implementation – Final Cumulative Report – Cooperative Agreement Number 641-A-00-04-00048."

We reviewed the documents provided. Although they discuss the attendance of Ghanaian officials at the workshops, the number of attendees is discussed for only two of five workshops. We were unable to determine from the reports the nature of the support provided by Ghanaian officials at the workshops conducted by Molteno. Therefore, we do not consider the reports to be adequate documentation for the claimed cost sharing contributions. No additional supporting documentation was provided. Accordingly, we have set those costs aside as unsupported.

d. Recipient's Reaction:

Molteno does not specifically address our questioned cost sharing amounts by element. Rather, they state that additional eligible cost sharing amounts have been identified, and that the analysis is available for review. Molteno's complete written response is included as an appendix on page 44.

e. Auditor's Response:

See page 23, note 3.e, for our response.

6. Material Development and Translation Costs

a. Summary of Conclusions:

We questioned $376 of the claimed material development and translation costs as ineligible, and $21,576 as unsupported. The ineligible costs of $376 represent the difference between the claimed costs and the actual costs for the number of days that we could verify in our audit. Since we were able to verify only 4 of 91 days claimed for material development and translation costs, we set aside claimed costs of $21,576 for the remaining 87 days as unsupported.

b. Basis of Recipient's Costs:

Molteno provided a cost sharing contribution schedule that identified the number of days by month for the period October 2003 through August 2004 for employee J. Mogodiri. The total number of days was 91 according to this schedule; the daily labor rate was $248 per day, for a total of $22,568.

c. Audit Evaluation:

We reviewed timesheets for the period October 2003 through August 2004, and interviewed the subject employee, including reviewing her daily journal. From this interview and review of timesheets and employee journal we were able to verify only four of the 91 claimed days for this cost sharing item. Additionally, we determined that the actual fully-burdened labor rate for the employee was $153.89 per day.

For the four days that we could verify, we calculated the difference between the claimed and actual costs for the identified employee for these days. For the remaining 87 days that we were unable to verify, we classified the entire claimed amount as unsupported.

d. Recipient's Reaction:

Molteno does not specifically address our questioned cost sharing amounts by element. Rather, they state that additional eligible cost sharing amounts have been identified, and that the analysis is available for review. Molteno's complete written response is included as an appendix on page 44.

e. Auditor's Response:

See page 23, note 3.e, for our response.

INTERNAL CONTROL STRUCTURE

Our examination disclosed certain deficiencies in the design and operation of the internal control structure at The Molteno Project. In our judgment, these deficiencies could adversely affect Molteno's ability to record, process, summarize and report costs associated with USAID grants in a manner consistent with grant provisions and applicable laws and regulations. The reportable conditions are detailed as follows:

1. <u>Segregation of Duties</u>

   a. Condition:

Molteno has limited segregation of duties within the finance and administration departments. Currently, Molteno has a finance/administration manager, a finance controller and a finance clerk. The majority of accounting for USAID grants and Molteno is handled by the finance controller and finance clerk.

The finance clerk processes requests for payments, prepares the checks, makes the payments, receives cash, handles petty cash, reconciles the bank statements and inputs costs to the accounting system. The finance controller also makes entries into the accounting system. We consider the fact that the finance clerk performs the payment function, reconciliations, as well as making entries into the accounting system to be an internal control weakness. Segregation of duties reduces the opportunities to allow any person to be in a position to both perpetrate and conceal errors or irregularities. Since the finance clerk performs tasks that include preparing payments, reconciling external reports (bank statements), and making entries into the books and records, errors or irregularities may not be detected in a timely manner.

   b. Recommendation:

We recommend that internal controls be improved through greater segregation of duties. For example, duties should be divided in such a manner that bank reconciliations are not performed by the person responsible for receiving and depositing cash and overseeing petty cash. To improve segregation of duties, the bank accounts should be reconciled by someone other than the person who processes the payments. Further, the reconciliations should be approved by the finance and administrative manager.

   c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

2. Training

a. Condition:

The members of Molteno's finance department have not received any formal training regarding USAID laws and regulations and are not familiar with OMB Circular A-122, Cost Principles for Non-Profit Organizations. These employees are responsible for reviewing costs for allowability and coding to the appropriate activity for payment. Lack of adequate training for the accounting staff increases the possibility that unallowable costs will be charged to USAID cooperative agreements and grants.

b. Recommendation:

We recommend that the financial/administrative manager and any other accounting staff involved in the processing of costs related to USAID grants or cooperative agreements be provided training on applicable laws and regulations. The training should provide an adequate understanding of laws and regulations to enable Molteno employees to identify and segregate unallowable costs under USAID grant agreements.

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

3. Timekeeping Controls

a. Condition:

Molteno does not have adequate timekeeping controls in place. Employees do not maintain detailed timesheets or record the time spent on specific projects or activities. There is no written certification by employees or supervisors regarding time worked; further, there is no record of actual cost objectives for which work was performed.

Timekeeping controls are important to assist in budgeting, preparing estimates for grant proposals, recording actual time worked on projects and calculating indirect costs. Since they did not have proper timekeeping controls, Molteno could not determine the actual direct labor hours related to specific projects or cost objectives, including the subject USAID grant. In addition, timesheets are required to enable Molteno to prepare adequate cost sharing schedules that show the personnel time and costs in support of in-kind cost-sharing arrangements as required by the cooperative agreement.

b. Recommendation:

We recommend that Molteno revise its policies and procedures to include adequate timekeeping controls in accordance with OMB Circular A-122, attachment B, paragraph 8.m, Support of Salaries and Wages.

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

4. Unallowable Costs

a. Condition:

Molteno does not have written policies and procedures to segregate and remove unallowable costs prior to billing USAID. For example, during our examination we noted that Molteno billed USAID for employee allowances that are expressly unallowable under OMB Circular A-122, paragraph 8, Compensation for Personal Services, and paragraph 20, Housing and Personal Living Expenses. Lack of written policies and procedures for identifying and segregating unallowable costs increases the risk that unallowable costs will be billed under USAID grants.

b. Recommendation:

We recommend that Molteno prepare written policies and procedures regarding identifying and segregating unallowable costs in accordance with OMB Circular A-122, Cost Principles for Non-Profit Organizations.

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

COMPLIANCE WITH GRANT AGREEMENT TERMS AND APPLICABLE LAWS AND REGULATIONS

Our testing of Molteno's transactions disclosed the following noncompliance conditions. We provided details of the conditions that resulted in questioned costs in exhibit A, page 7 of this audit report.

1. Timekeeping System

   a. Condition:

Molteno does not have adequate timekeeping procedures in place. Molteno employees do not routinely record their time on timesheets to support direct and indirect labor costs. Employees did not consistently utilize timesheets or other records to indicate those agreements/grants to which labor costs should be charged. This is not in compliance with OMB Circular A-122, attachment B, paragraph 8.m, Support of Salaries and Wages, which states:

> *(1) Charges to awards for salaries and wages, whether treated as direct costs or indirect costs, will be based on documented payrolls approved by a responsible official(s) of the organization. The distribution of salaries and wages to awards must be supported by personnel activity reports, as prescribed in subparagraph (2), except when a substitute system has been approved in writing by the cognizant agency. (See subparagraph E.2 of attachment A.)*
>
> *(2) Reports reflecting the distribution of activity of each employee must be maintained for all staff members (professionals and nonprofessionals) whose compensation is charged, in whole or in part, directly to awards. In addition, in order to support the allocation of indirect costs, such reports must also be maintained for other employees whose work involves two or more functions or activities if a distribution of their compensation between such functions or activities is needed in the determination of the organization's indirect cost rate(s) (e.g., an employee engaged part-time in indirect cost activities and part-time in a direct function). Reports maintained by non-profit organizations to satisfy these requirements must meet the following standards:*
>
> > *(a) The reports must reflect an after-the-fact determination of the actual activity of each employee. Budget estimates (i.e., estimates determined before the services are performed) do not qualify as support for charges to awards.*

(b) *Each report must account for the total activity for which employees are compensated and which is required in fulfillment of their obligations to the organization.*

(c) *The reports must be signed by the individual employee, or by a responsible supervisory official having first hand knowledge of the activities performed by the employee, that the distribution of activity represents a reasonable estimate of the actual work performed by the employee during the periods covered by the reports.*

(3) *Salaries and wages of employees used in meeting cost sharing or matching requirements on awards must be supported in the same manner as salaries and wages claimed for reimbursement from awarding agencies.*

Molteno does not have a timekeeping system that meets these standards. As a result, Molteno's direct and indirect labor assertions and/or estimates are not verifiable to auditable records. Therefore, the assertions and/or estimates are not suitable as a basis for cost reimbursement under a USAID grant.

b. Recommendation:

We recommend that Molteno establish a timekeeping system that is compliant with OMB Circular A-122; specifically, employees should record their actual time spent working on a project/cost objective, on a daily basis.

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

2. Salary Allowances

a. Condition:

Several of Molteno's employee benefits are in noncompliance with OMB Circular A-122. Molteno's employee benefits include an allowance for personal use of company vehicles and a housing allowance. These costs are specifically unallowable under OMB Circular A-122, attachment B, paragraph 8, Compensation for Personal Services – Support of Salary and Labor, paragraph 19, Goods or Services for Personal Use, and paragraph 20, House and Personal Living Expenses.

(1) Paragraph 8, Compensation for Personal Services, Organization Furnished Automobiles, states "That portion of the cost of organization-furnished automobiles that relates to personal use by employees (including transportation to and from work) is unallowable as fringe benefit or indirect costs regardless of whether the cost is reported as taxable income to the employees."

(2) Paragraph 19, Goods or Services for Personal Use, states "Costs of goods or services for personal use of the organization's employees is unallowable regardless of whether the cost is reported as taxable income to the employees."

(3) Paragraph 20, House and Personal Living Expenses, states:

(a) Costs of housing (e.g., depreciation, maintenance, utilities, furnishings, rent, etc.), housing allowances and personal living expenses for/of the organization's officers are unallowable as fringe benefit or indirect costs regardless of whether the cost is reported as taxable income to the employees. These costs are allowable as direct costs to sponsored award when necessary for the performance of the sponsored award and approved by awarding agencies.

(b) The term "officers" includes current and past officers and employees.

b. Recommendation:

We recommend that Molteno accumulate these costs separately from their salary costs, and remove them from future billings to USAID unless such costs are specifically approved by the awarding agency.

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

3. Travel Policies and Procedures

a. Condition:

Molteno has written travel policies and procedures. Its official policy regarding per diem rates prescribes specific rates for travel within South Africa and for international travel. In practice, however, Molteno did not apply the prescribed rates for trainers conducting workshops in Ghana. Molteno charged accommodation costs that were higher than the prescribed rate and higher than actual costs incurred. In addition, Molteno charged both the per diem rate as well as the actual costs of meals which should have already been included in the employee's per diem allowance.

Because of this actual practice observed during our audit, Molteno is in noncompliance with its travel policies and procedures and with OMB Circular A-122, attachment B, paragraph 51.b, Lodging and Subsistence. Paragraph 51.b. states:

> *Costs incurred by employees and officers for travel, including costs of lodging, other subsistence, and incidental expenses, shall be considered reasonable and allowable only to the extent such costs do not exceed charges normally allowed by the non-profit organization in its regular operations as a result of the non-profit organization's written travel policy...*

b. Recommendation:

We recommend that Molteno comply with its written travel policies and procedures. In addition, we recommend that the travel costs billed in excess of the Molteno travel rates not be allowed.

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

4. Procurement Policies and Procedures

a. Condition:

We were unable to verify that Molteno solicited bids for goods and services in order to assure that costs were reasonable. Molteno's written procurement policies require that at least three quotations including terms and conditions of the purchase are included with purchase requisitions. Molteno's representatives indicated that although bids were obtained, supporting documentation was not available.

OMB Circular A-110, Paragraph 43 – Competition states:

> *All procurement transactions shall be conducted in a manner to provide, to the maximum extent practical, open and free competition. The recipient shall be alert to organizational conflicts of interest as well as noncompetitive practices among contractors that may restrict or eliminate competition or otherwise restrain trade... Awards shall be made to the bidder or offeror whose bid or offer is responsive to the solicitation and is most advantageous to the recipient, price, quality and other factors considered. Solicitations shall clearly set forth all requirements that the bidder or offeror shall fulfill in order for the bid or offer to be evaluated by the recipient.*

As a result of Molteno's failure to adequately document its compliance with its procurement policies, there is no assurance that costs charged to its USAID projects were at reasonable prices. This condition may have resulted in additional costs charged to the cooperative agreement.

It should be noted that under its current contractual obligations, Maskew, Miller, Longman are the sole supplier of materials used in the Breakthrough to Literacy and Bridge to English programs. Accordingly, it is not obligated to obtain bids for these materials.

b. Recommendation:

We recommend that Molteno comply with its established procurement policies and procedures in order to provide assurance that open and fair competition among vendors is obtained to the maximum extent practical.

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

5. Failure to Identify and Segregate Unallowable Cost

a. Condition:

Molteno does not identify and segregate unallowable costs. Interest charges on credit cards were included in bank charges and housing allowances, and use of organization vehicles for personal use was included as fringe benefits costs. OMB Circular A-122, attachment A, Basis Considerations, states

> *(1) Composition of total costs. The total cost of an award is the sum of the allowable direct and allocable indirect costs less any applicable credits.*
>
> *(2) Factors affecting allowability of costs. To be allowable under an award, costs must meet the following general criteria:*
>
> *Be reasonable for the performance of the award and be allocable thereto under these principles.*
> *Conform to any limitations or exclusions set forth in these principles or in the award as to types or amount of cost items.*

Molteno's interest, housing allowance and personal use of company vehicle costs were not identified as unallowable although they are defined as unallowable in the OMB Circular A-122, attachment B. Failure to properly identify and segregate unallowable costs may result in these costs being charged to the cooperative agreement.

b. Recommendation:

We recommend that Molteno establish written policies and procedures to properly identify and segregate unallowable costs in its general ledger and billings. These unallowable costs must be excluded from any cost proposals, billings, or claims on U.S. government funded projects.

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

6. Failure to Maintain Adequate Supporting Documentation for Incurred Costs

   a. Condition:

Molteno does not maintain adequate supporting documentation for incurred costs. During the course of our evaluation we noted that costs claimed for accommodations were not supported by invoices or receipts. These documents are required by Molteno's written policies and procedures for reimbursement of travel costs incurred. Additionally OMB Circular A-122, attachment A, Basic Considerations, requires that in order for a cost to be considered allowable, it must be adequately documented in the recipients' records. Failure to provide adequate documentation may result in unallowable costs being charged to the cooperative agreement.

   b. Recommendation:

We recommend that Molteno enforce its own written policies and procedures, as well as provide additional training to employees to ensure that employees understand the requirements for adequate documentation of incurred and claimed costs.

   c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

   d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

7. Cost Sharing

   a. Condition:

Section A.8 of the cooperative agreement requires Molteno to expend an amount not less the $47,800 of the total activity costs. Our audit disclosed that a significant portion of Molteno's claimed cost sharing contributions are not verifiable to their books and records as required in Paragraph C.19(c) of the cooperative agreement which states:

> *All contributions, both cash and in-kind, shall be accepted as part of the recipient's cost sharing (matching) when such contributions meet all of the following criteria:*
>
> *(1) Are verifiable from the recipient's records...*

For CFY 2004, Molteno claimed travel days, translation and adaptation labor costs and attendance by Ghanaian officials at Molteno workshops as cost-sharing contributions. The organization's records do not provide adequate supporting documentation for these costs. As a result, those claimed contributions are not verifiable. See exhibit B, page 22, for additional information.

b. Recommendation:

We recommend that Molteno prepare and implement written policies and procedures that provide for adequate documentation of all costs considered to be cost sharing expenses. The supporting documentation must be sufficient to satisfy OMB Circular A-122, as well as requirements of the cooperative agreement(s).

c. Recipient's Reaction:

The recipient concurs with our recommendation and will implement corrective action. Molteno's complete written response is included as an appendix on page 44.

d. Auditor's Response:

Molteno's corrective action should be reviewed at a future date to determine its adequacy.

FOLLOW-UP ON PRIOR AUDIT FINDINGS

During our examination we obtained copies of the audited financial statements for FY 2004 and FY 2003 performed by BDO Spencer Steward (Johannesburg) Inc., Chartered Accountants (South Africa), dated April 25, 2005 and May 2, 2004 respectively. Both reports issued qualified opinions because the auditors:

> "Did not observe the counting of the physical inventories at year end. The project's records did not permit the application of adequate alternative auditing procedures regarding this inventory. Consequently, we (the auditors) did not obtain all the information and explanations we considered necessary to satisfy ourselves as to the existence and valuation of inventory."

In the FY 2003 statements under the heading "Emphasis of matter" the auditors wrote "Without further qualifying our opinion above, we draw attention to the fact that stock count records have not been kept as required by Section 284(I)(e) of the Companies Act in South Africa."

We performed a follow-up review to determine the status of the conditions identified in the report. Section 284 of the Companies Act of South Africa (1973) states:

> *1) Every company shall keep in one of the official languages of the Republic such accounting records as are necessary fairly to present the state of affairs and business of the company and to explain the transactions and financial position of the trade or business of the company, including--*
> *e) statements of the annual stocktaking.*

We reviewed Molteno's polices and procedures that were revised to address the finding discussed in the audits of the financial statements. These procedures set forth specific guidelines for requisitioning stock and for the performance and recording of quarterly stock inventories. The recipient's revised policies and procedures appear to adequately address the matters addressed in the prior audits. However, the recipient did not provide adequate supporting documentation to allow us to verify that the procedures were in effect and that they meet the requirements of Section 284(I)(e) of the Companies Act in South Africa.

AUDIT OF THE FINANCIAL STATEMENTS

USAID requested that an audit of the recipient's organization-wide financial statements be performed if the recipient had been authorized to charge indirect costs. Although authorization to charge indirect costs is not specifically addressed in the cooperative agreement, as discussed in exhibit A, note 6, page 14 of this report, Molteno's budget submitted for approval included the allocation of overhead costs to base salaries in order to develop a fully burdened rate.

During our examination we obtained a copy of the financial statements for FY 2004 performed by BDO Spencer Steward (Johannesburg) Inc., Chartered Accountants (South Africa), dated April 25, 2005. The auditors issued a qualified report because they were unable to extend their examination beyond receipts actually recorded. In addition, they did not observe the counting of the physical inventories at year end. The project records did not permit the application of adequate alternative auditing techniques regarding the inventory. Consequently, they did not obtain all the information and explanations they considered necessary to satisfy themselves as to the existence and valuation of inventory. Except for the effect on the financial statement of those qualifications, the auditors determined that the financial statements fairly present, in all material respects, the financial position of the company at December 31, 2004 and the results of operations and cash flows for the year then ended.

We attempted but were unable to reconcile the financial statements to the recipient's books and records. With the finance/administrative manager's assistance, we reviewed the data originally compiled for the preparation of the financial statements but were unable to determine how the data presented was compiled. Consequently, we were unable to verify conclusively that the financial statements fairly present, in all material respects, the financial position of the company.

As discussed in note 6 of exhibit A on page 14, in order to verify that the overhead rate applied to base salaries was reasonable, we performed transaction tests of significant home office accounts by tracing claimed costs to invoices and payroll documents. We noted no exceptions. Because all direct costs and significant indirect costs were traced to source documents, our inability to verify that the financial statements fairly present, in all material respects, the financial position of the company did not have a significant impact on our audit results in other areas.

RECIPIENT ORGANIZATION AND SYSTEM

ORGANIZATION:

The Molteno Project (Molteno) is a non-profit organization that develops and implements teacher development programs through educational materials in African languages and English. It was established in 1975 as a research and development project of Rhodes University's Institute for the Study of English in Africa. The purpose of the project was to research, develop and implement quality English as a Second Language programs for learners in disadvantaged government schools in South Africa. In 1994, The Molteno Project was incorporated as an association not for gain under Section 21 of the Companies Act of South Africa. At that time Rhodes University conferred the copyrights for its "Breakthrough to Literacy" program to Molteno. From the inception of the project, a legally binding agreement conferring exclusive publishing rights has been in effect with Longman Publishing (now Maskew, Miller, Longman). Based in Johannesburg, South Africa, Molteno has five offices throughout South Africa that attend to local training needs in six provinces. It also currently has programs in Lesotho, Ghana and Malawi. The organization had 49 employees during 2004.

The Board of Directors is responsible for operation of the organization and the effective utilization of funds. All donations are received either for specific projects or to cover the operating expenses of the organization. Donations for operating expenses are reflected in the operating and expenditure account in the year in which they relate. Donations for specific projects are allocated to the relevant project. Revenue in FY 2004 totaled approximately \$2,638,000, which included \$2,110,000 in donations and grants and \$326,000 in royalties received as a result of its development of the language programs.

ACCOUNTING SYSTEM:

We did not examine Molteno's accounting system during the period of performance of the cooperative agreement, fiscal years (FYs) 2003 through 2004. However, we noted certain inadequacies in Molteno's accounting system such as limited segregation of duties in the accounting and finance departments, and timekeeping deficiencies. For further details see exhibit C, Internal Control Structure, note 1, page 27 and note 3, page 28.

Molteno maintains a job cost accounting system using Pastel accounting software. Projects are assigned individual project numbers that are used to accumulate associated direct costs at the cost element level in Pastel. Payroll is also maintained monthly in the Pastel accounting system.

Molteno's fiscal year is January 1 to December 31. Financial statements are audited by BDO Spencer Steward, Chartered Accountants, Johannesburg, South Africa.

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RELEVANT DATES

Date of Request for Audit:	January 4, 2006
Entrance Conference Date:	February 27, 2006
Date of Draft Issuance to USAID	April 18, 2006
Date of USAID Response to Draft	October 5, 2006

AUDIT REPORT AUTHORIZED BY:

/s/
DONNA PELTOMAKI
Branch Manager
DCAA European Branch Office

AUDIT REPORT DISTRIBUTION AND RESTRICTIONS

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RESTRICTIONS

1. Information contained in this audit report may be proprietary. It is not practical to identify during the conduct of the audit those elements of the data which are proprietary. Make proprietary determinations in the event of an external request for access. Consider the restrictions of 18 U.S.C. 1905 before releasing this information to the public.

2. Under the provisions of Title 32, Code of Federal Regulations, Part 290.7(b), DCAA will refer any Freedom of Information Act requests for audit reports received to the cognizant contracting agency for determination as to releasability and a direct response to the requestor.

3. Do not use the information contained in this audit report for purposes other than action on the subject of this audit without first discussing its applicability with the auditor.

RECIPIENT'S LETTER OF RESPONSE

The Word document below includes the recipient's complete written response. The document can be opened for review and printing by double-clicking on the icon below.

MOLTENO PROJECT
Final Response final

Mr. James Athanas
Senior Contracting Officer
U.S. Agency for International Development (USAID)
E45/3 Independence Avenue
P.O. Box 1630
Accrs, Ghana

RE: Management Comments on the Defense Contract Audit Agency (DCAA) AUDIT REPORT NO: 2191-2006U17900003

Dear Sir,

The Molteno Project thanks the Defense Contract Audit Agency (DCAA) for completing their audit field work (March 10th 2006) and draft report (received on August 2nd, 2006) and for giving us the opportunity to respond to your findings. We believe that the audit team performed a very thorough audit and assisted our current financial management team to better understand the various rules, regulations and provisions that govern our Cooperative Agreement.

BACKGROUND

The Molteno project is one of the most successful language and literacy programs in Africa. It started in Rhodes University in South Africa in 1976 and over the past 31 years has helped hundreds of thousands of African children and adults to effectively communicate.

The Molteno Project is a registered Section 21 (Not for Profit) Organization that has successfully partnered with and worked for many large South African and International Donor funding organizations including Irish Aid, the United Nations, various trusts, and DFID.

In 2003, the USAID/Ghana Mission approached Molteno as a result of its reputation for being able to develop and deliver cost effective training projects and programs. Prior to 2003 Molteno had never worked with USAID.

RESPONSE TO FINDINGS

As noted above, the DCAA team members that completed the audit have a very good understanding of the US Government rules and regulations. We have no doubt that they understand how those rules should be implemented on projects such as our Molteno Project. We agree that there are some expenses that were charged that were either legitimately ineligible as per the OMB A-122 requirements or that the internal Molteno procedures were not correctly followed and that such costs should not have been charged to the Cooperative Agreement. For these costs which we identify and discuss below, we agree with the auditors and plan to reimburse USAID.

However, while not disagreeing with any points or findings raised by the audit team, we do have some overarching and specific concerns that we would like to address.

We believe it is important to review the audit findings in the context of how this project was identified and how the CA was signed.

When the USAID/Ghana project was conceived, the USAID Education Team Leader was extremely keen to have Molteno submit a proposal ASAP so that the (pilot) project might start within a month of the initial USAID/Ghana team visit to Molteno in South Africa. She indicated that the proposal process could be fast tracked and suggested that funds be included for activities such as evaluation, project materials, travel/per diems, however there was no suggestion to allocate funds for financial strengthening or audits. Please see attached email dated September 11, 2003 from Lisa Franchett to various recipients. **(Grant Income Communication)**.

The Molteno team did their best to comply with the USAID request to submit documents to get the project up and running as soon as possible.

We believe that it is important to note that there was **no Pre-Award Survey performed on Molteno and no post award financial review or oversight**. No training was ever offered on US Government or USAID policies and procedures (e.g. OMB-A-122 and Mandatory Standard Provisions).

We also believe it is important to note that **nowhere in the Cooperative Agreement is there any mention of Overhead Rates, Indirect Cost Rates, Negotiated Indirect Cost Rates, etc.** to suggest that Molteno would be operating under Indirect Cost Rate rules and regulations. In the Cooperative Agreement Budget, there are only seven Cost Elements or line items namely:

Personnel	$ 95,682
Fringe Benefits	$ 21,815
Travel	$ 74,100
Equipment (Materials)	$239,520
Supplies	$ 11,610
Contractual	$ 3,240

Other direct costs (audit)	$ 2,000
Total Estimated Amount	$447,967

While we are not specialists in USAID audit reporting (and as this was an Agency Contracted Audit) we note that a significant amount of the issues and findings relate to indirect costs and overhead related items. We sincerely disagree with the majority of findings that are essentially based on questioning Molteno's indirect cost rate or overhead rate.

Again, to see this project in context, before this CA, Molteno had never worked with calculated OH or indirect cost rates and only considered such to meet the needs and suggestions of USAID.

From speaking with the original Financial Manager, Rentia Hamilton, who was present during the time of the budget development, it becomes apparent that USAID insisted that Molteno develop the budget in USAIDs format. This deviated significantly from our standard operating procedure and required reliance on USAID for guidance, some of which may not have been completely clear.

For all projects managed by Molteno (including for other International Donors other than USAID) the standard methodology for budgeting, completing and billing projects is on a daily fee basis which includes certain provisions for office/"overhead" expenses. Accordingly, in hindsight, it would have made much more sense to have set up this pilot project under a Fixed Price Contract where the concept of Indirect Costs etc do not apply. As the USAID/Ghana project was our first interaction with USAID, we would have hoped that the Mission would have assisted us to understand the most appropriate method of contracting with it. It is our point of view that the CA was meant to be comparative to how we had operated with all Donors, Companies and Trusts for the prior 30 years and that such concepts as Negotiated Indirect Cost Rates would not be an issue.

However, the Grant Budget was developed (with USAID oversight) to generate a Daily Rate made up of Base Salary costs, normal Fringe Benefits, and then the new concept of "Overhead." At this point in time, we cannot state whether the calculations performed by the existing Financial Manager were correct in terms of DCAA and USG overhead rate calculations but we can certainly state that the daily rates charged on the USAID/Ghana project were not in excess of what had been charged to other major international donors for similar work and we can provide documentary evidence of this.

It was raised by the auditors that the Daily Rate charged by Molteno exceeded what they determined (through what appeared to be an overhead rate audit) to be allowable based on costs. It is our belief that when we calculated the Daily Rate for the budget, and when this was approved, that such Daily Rates were allowable. We believe they are certainly reasonable as this is what other Donors, Companies and Trusts were willing to pay Molteno.

When reviewing the OMB A-122 guidance for Non-Profit Organizations we note that in the very first paragraph under Purpose, it states ***"The principles are designed to provide that the Federal Government bear its fair share of costs except where restricted or prohibited by law."***

We would like to suggest that the Mission/Auditors allow Molteno to use the budgeted Daily Rate as an allowable amount.

The other significant concern we have relates to the issue of timekeeping or timesheets.

We fully accept and understand that the OMB A-122 provides exact criteria for how USAID would like to see their recipients keep records for any and all employees who charge a part or all of their time to a USAID CA. And as noted above, if the Mission would have performed a Pre-Award Survey or any post award reviews we believe that such an exercise would have better enabled the Project to meet USAID specific requirements, however, from reviewing the timesheets that we have on file for the 2003 and 2004 period, we believe that our documentation adequately supports the activities that took place and were charged to USAID.

While our current team who assisted with the preparation of this audit response was not part of the original project financial management, and they were not present during the period of the actual audit, we believe that a significant number of records were not seen by the auditors. It is our understanding that during the period of the audit the existing Molteno Financial Manager, Velile Mqhum, was either not asked or (more likely) did not realise that a significant amount of records existed in the files in his office. This could explain why there are so many findings that state that no timesheets were kept. (Please note that Mr. Mqhum was only the Financial Manger at Molteno for approximately two and a half months before resigning and it is logical that he never fully grasped the contents of all of the various project files.)

As an attachment to this response, we have documented a variety of detailed and summary reports that show that timesheets were in fact kept and that management stressed (as early as March 5th, 2003) that completing timesheets was mandatory **(Time Sheet Register)**. In addition, we found email evidence from June 7th, 2004 to many Molteno employees (including the CEO) that timesheets must be appropriately signed by the employee's immediate supervisor as is required by OMB A-122 **(Timesheet Memo)**. While we agree with the auditors that the format of the timesheets might not be exactly what the OMB requires, we believe that enough documentation exists for a reasonable person to conclude that the time charged to the project is supported by timesheets and/or other original documentation (e.g., written diaries - kept daily)

We are sorry that when the auditors were here that they may not have had access to any or all of the submitted and filed timesheets.

Accordingly, to substantiate our time charges we have performed a Life of Project time analysis for the most significant employees for each of the three categories being: Development & Training (Gloria Mfulathela and Connie Zwane) ; Quality Assurance (Paula Gains); and Administration and Support (Rentia Hamilton and Ivy Selepe) . We attach a copy of the supporting documentation **(Personnel activity Supporting Documentation and Ghana Royalty and Time Reconciliation)** to allow reviewers from USAID to substantiate our work.

Our findings were that for these five employees the time charged on the timesheets correctly matched the time charged on the invoices except for certain activities charged on invoice 4 where time was charged on the weekend when the team was in Ghana doing workshop delivery and school based support. We note that the auditors also mentioned the issue of employees charging time on the weekends. We would like to point out that it was clearly not possible for employees to return home to SA for the weekend and we cannot rule out that they did not, in fact, actually do work on the weekends, however, we will agree that we should not have charged such time and will consider such time to be disallowed. When we calculate the Daily Rate for these employees and apply the days they did not work we arrive at a total of $4,020. We will discuss this again in the detailed section below.

DETAILED AUDIT RESPONSES

We understand that the auditors would like responses to each of the findings as indicated in the report. In this section we attempt to reply to the sections where the DRAFT audit report specifically requested such. As noted above, it would appear that the issue of overhead and indirect rates permeate just about all of the findings and this make it very difficult for us to reply to many of the findings as we disagree that Indirect or Overhead rates should apply to this CA. Again, there is absolutely no mention of Indirect Costs or Overhead rates in the agreement – including the seven budget line items. Accordingly, we implicitly disagree with any finding where Indirect Costs or Overhead Calculations are mentioned.

Page 4 – Section RESULTS OF AUDIT – Fund Accountability Statement

As mentioned above, since the Project disagrees that the audit should have considered indirect cost rates in its findings and as we believe that all of the findings on the FAS have an indirect cost analysis included we cannot comment on the FAS finding as a whole. However, we do accept that they were some duplicate charges to the project or other disallowables which should not have been charged and we will discuss them in the individual findings responses below.

As noted above the auditors findings related to the FAS are developed under the assumption that indirect overhead rates apply. We have already addressed why we do not believe overhead rates are relevant and believe that our discussion above on Daily Rates addresses why we believe our interpretation of the CA is legitimate. Below we explain how we support any amounts that are properly questioned as ineligible.

The only way for us to extract what we believe are ineligible costs is to address the line items notes in the FAS on Draft Audit page 7.

Regarding Reimbursements (Page 8 – item 3)

We attach a series of communications (Income Reconciliation) that indicates that the $3,489.22 never hit the Molteno bank account in South Africa. We can only ask that the USAID/Ghana controllers office continue to work with us on this as we believe that such funds must have been directly spent by USAID/Ghana on some local project activity or else such funds were miscoded. As the Reference and Disbursement information is USAID specific (e.g. MD-641-46411761-MIG-DS-11 (0-1), we must assume that you will have more information than us about where such funds went.

Regarding Personnel Costs (Notes 4, 5, and 6)

The approved Budget as per Section A.4 of the CA shows two line items for time-related activities. Personnel for $95,682 and Fringe Benefits for $21,815.

We have mentioned above our disagreement with Overheads and point out that we do not believe that the FAS should include line items that did not exist in the original Budget.

As detailed above in our opening comments on Daily Rates and then Timesheets, we sincerely believe that if the Mission accepts our justification about Daily Rates and then applies our detailed analysis of actual time spent (based on timesheets) and agreed to invoices submitted to USAID then we believe that our documentation supports $117,497 less the $4,020 (which we identified as weekend time charges and accepted as ineligible) for a total of $113,477.

Molteno agrees that **$4,020** is ineligible.

Regarding Travel Costs

Molteno accepts that the Airfare Cost of **$1,480** can be questioned as this related to a airfare cost for a trip that had to be cancelled. We also accept and agree that the VAT exemption might have been able to have been obtained but believe that VAT issues for work performed on activities outside of South Africa can be very difficult to obtain and time consuming. Accordingly the VAT amount of **$332** is accepted to be disallowed.

However, on the ineligible and unsupported Accommodation and Per Diem claims we believe that now that we have found the timesheets that adequate documentation exists. As noted above, we performed an extensive Life of Project analysis for documenting time charged for five significant employees and found that except for certain weekend time charges, the documentation adequately supported the invoiced time. We believe that the same applies to the Accommodation and Per Diem claims and request that the Mission agree with this.

Molteno agrees that **$1,480 and $332** totalling **($1,812)** is ineligible.

Regarding Other Direct Costs – Note 9

As noted above we accept that VAT is a problem for USAID and while we believe we would have struggled to obtain a VAT exemption we will accept that the charge **($57)** is ineligible. Regarding the questioned costs of excess baggage (for the two trainers carrying training materials) and the rental car documentation, we have found the rental car receipt payment and attach it here **(Excess Baggage Documentation & Invoice Car Rental)**. We hope that you can appreciate that excess baggage processing – frequently at the last minute can be trying - and receipts, especially for cash payments might be difficult to obtain. Our people were certainly on the job and laden with materials.

Cost Sharing (Exhibit B)

When trying to substantiate our In-Kind Contributions we essentially attempted to find enough contributions to satisfy our required amount. Rather than trying to justify our original amounts, one of which we believe is justified as noted further below, we rather identify a clear and supported contribution that, according to CA Standard Provision C.19 guidelines, is allowable.

For all of the printing costs that the Molteno project incurs, there is a fee that the authorized and USAID-recognized (due to long-standing legal requirements) printer charges for such work. For the Molteno project, the Molteno CEO negotiated a special 5% fee discount which was passed on to USAID. The documentation of the fee agreement and the Cost Sharing calculation are attached **(Ghana Royalty + Cost Sharing Documentation)**. The total value of this contribution was $13,956.88.

The other major contribution which we now have complete support for is the 91 work days for the trainer, Johanna Mogodiri. The financial management team sat with Johanna and her personal diary and documented each of the 91 days as per the attached schedule. **(Cost Sharing Documentation 1)**. We calculate the value of this to be $7,714.

The total of these two items raises the contribution to more than the required $47,800.

Internal Control Findings

The auditors identified four findings on Internal Controls which they deemed to be reportable conditions.

We generally agree with their findings and believe that by implementing the recommendations of finding number two (Training), we will then be better able to address the other three findings.

As noted in the opening paragraphs of this letter, Molteno never had the benefit of a Pre-Award Survey or a follow up financial review. These activities would have gone some way towards providing the training mentioned in the finding. Through the audit process we were exposed to the requirements of the OMB A-122 requirements and now have a greater appreciation of the level of detail that financial managers need to know as well as the extent of policies and procedures that need to be implemented to become financially compliant.

Molteno agrees to identify a capable accounting or consulting firm to work with us to learn the OMB A-122 requirements so that all of the USAID requirements can be met. We believe that such consultants will assist us to implement the other three recommendations which were:

(1) Segregation of Duties
(3) Timekeeping Controls; and
(4) Unallowable Costs

Regarding the Segregation of Duties issue, we would like to highlight that Molteno is currently operating under extreme cost pressures so the likelihood of hiring additional staff is out of the question. Accordingly, we believe that we will need to restructure how our current financial staff operate and possibly utilize the services of the CEO or other senior officers to provide approvals or oversight.

Compliance with Grant Agreement Terms and Condition Findings

We note that the auditors identified seven non-compliance conditions as listed below:

1. Timekeeping System
2. Salary Allowances
3. Travel Policies and Procedures
4. Procurement Policies and Procedures
5. Failure to Identify and Segregate Unallowable Cost
6. Failure to Maintain Adequate Supporting Documentation for Incurred Costs
7. Cost Sharing

Regarding timekeeping systems, we believe that the auditors did not necessarily see all of the then existing timesheets but certainly agree with their findings. We certainly understand the need to have detailed documentation for every employee who charges all or part of their time to a USAID project. We also understand the need to have such timesheets approved by an official who can vouch that the activities were actually performed by the employee. We have bought into the concept of timesheets and systems to support an indirect cost rates.

Regarding Salary Allowances we understand that while Molteno may have in-house policies that may differ from USAID policies, we need to be able to identify and exclude any expenses that are not allowable under OMB A-122 cost principles.

Regarding Travel Policies and Procedures we understand that the OMB A-122 policies provide clear guidance on what the procedure should be and we intend to review our policies in that light.

Regarding Procurement polices we agree with your recommendations and will continue to demand quotes to ensure that reasonable and arms-length prices are obtained.

Regarding Failure to Identify and Segregate Unallowable Costs we will we first ensure that we understand the issues around allowable and allocable costs, especially regarding Fringe Benefits, and then consider how to change our accounting systems, if necessary to properly reflect/segregate disallowed costs.

Regarding the Failure to Maintain Adequate Supporting Documentation for Incurred Costs we recognize that it is our duty and responsibility to be able to adequately support all charges to USAID contracts. We need to develop or improve our systems and methodologies and train our people to meet USAID's needs. If the South Africa Mission will have a training session we will certainly send our Finance staff.

Regarding Cost sharing we will review the guidance in the Mandatory Standard Provisions and ensure that our methodology for documenting shared costs is compliant.

As mentioned in the Internal Controls section above, we would like to highlight that Molteno is a very lean organization which does not have any general budget support. It exists from year to year and is currently working on extremely tight budget constraints. Any payback of significant funds to USAID would cause very serious financial strain and might force the closure of the organization which has been successfully operating for over 30 years now.

From speaking with your Project and Program officers you will be able to confirm that together, the USAID/Ghana and our Molteno team's developed and delivered a highly successful pilot project. We would hope that the Mission and/or RIG would consider the successful outcomes of this project when making your determination.

Finally, we would again like to thank USAID for giving us the opportunity to be your cooperative partner.

If you have any questions or require additional information please feel free to call me at any time.

Sincerely,

Masennya Dikotla
Chief Executive Officer