OFFICE OF INSPECTOR GENERAL

USAID/EL SALVADOR NEEDS TO IMPROVE ITS MANAGEMENT OF THE REGIONAL TRADE AND MARKET ALLIANCES PROJECT TO ACHIEVE EXPECTED RESULTS

AUDIT REPORT NO. 1-519-17-001-P
October 28, 2016

SAN SALVADOR, EL SALVADOR

Office of Inspector General

October 28, 2016

MEMORANDUM

TO: USAID/El Salvador Mission Director, Lawrence J. Sacks

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

SUBJECT: USAID/El Salvador Needs to Improve Its Management of the Regional Trade and Market Alliances Project to Achieve Expected Results (Report No. 1-519-17-001-P)

This memorandum transmits our final report on the subject audit. Our objective in performing the audit was to determine whether the project was achieving its expected results related to increasing market access for growers and sellers of value-chain products vital to food security, facilitating trade, and building institutional capacity. In finalizing the report, we considered your comments on the draft report and included them in their entirety, excluding attachments, in Appendix II.

The report contains 13 recommendations to help you improve USAID/El Salvador's Regional Trade and Market Alliances Project. After reviewing information provided in response to the draft report, we acknowledge management decisions on 12 recommendations and final action on recommendations 1, 2, 4, 5, and 8. Please provide evidence of final action to the Audit Performance and Compliance Division. Recommendation 12 is open pending determination by February 28, 2017, of the allowability of questioned costs.

Thank you and your staff for the cooperation and assistance extended to us during this audit.

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SUMMARY OF RESULTS

Central America faces major development challenges, including high levels of poverty and hunger and limited market access for poor farmers.[1] The United States has helped by promoting free trade in Central America for more than a decade and by making several countries in the region the focus of its Feed the Future initiative to reduce poverty and hunger.

USAID supports both efforts through the Regional Trade and Market Alliances Project based in El Salvador. To implement the project, in April 2013 USAID/El Salvador awarded Nathan Associates Inc. (Nathan) a 3-year, $15.2 million contract with a 2-year option to support regional trade in selected agricultural products.[2] The project's activities focus primarily on Guatemala, Nicaragua, Honduras, and El Salvador. As of June 30, 2015, USAID/El Salvador had obligated $14.1 million and disbursed $5 million for the project.

The project awarded 21 grants—18 to producers of honey, plantains, beans, cacao, mixed vegetables, and potatoes and 3 to regional organizations involved in trade facilitation. The grants to producers, valued at $5 million, were to improve the quality of their products to increase demand for them in regional markets, boost sales, and raise growers' incomes, thereby combating hunger.

Grants to regional organizations, worth $1.2 million, were to strengthen their ability to facilitate trade. The grants support coordination between public and private sector actors, training, and the development of a system that would provide logistical information, such as transport time and cost, to users in Central America.

A second activity was facilitating trade through regulatory reform. The project helped ease border crossings by encouraging the use of cameras and radio frequency devices and by coordinating immigration controls. Further, it provided training to customs officials and private sector organizations in areas such as strategic planning and improving processes at border crossings.

A third activity was providing technical assistance in strategic planning to La Secretaría de Integración Económica Centroamericana (the Central American Secretariat of Economic Integration, known as SIECA).

The project's primary performance indicators and targets were:

- Establishing 20 alliances between small producers and regional buyers, guaranteeing the producers greater market access.
- Increasing the value of exports of supported producers by at least 15 percent.
- Reducing transaction costs including transportation for selected products by 5 percent.

[1] The regional poverty rate was 28 percent, and rates of hunger were in the teens for all but Costa Rica, Mexico, and Panama, according to *Regional Overview of Food Insecurity: Latin America and the Caribbean,* Food and Agriculture Organization of the United Nations, 2015. The report includes Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, and Panama in Central America.
[2] The audit covered the first 2 years of the contract, from April 2013 to June 2015. USAID stated that on September 29, 2015, it extended the contract to April 2018 and increased the value to $19 million.

The Office of Inspector General (OIG) conducted this audit to determine whether the project was achieving its expected results related to increasing market access for growers and sellers of value-chain products vital to food security, facilitating trade, and building institutional capacity.[3]

We found the project was not achieving expected results, having underperformed on the above indicators and targets. During the first 2 years of implementation, the mission did not manage the project to achieve its market Alliance and export goals; it faced delays in awarding grants and purchasing equipment, the primary activities intended to achieve the performance targets.

In addition, the project had achieved no measureable progress on reducing transaction costs in selected value chains, important for trade facilitation. While the project prepared baselines for this indicator and supported some activities that contributed to it, Nathan had not yet reported any data to indicate whether it would achieve its cost-reduction goal. Because the project was still collecting data in this area, we are not making a specific recommendation related to this issue.

The project had made more progress on building institutional capacity. At SIECA, staff expressed appreciation for the support they had received from the project, noting it had assisted them with developing administrative manuals and doing strategic planning.

The audit identified the following challenges that require USAID/El Salvador's attention:

- The project had not made appreciable progress on its market alliance and export goals (page 4). As of June 30, 2015, after expending $5 million and with just over 9 months remaining, the project had helped establish 1 of an expected 20 alliances and made no measureable progress on increasing exports by 15 percent. The producers of the selected agricultural commodities need these alliances to sell their products to regional buyers.

- The contractor did not consider nutrition and income in selecting products for export (page 5). Instead, Nathan considered products based on variables like market potential and private sector interest. Thus, the project may not have the intended impact on income and nutrition.

- The mission did not verify that the project met performance monitoring and data quality standards (page 6). The indicator measuring increased exports was not valid because many producers had never exported at all. Another indicator also was invalid, and the project did not document the rationale for targets.

- The project did not implement activities in the Dominican Republic (page 7).The USAID mission director there decided the project's activities did not align with the mission's strategy. We were unable to confirm whether the bureau in Washington that oversees this region endorsed this decision.

Auditors also found that the contractor did not follow Federal regulations for awarding consulting work (page 9). Nathan awarded $172,570 in contracts for grant monitoring and SIECA support

[3] Value chains include all the activities required to turn inputs into products and deliver them to the final customer. The value chain approach "seeks to understand...an industry—from input suppliers to end market buyers…and the business environment in which the industry operates." https://www.microlinks.org/good-practice-center/value-chain-wiki/overview-value-chain-approach.

but did not follow regulations related to competition, documentation of negotiation, and avoidance and mitigation of conflicts of interest.

To address these issues, we recommend that USAID/El Salvador:

1. Work with Nathan Associates Inc. to implement a plan to help producers address obstacles noted by regional buyers (page 5).

2. Implement a plan for timely delivery of equipment that will allow adequate time for grantees to achieve their export goals (page 5).

3. Document a plan to measure the impact of interventions on nutrition and incomes for small farmers supported by the project (page 6).

4. Review and document the value chains chosen, to determine whether they met nutrition and income criteria established in the contract, and make adjustments as appropriate (page 6).

5. Document a meaningful indicator to measure the project's impact on supported producers (page 7).

6. Document the project's rationale for expected targets, and make adjustments as appropriate for the remainder of the activity (page 7).

7. Develop written instructions to staff requiring documentation of targets in line with USAID policy (page 7).

8. Instruct Nathan Associates Inc. to verify the number of small producer units that will participate in export value chains supported by the project (page 7).

9. Develop a joint training program for technical officers and the monitoring and evaluation specialist to review their shared responsibilities for performance monitoring and data quality, as described in the January 2014 mission order (page 7).

10. Formally request that the Bureau for Latin America and the Caribbean review and issue a written decision on the curtailment of project activities in the Dominican Republic (page 8).

11. Perform a financial review of Nathan Associates Inc. to determine whether its systems meet acquisition requirements (page 10).

12. Determine the allowability of $172,570 in ineligible questioned costs for consulting contracts that did not follow regulations, and recover from Nathan Associates Inc. any amount deemed unallowable (page 10).

13. Issue written instructions to the contracting officer's representative regarding proper procedures for contract approvals (page 10).

Detailed findings appear in the following section, and Appendix I describes the audit scope and methodology. Management comments appear in their entirety minus attachments in Appendix II, and our evaluation of them begins on page 11.

AUDIT FINDINGS

Mission Did Not Manage Project To Achieve Market Alliance and Export Goals

Establishing alliances between producers and regional buyers and increasing exports are critical components of the project. USAID/El Salvador's 2011-2017 Regional Integrated Trade and Food Security Strategy noted, "These alliances have proven to be win-win approaches that improve quality and consistency of supplies for buyers and facilitate technology transfer and predictability of market conditions for growers." The contract sought to build 20 such alliances between regional buyers and small producers, of which at least 5 would result in signed contracts. The monitoring and evaluation plan projected that 2 years into the contract, the project would have helped establish 16 alliances and signed 12 contracts. For exports, the contract set a goal to increase export sales for supported producers by at least 15 percent by April 2016.

As of June 2015, despite working with 21 regional buyers and helping producers attend regional trade events, Nathan officials could point to only 1 signed contract. It was an agreement between a regional buyer of red beans and producers in Guatemala, El Salvador, and Nicaragua.

Further, project-supported producers had yet to export their products. While the project had awarded grants worth about $5 million in early 2015 to producers for export, it had reported no sales. In addition, the project had not yet delivered the equipment it promised to grantees for increasing the value of their products. For example, the project planned to procure equipment to wash, dry, refrigerate, process, and package commodities, thereby adding value and increasing exports.

Several factors explain the limited progress. Project officials cited delays in grant awards as one. According to the year 2 work plan, the project should have awarded the grants by September 2014 but did not until early in 2015. A USAID official suggested that challenges in finding producers interested in the grants also caused delay. Further, the audit found that delays in the procurement of equipment pushed back delivery dates to late 2015 and early 2016, and the project still had not procured all of the equipment. USAID officials admitted they might have overestimated what they could accomplish in the first 2 years of the project, and the delays further aggravated progress.

In addition, auditors spoke with multiple buyers in Guatemala, Honduras, and Nicaragua who observed many challenges in establishing alliances with project producers. For example, a buyer in Guatemala claimed a lack of producers who could provide a steady product supply for the entire year. Another buyer said that many small producers could not reliably deliver a consistent, quality product and did not have the business structure or culture needed for success. In Nicaragua, the project linked a company to a local cacao producer; however, the producer's low production made its product uncompetitive. The buyer said, even with product assistance, he did not believe the producer would harvest enough cacao to export before the end of 2016.

USAID has already acted on some of these problems. Recognizing that the lack of measurable progress toward establishing market alliances and increasing exports limits the opportunities to sustainably reduce poverty and hunger, USAID exercised the option period, which will give the project more time to achieve its goals. Further, mission officials told us after fieldwork that producers and buyers had signed additional alliances.

To address the other issues, we make the following recommendations.

> ***Recommendation 1.*** *We recommend that USAID/El Salvador work with Nathan Associates Inc. to implement a plan for helping producers overcome obstacles noted by regional buyers.*

> ***Recommendation 2.*** *We recommend that USAID/El Salvador, in coordination with Nathan Associates Inc., implement a plan for expediting delivery of equipment that grantees need to achieve their export goals.*

Contractor Did Not Consider Nutrition and Income in Selecting Products for Export, as Required

The contract required Nathan to choose products for export (or value chains)[4] using the following criteria:

- Benefit to small producers.
- Job opportunities for women in rural areas.
- Improvement of farmers' incomes and those of poor rural inhabitants.
- Improvement of the region's food security and nutrition.
- Achievement of a multiplier effect on investment.

Yet Nathan did not consider nutrition and income. A report prepared in December 2013 indicated that project officials chose 26 agricultural commodities to review, and narrowed this list to 13 based on factors such as market growth potential, private sector interest, comparative advantage, policy, and infrastructure. They then considered the 13 in terms of the job opportunities they would offer women and youth, and narrowed the list again to eliminate products like eggs, because of its limited growth potential in the region. Eventually, officials selected honey, plantains, beans, cacao, mixed vegetables, and potatoes.

After the selection, the mission prepared an analysis to support the value-chain selection. It said these selections would support income-generating potential for poor households through growth in rural, small businesses. However, this analysis did not address the nutrition and income benefits of each potential commodity. Moreover, the analysis did not reveal that Nathan changed its selection criteria. In its proposal, Nathan included factors like nutrition, which it used to rate horticulture, dairy products, beans, and fruit as having high potential while rating cacao "marginal." However, Nathan's final selections belie these criteria.

Because Nathan did not consider the factors as it should have, the project may not have the intended impact on nutrition and income. What's more, the project will have difficulty measuring

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[4] Since it supports not just production of these commodities but also regional marketing and distribution, the project targets value chains—all the activities needed to convert inputs to outputs.

that impact since it did not collect baseline data showing income and nutrition levels prior to the project. Therefore, we make the following recommendations.

> ***Recommendation 3.*** *We recommend that USAID/El Salvador document a plan to measure the impact of value-chain interventions on nutrition and income for small farmers supported by the project.*

> ***Recommendation 4.*** *We recommend that USAID/El Salvador review and document the choice of value chains to determine whether they met the nutrition and income criteria established in the contract and make adjustments as appropriate.*

Mission Did Not Verify That Project Met Performance Monitoring and Data Quality Standards

According to Agency policy, performance monitoring is "the ongoing and routine collection of performance data to reveal whether desired results are being achieved and whether implementation is on track." The project should collect valid data—data that "clearly and adequately represent the intended result" and set "ambitious, but achievable" targets," being sure to document the thought process behind them.[5]

To codify ADS, in January 2014 USAID/El Salvador issued Mission Order 203. It makes the mission's monitoring and evaluation specialist "responsible for compliance with and implementation of USAID regulations and guidance referring to performance management and monitoring." The mission order also requires technical officers to review and approve monitoring and evaluation plans, conduct site visits, and analyze reported data to ensure they meet standards; if not, these staff are to determine if improvements are needed. Together, these requirements ensure that data are accurate and useful in assessing project performance.

The audit found the following problems with indicators, targets, and data:

- One project indicator was supposed to measure the percentage increase in export value, and its target was 15 percent; since most producers had never before exported, both the indicator and the target were flawed.

- The target for the number of small producer units participating in regional and export value chains was 1,500. A USAID official said various offices, including the technical and contracting offices, had set the target during a brainstorming session but did not document how. A project official said the initial assumption was that the project could support 500 small producer units per country in Honduras, El Salvador, and Guatemala. Later, officials added Nicaragua without adjusting the target.

- In June 2015 the project reported supporting 7,412 small producer units, but officials explained that figure was total small producer units, not necessarily ones that participated in regional and export value chains. A Nathan official called this figure a forecast that Nathan would adjust in later reports. As such, it was invalid.

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[5] Automated Directives System (ADS), "Assessing and Learning," effective 11/02/2012, sections 203.3.2 and 203.3. This guidance was in effect at the time of the audit.

These weaknesses occurred because officials did not monitor performance and ensure data quality. According to a mission official, USAID/El Salvador did not train staff to ensure that they understood their responsibilities under the new mission order and that technical officers and the mission monitoring and evaluation specialist worked together to ensure compliance with all Agency requirements.

As a result of these monitoring and evaluation weaknesses, USAID cannot determine the extent to which project activities have helped producers. To address these issues, we make the following recommendations.

> ***Recommendation 5.*** *We recommend that USAID/El Salvador document a meaningful indicator to measure the project's impact on supported producers.*
>
> ***Recommendation 6.*** *We recommend that USAID/El Salvador document the rationale for expected targets for the Regional Trade and Market Alliances project and make adjustments as appropriate for the remainder of the activity.*
>
> ***Recommendation 7.*** *We recommend that USAID/El Salvador develop written instructions to staff requiring them to comply with USAID policy by documenting targets.*
>
> ***Recommendation 8.*** *We recommend that USAID/El Salvador instruct Nathan Associates Inc. to verify the number of small producer units participating in regional and export value chains supported by the project.*
>
> ***Recommendation 9.*** *We recommend that USAID/El Salvador develop a joint training program for technical officers and the monitoring and evaluation specialist to review their shared responsibilities for performance monitoring and data quality, as described in Mission Order 203.*

Project Did Not Implement Activities in the Dominican Republic

The project planned to support training, capacity building, and workshops for the Government and the private sector in the Dominican Republic, one of seven countries the contract covered. These activities focused on border management, customs, and logistics for getting perishable goods to market.

According to USAID/El Salvador, the exact activities would depend on requests from the Dominican Government and groups in the region. In multiple e-mail messages, both SIECA and Government officials requested trade-related support from the project, including assistance with performing studies. A USAID/El Salvador official said the project planned to spend about $250,000 to comply with those requests.

However, the project did not perform the planned activities because the USAID/Dominican Republic's mission director felt they did not align with the mission's development strategy. Because USAID had dropped the Dominican Republic from the Feed the Future initiative, the mission did not include agriculture or trade activities in its strategy, and the mission director expressed concern that the project activities might confuse counterparts. She said the Bureau for Latin America and the Caribbean had approved the decision, but she could not provide any document showing approval.

Removing the Dominican Republic from the scope of the project will reduce its impact on regional trade. Therefore, we make the following recommendation.

> ***Recommendation 10.*** *We recommend that USAID/El Salvador formally request that the Bureau for Latin America and the Caribbean review and issue a written decision on the curtailment of project activities in the Dominican Republic.*

OTHER MATTER

Contractor Did Not Follow Federal Regulations for Awarding Consulting Work

Part 6 of the Federal Acquisition Regulation (FAR) contains requirements related to competition and the justification for not competing awards. According to the FAR, the Government "shall promote and provide for full and open competition" except under certain situations and with justification. However, the exception to competition must include both a "description of efforts made to ensure that offers are solicited from as many potential sources as is practicable" and a "description of the market research conducted or [reasons why it was not performed]." Both the FAR and Nathan's internal policies require a memorandum documenting the negotiation process between Nathan and any contractors it selects to help it implement projects. To prevent organizational conflicts of interest, both the FAR and USAID policy preclude a contractor from implementing an activity if the contractor had a "substantial role" in its design.

The contractor awarded multiple contracts to consultants associated with a single consulting firm in Guatemala and to the firm's subsidiary. The table below details the awards.

Project Contracts Nathan Awarded to a Guatemalan Firm, Its Subsidiary, and Its Consultants

Main Purpose	Awarded Competitively?	Value
Develop a grant-monitoring system	No	$19,800
Implement a grant-monitoring system	Yes	$78,750
Implement a system for strategic planning at SIECA	No	$74,020
Total		**$172,570**

Source: Prepared by OIG with award amounts from the project.

However, Nathan did not follow regulations when awarding these contracts. Auditors identified the following problems:

- **No valid exception to competition.** In January 2014, Nathan awarded a $19,800 contract to develop a grant-monitoring system. To justify awarding the contract noncompetitively, project officials said no other company in Central America had rights to the firm's strategic planning methodology, and therefore no other company could develop an effective monitoring system.

  Nathan later awarded noncompetitive contracts totaling $74,020 to four consultants working for the same firm to help implement a strategic planning system at SIECA. Nathan officials recommended the consultants to SIECA because they felt the consultants' methodology was superior—although the officials considered no other approaches. Nathan officials' assessment that the methodology was superior was not documented and they did no market research.

- **No documentation to support negotiation.** Nathan did not adequately document its negotiations for the monitoring contracts. Despite the requirement to prepare negotiation memorandums, Nathan could not provide the audit team with them or with Nathan's methods for determining fair and reasonable prices for these two contracts. Given that the amounts awarded matched the amounts in the contractor's initial proposals, Nathan does not appear to have negotiated these contracts.

- **No measures to address potential conflict of interest.** Nathan awarded a $78,750 contract to the parent firm for the implementation of the grant-monitoring system. Although the award was subject to competition, since the subsidiary firm had a "substantial role" in developing the system, Nathan should have taken action to avoid a potential conflict of interest.

These problems occurred because Nathan favored the strategic planning methodology used by the primary firm. A Nathan official explained that he studied under one of the developers of the monitoring system and had seen it implemented in other organizations successfully. Because of this, the official approached the firm to submit a proposal for the development contract and later awarded work to the firm's consultants to support SIECA.

The USAID contracting officer only reviews and approves subcontracts over $150,000. In this case, since the individual awards fell below that, they did not require consent. Nevertheless, Nathan mistakenly asked the contracting officer to approve the initial award to the firm, and the contracting officer's representative, who lacked authority to approve it, did so. That action was inappropriate since Nathan was subject to FAR and USAID requirements.

As a result of this flawed award process, Nathan gave multiple awards totaling $172,570 to consultants associated with a Guatemalan firm, the firm itself, and its subsidiary. Although USAID believes that the consultants are providing useful and effective services, the awards did not comply with U.S. Government requirements, making these costs potentially ineligible. To address these issues, we make the following recommendations.

Recommendation 11. *We recommend that USAID/El Salvador perform a financial review of Nathan Associates Inc. to determine whether its systems meet acquisition requirements.*

Recommendation 12. *We recommend that USAID/El Salvador determine the allowability of $172,570 in ineligible questioned costs for consulting contracts that did not follow acquisition regulations, and recover from Nathan Associates Inc. any amount deemed unallowable.*

Recommendation 13. *We recommend that USAID/El Salvador issue written instructions to the contractor officer's representative on the proper procedures for contract approvals.*

EVALUATION OF MANAGEMENT COMMENTS

The mission agreed or partially agreed with 12 of the 13 recommendations. We acknowledge management decisions on 12 of the 13 recommendations and final action on recommendations 1, 2, 4, 5, and 8. An evaluation of management comments follows.

Recommendation 1. The mission agreed to implement a plan to help producers overcome obstacles noted by regional buyers and noted that the project's second and third year work plans contained capacity-building activities that would address those obstacles. In addition, mission officials noted that after the audit fieldwork, the project had helped establish 20 additional market alliances. Having reviewed the documents provided, including a trade alliance strategy, we acknowledge the mission's management decision and final action.

Recommendation 2. The mission agreed to expedite equipment deliveries and has implemented a plan to expedite the delivery of equipment to producers. After reviewing the documents provided, we acknowledge the mission's management decision and final action.

Recommendation 3. The mission partially agreed, consenting to implement a plan to measure the overall impact of value-chain interventions on incomes—not on nutrition—of small farmers supported by the project. Mission officials planned to contract a survey in the communities assisted by the project to understand how project interventions have affected households and "to what extent investment, and direct and indirect employment opportunities have contributed to improve household incomes." The mission gave a target completion date, later revised, of February 28, 2017. We acknowledge the mission's management decision.

Recommendation 4. The mission disagreed with documenting the choice of value chains to see if those chosen met nutrition and income criteria, stating that household nutrition and incomes are outside the scope of the project. Mission officials defended the choice of value chains—which the contractor documented in the project's Phase I Final Report, issued December 19, 2013—and stated that higher sales for supported producers would improve small farmers' incomes and provide food security in the region. Therefore, the mission decided that no action was necessary.

Given the mission's response and the limited future benefit to performing this review this late in the project's life, we acknowledge a management decision and final action. We do, however, suggest that the mission, if any future value chains or products are chosen for export under the project, that it clearly instruct Nathan what criteria is mandatory for them to consider.

Recommendation 5. The mission agreed to create an indicator to measure the project's impact on supported producers and noted that, in addition to indicators being reported quarterly, the contractor is tracking 16 additional indicators covering areas such as job creation, export value, and return on investment. The mission provided a copy of these indicators with results as of December 2015. Having reviewed the documents provided, we agree that they will provide adequate information about the project's impact on supported producers. Therefore, we acknowledge the mission's management decision and final action.

Recommendation 6. The mission agreed to document targets. The mission stated that it would work with the contractor to update the project's monitoring and evaluation plan to include a rationale for targets. It gave a target completion date, later revised, of October 30, 2016. We acknowledge the mission's management decision.

Recommendation 7. The mission agreed to issue written instructions to staff regarding the requirement to document targets. It gave a target completion date, later revised, of March 31, 2017. We acknowledge the mission's management decision.

Recommendation 8. The mission agreed to instruct the contractor to verify the number of small producers participating in export value chains. The contractor revised the reported number of small producers participating, from 7,412 to 3,784. We reviewed the project's quarterly report as of December 2015 and verified that the adjustment was made. We acknowledge the mission's management decision and final action.

Recommendation 9. The mission agreed to conduct training for technical officers and monitoring and evaluation staff to explain Mission Order 203. It gave a target completion date, later revised, of April 30, 2017. We acknowledge the mission's management decision.

Recommendation 10. The mission agreed to ask the Bureau for Latin America and the Caribbean to review and issue a written decision on the curtailment of project activities in the Dominican Republic by December 31, 2016. We acknowledge the mission's management decision.

Recommendation 11. The mission agreed to perform a financial review of Nathan Associates Inc. and determine whether its systems meet acquisition requirements. The mission planned to send a letter to the contractor directing it to prepare a corrective action plan in response to the audit findings. Later, the mission said, the Office of Acquisition and Assistance would conduct a financial review. It gave a completion date, later revised, of June 30, 2017. We acknowledge the mission's management decision.

Recommendation 12. The mission agreed to determine the allowability of questioned costs pending a review of procurement processes and, if required, market research. The estimated date of the determination is February 28, 2017. Because the determination is pending, a management decision has not been reached.

Recommendation 13. The mission agreed to provide guidance to the contracting officers' representative outlining best practices for approvals under the contract. It gave a target completion date, later revised, of December 31, 2016. We acknowledge the mission's management decision.

SCOPE AND METHODOLOGY

Scope

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

The purpose of this audit was to determine whether USAID/El Salvador's project was achieving its goals of improving trade facilitation, institutional capacity building, and market access in value chains vital to food security.

The audit covered the project's activities from inception to June 30, 2015. As of June 30, 2015, USAID/El Salvador had obligated $14.1 million and disbursed $5.0 million for the activities implemented in Panama, Costa Rica, El Salvador, Honduras, Nicaragua, and Guatemala. The disbursed amount represents the amount tested during this performance audit.

In planning and performing the audit, we researched information on regional trade activities in Central America. We examined award documents and amendments, work plans, the monitoring and evaluation plan, quarterly progress reports, and other assessments performed by the project. We also reviewed relevant legal and policy criteria such as the Bumpers Amendment, the Federal Acquisition Regulation, and USAID policies governing business analysis, direct contracting, performance monitoring, data quality, and organizational conflicts of interest. In addition, we studied planning and strategy documents such as USAID/El Salvador's 2011-2017 Regional Integrated Trade and Food Security Strategy, documentation supporting review of environmental compliance, and a gender assessment.

We performed the audit from May 4 to November 13, 2015. We conducted fieldwork at USAID/El Salvador and Nathan in San Salvador. In addition, the audit visited grantees, regional buyers, consultants, and Government officials in Guatemala (May 19-22), El Salvador (May 26-May 27), Honduras (July 6-8), and Nicaragua (July 9-10). The audit team also visited the border crossing at El Amatillo between El Salvador and Honduras. Finally, we spoke with an agent of the Office of the U.S. Trade Representative via telephone.

Methodology

To answer the audit objective, we assessed controls and procedures that USAID/El Salvador had to provide contract oversight. We reviewed USAID/El Salvador's 2011-2017 Regional Integrated Trade and Food Security Strategy to get an understanding of the overall goals of regional trade activities and the project's expected contributions to these goals. From this, we studied the project indicators used to monitor progress and the results reported through June 30, 2015.

We met with mission officials and discussed the design of the project, the contractor selection process, and the mission's daily monitoring and approval of activities. We spoke with a USAID lawyer about the legal and regulatory requirements that affect the project. We also met with

USAID/El Salvador officials from the contracting and strategic development office to learn more about USAID and federal policy regarding performance monitoring and acquisition. We visited the mission's financial management office to find out about the controls in place for approval of payments and oversight of the contractor's cash burn rate.

We met with the contractor and partners supporting project activities. In our meetings with Nathan, we learned more about project activities and the contractor's internal processes for activity monitoring, financial oversight, and monitoring of grants and subcontracts. During audit fieldwork, we met with selected grantees, including producers, Chambers of Commerce, and other development organizations supporting trade. To get the perspective of regional buyers, we spoke with various buyers of agriculture commodities, such as Walmart and Unispice in Guatemala and Tesoros de Nicaragua in Nicaragua. To get an understanding of institutional capacity-building activities, we met with SIECA and its consultants. To assess coordination of activities, we corresponded with USAID missions in Nicaragua, Guatemala, Honduras, and Dominican Republic, and we spoke with an agent at the Office of the U.S. Trade Representative. Finally, we met with customs officials in El Salvador who received training from the project.

We reviewed project indicators designed to measure progress on the following goals:

- To increase the value of exports of targeted agricultural commodities by at least 15 percent as a result of U.S. Government assistance.

- To establish 20 alliances that link small producers to regional buyers.

- To reduce transaction costs for supported producers.

We also assessed other output indicators, including the number of small producer units that the project supported and the amount of technical assistance and training the project provided. For the project indicators noted above on which the project reported data, we traced results to supporting schedules that detailed the breakdown of the figures. For example, for the alliance that the project helped facilitate, we reviewed a progress report detailing the contract. For the technical assistance and training indicators, the project provided supporting schedules detailing the hours by individual providing technical assistance or receiving training. For the number of small producer units supported, although we did not consider the reported figure valid, we examined a schedule the project provided showing the number of units supported by grantee.

For contracting, we studied file documentation maintained by USAID/El Salvador on the award and negotiation of the project. In addition, we reviewed documentation supporting the mission's approvals of Nathan's consultants and subcontractors. At Nathan, we examined the company's procurement processes and manual and looked through their internal contract files.

We relied in part on computer-processed data in progress reports prepared by Nathan. We assessed data reliability by studying the systems used to gather and report the information. In addition, we reviewed reported results and their supporting data. We also conducted interviews and site visits to gather support for the audit objective. Our review of system controls and the results of data tests showed that, despite one instance of invalid data, Nathan supported its reported results.

We performed site visits to verify activities were taking place and to better understand challenges the project faced. The audit team selected and visited 18 grantees (out of 21), 4 regional buyers (out of 21 that the project is working with), other donors, Zamorano University in Honduras, SIECA, El Salvadoran customs officials, and consultants supporting the project. We chose grantees and the buyer's representative of the project's activities in each country, taking into account their geographic locations to use our time efficiently. Because we based our site selections on judgmental samples, our results and conclusions were limited to the items and areas tested and cannot be projected to all project sites. We believe we tested sufficiently to support the audit's findings.

MANAGEMENT COMMENTS

USAID | CENTRAL AMERICA
FROM THE AMERICAN PEOPLE

MEMORANDUM

Date: May 4, 2016

To: Jon Chasson, Regional Inspector General/San Salvador

From: Lawrence J. Sacks, USAID/El Salvador Mission Director,

Subject: Mission response to the audit of USAID/El Salvador Regional Trade and Market Alliances Project (Report No. 1-519-16-005 P)

USAID/El Salvador thanks the Regional Inspector General/San Salvador (RIG) for conducting the referenced performance audit of the Regional Trade and Market Alliances Project (RTMA). RTMA has successfully positioned itself as a leading instrument in providing technical assistance in the areas of agribusiness and trade capacity building, and engaging with key regional and national organizations. In September 2015, USAID/El Salvador approved the option period for RTMA, extending the project for two additional years, until April 2018, for a total estimated cost of $18.9 Million. During this phase, it is expected that RTMA will consolidate the results achieved during the base period and work with the project's beneficiaries to ensure that results are sustained beyond the implementation of USAID's project.

We welcome RIG's contributions to assist us to improve the performance and impact of RTMA's activities to continue increasing capacities of Central American agriculture producer's organizations to access regional markets and promoting trade facilitation policies to reduce the costs of crossing borders and improve regional economic integration.

In this response, you will note that our Mission has already started actions to address many of the recommendations of the audit of USAID/El Salvador Regional Trade and Market Alliances Project report (Report No. 1-519-16-005 P).

Recommendation 1. "We recommend that USAID/El Salvador work with Nathan Associates Inc. to implement a plan for helping producers overcome obstacles noted by regional buyers."

Comments: USAID El Salvador agrees with this recommendation. USAID/El Salvador has addressed this recommendation by working with the contractor and with grantee organizations. The establishment of market alliances between producers and buyers to attain sustained export sales is one of the key expected results for RTMA. In the work plans for Year 2 and Year 3, USAID approved activities to support the producer's organizations capacities to sustainably achieve and maintain access to markets. Annex 1A presents a logical process of the capacity building and market alliances process implemented to support producers to overcome obstacles to compete in regional markets. Through grants and technical assistance, RTMA is supporting the project's grantees and beneficiary organizations in key areas such as financial management, governance, improved processing lines (equipment), operational efficiency (processing and packaging) and marketing management with clients and other stakeholders. Through grants and technical assistance, the project is helping producers increase productivity and quality; improve production planning and delivery schedules; and improved organizational capacity, through trainings and coaching on governance and financial management. The project is also promoting a culture of accountability and orientation to results, through quarterly accountability meetings with grantees. The implementation of this strategic approach has led to achievement of the contract's expected results: As of December 2015, RTMA grantee producers' organizations and buyers had signed 21 market alliances. These alliances have facilitated producers' organizations and buyers to sign 11 contracts for export, as of March 30, 2016. The list of alliances is part of Annex 1B to this memorandum.

As documented in the above mentioned annexes, the Mission has already taken action and worked with the contractor to implement a plan as recommended by the draft audit report. Accordingly, USAID/El Salvador requests that this recommendation be closed upon issuance of the final audit report.

Recommendation 2. "We recommend that USAID/El Salvador, in coordination with Nathan Associates Inc., implement a plan for expediting delivery of equipment that grantees need to achieve their export goals."

Comment: USAID/El Salvador agrees with the audit recommendation. USAID/El Salvador has ensured that the procurement processes of equipment and other necessary technical assistance have been carried out in compliance with appropriate standards, and that the contractor has implemented a plan to execute prompt delivery of the purchased equipment to the grantees. As of March 2016, the project had awarded contracts for the purchase of post-harvest equipment for 14 producers' organizations. RTMA and its local technical partners are providing technical assistance for successful operation of post-harvest production processing lines.

Annex 2 presents a list of the equipment procured and the installation completion dates for each beneficiary organization. According to this annex, the equipment has been installed and is operational in five of the fourteen processing plants. The plan calls for the installation of the equipment in the remaining plants by June 30, 2016.

Based on the actions taken and planned, USAID/El Salvador requests that this recommendation be closed upon issuance of the final audit report.

Recommendation 3. "We recommend that USAID/El Salvador develop and document a plan to measure the impact of value-chain interventions on nutrition and incomes for small farmers supported by the project."

<u>Comments:</u> USAID/El Salvador partially agrees with this recommendation with respect to developing and documenting a plan to measure the impact of value-chain interventions on incomes. In this respect, as explained in Contract AID-596-C-13-00001, page 13/77, direct targeted interventions to affect individual farmers' incomes or household incomes are out of the scope of this project. The contract specifies that "*the regional program will complement producer's technical assistance efforts but is not intended to provide direct support at farmer's productivity level,*[6]*.*" The statement of work for this contract also specifies that "*this component*

[6] Contract AID-596-C-13-00001, page 13/77

will develop market driven opportunities that can be efficiently attained through a regional platform… targeting private sector buyers and small producers, through alliances with producers technical assistance programs (organizations)."

Despite the scope and limitations of a regional project to support household level farmers' incomes directly, USAID/El Salvador is aware of the need to understand how the activities of this project have contributed to the overall food security of the communities it has benefited. Through the soon to be awarded Monitoring, Evaluation and Learning (MEL) mechanism, the Mission will contract a survey in the communities where RTMA supports post-harvest processing of producers' organizations to understand how the project has impacted households and to what extent investment, and direct and indirect employment opportunities have contributed to improve household incomes. The MEL mechanism is expected to be awarded by June 30, 2016.

The target closure date for completion of the survey is no later than six months after the award of the MEL Contract, or December 31, 2016.

With respect to "nutrition for small farmers", USAID/El Salvador disagrees with the recommendation. USAID's definition of Food Security states: "Food security is having, at all times, both physical and economic access to sufficient food to meet dietary needs for a productive and healthy life."[7] In the statement of work of this contract, the problem to address is defined as follows: "*Central America chronic under nutrition (stunting or low height- for-age) is the most critical nutritional problem facing the region and reflects development problems that result mainly from <u>limited income earning opportunities</u>*.[8]In line with this definition, the project will "*complement USAID bilateral programs to improve farmer's incomes in targeted food insecure areas through technical assistance programs and rural value chain interventions. ...The project is not designed to directly support farmer level technical assistance, but instead, to support small producers organizations to access expanded regional markets.*" The term *"nutrition"* is referred to in the contract to reflect a broader higher level objective as part of the USG Global Hunger and Food Security Strategy to improve "*food security and nutrition*." The project's contribution to "*food security and nutrition*" is through increased incomes of small producers' organizations (producers' groups) through increased sales and improved value of their products. The tasks outlined in the statement of work and the expected results of this project are established accordingly.

Recommendation 4. "We recommend that USAID/El Salvador review and document the choice of value chains to determine whether they met the nutrition and income criteria established in the contract and make adjustments as appropriate."

Comment: USAID/El Salvador disagrees with this recommendation. As explained in the Mission's response to recommendation # 3, direct targeted interventions to affect individual farmers' incomes or household nutrition is out of the scope of this project. The selection of value chains supported by the project is documented in the contractor's MARKET ACCESS FOR CRITICAL VALUE CHAINS—VALUE CHAIN IDENTIFICATION, SELECTION, MAPPING, AND ANALYSIS PHASE I FINAL REPORT[9], dated December 19, 2013. This report is a robust analysis which filters potential products produced and traded throughout targeted countries in

[7] https://www.usaid.gov/what-we-do/agriculture-and-food-security/increasing-food-security-through-feed-future

[8] Contract AID-596-C-13-00001, Page 8 of 77 pages

[9] USAID Regional Trade and Market Alliances Project, December 2013.

Central America. These filters are: market growth potential, enabling environment, social impact (employments, producers base), regional trade potential and project relevance. Implementation of this methodology enabled the selection of value chains (potatoes, mixed vegetables, beans, onions, plantains, honey, cacao) under the project. Through increased production and sales of these products, producers' organizations will improve their post-harvest capacities, regional market access and sales to regional markets. Increased sales and productivity will then lead to improved food security, through improved small farmers' incomes, and thereby support the USAID goal of improving "*food security and nutrition*" in the region.

Recommendation 5. "We recommend that USAID/El Salvador develop and document a meaningful indicator to measure the project's impact on supported producers."

Comment: USAID/El Salvador agrees with this recommendation and actions have been implemented to address it. In addition to the Project's Monitoring and Evaluation Plan approved by USAID in November 2013, and reported on by the contractor on a quarterly basis, USAID's Regional Trade and Market Alliances Project is tracking 16 additional indicators to measure performance of grantee organizations (local technical partners and producers organizations), as follows:

1. Percentage of staff from organizations certified in Grants Management
2. Percentage of staff from organizations certified in technical competencies
3. Governance
4. Efficiency and Performance of production lines
5. Yield on final product
5. Percentage of compliance of Chronogram
6. Percentage of Target of value added products generated (Volume)
7. Net Promoter Score of Clients
8. Net Promoter Score of Beneficiaries
9. Net Promoter Score of Associated producing units
10. Percentage of sales obtained from Value added products (US dollars)
11. Total Value Increase of Export sales
12. Number of regional alliances
13. Number of New jobs created
14. Number of Small producer units exporting
15. Percentage of beneficiaries with improved risk score
16. Return on Investment

USAID/El Salvador believes that these indicators meaningfully measure the project's impact on supported producers. Annex 3 presents a detailed list of indicators, baselines and results achieved.

Based on the actions taken, the Mission requests that this recommendation be closed upon the issuance of the final audit report.

Recommendation 6. "We recommend that USAID/El Salvador document the rationale for expected targets for the Regional Trade and Market Alliances project and make adjustments as appropriate for the remainder of the activity."

Comment: USAID/El Salvador agrees with this recommendation. The Mission will work with Nathan Associates Inc. to update the activity M&E Plan. The updated the M&E plan will include the rationale for setting targets.

The target completion date is June 30, 2016.

Recommendation 7. "We recommend that USAID/El Salvador develop written instructions to staff requiring them to comply with USAID policy by documenting targets."

Comment: USAID/El Salvador agrees with this recommendation and will develop written instructions to staff requiring them to comply with USAID policy, emphasizing the importance of documenting targets.

The target completion date is June 30, 2016.

Recommendation 8. "We recommend that USAID/El Salvador instruct Nathan Associates Inc. to verify the number of small producer units that will participate in regional and export value chains supported by the project."

Comment: USAID/El Salvador agrees with this recommendation. The Mission has worked with the contractor to adjust and disaggregate the data to capture the results of the project on small producers' units that export and that sell to domestic markets separately. After publication of the baselines for producers' organization grants on June 30, 2015, the Contracting Officer Representative held a meeting with the project's staff. The meeting on August 26, 2015 is documented and the project's monitoring and evaluation staff agreed that the "number of small producers units" supported by the project would be revised to include only the "number of small producers units exporting" that participate in export value chains. In subsequent reporting documents, including quarterly reports, this indicator was adjusted from 7,412 to 3,784 small producers units. It is important to highlight that even though this indicator only reflects the producers that export, the project has impacted a broader number of producers. The nature of agricultural processes, and organizational capacity building activities, has allowed RTMA to also support producers that sell in domestic markets.
The indicator data is revised and the results are adjusted to reflect only the producers that participate in exports.

Annex 4 presents the Site Visit Report of the USAID COR and Nathan Monitoring and Evaluation staff during which the COR requested that the indicators be revised to include only the producers that export and that the baselines and targets be revised accordingly.

Based on the actions taken, the Mission requests that this recommendation be closed upon the issuance of the final audit report.

Recommendation 9. "We recommend that USAID/El Salvador develop a joint training program for technical officers and the monitoring and evaluation specialist to review their shared responsibilities for performance monitoring and data quality, as described in Mission Order 203."

Comment: USAID/El Salvador Mission agrees with this recommendation and will conduct training for technical officers and monitoring and evaluation specialists to explain Mission Order 203 and make sure that the Mission's staff has a better understanding of the responsibilities of performance monitoring and data quality.

The target completion date is September 30, 2016.

Currently, the Bureau for Policy, Planning and Learning is revising and updating ADS 203, and it is expected that the new version of the ADS may be launched in September 2016. The Mission will continue to follow ADS 203 until the new ADS 200 series is approved as official agency policy (as there is no guarantee it will be approved in September). However, the Mission will take advantage of this update to train technical officers and monitoring and evaluation specialists by offering a preview of potential upcoming changes as highlighted in the draft ADS 200 and how this could create possible changes to Mission Order 203. Once the new ADS 200 series is officially approved, there will be a follow up training to present the changes under the new policy and how they will impact the Mission.

Recommendation 10. "We recommend that USAID/El Salvador formally request that the Bureau for Latin America and the Caribbean review and issue a written decision on the curtailment of project activities in the Dominican Republic."

Comment: USAID/El Salvador agrees with this recommendation and will follow up with the Bureau for Latin America and the Caribbean and USAID/Dominican Republic to draft a written decision on the curtailment of project activities in the Dominican Republic.

The target completion date is September 30, 2016.

Recommendation 11. "We recommend that USAID/El Salvador perform a financial review of Nathan Associates Inc. to determine whether its systems meet acquisition requirements."

Comment: USAID/El Salvador agrees with this recommendation. The Regional Office of Acquisitions and Assistance (ROAA) contacted the Cost and Audit Support (CAS) Division of the Office of Acquisition and Assistance (OAA) in Washington, DC and requested input and support on determining the adequacy of Nathan Associates, Inc. procurement procedures. Based on the input received from CAS, our plan for addressing this recommendation is for ROAA to send a letter to the contractor informing them that their procurement procedures were inadequate for the specific subcontracts identified in the RIG audit report, and requesting the contractor's corrective plan of action, with the final implementation date for that plan set at September 30, 2016. Then CAS staff will conduct the recommended review, and provide a report of their findings by January 31, 2017.

Recommendation 12. "We recommend that USAID/El Salvador determine the allowability of $172,570 in ineligible questioned costs for consulting contracts that did not follow acquisition regulations, and recover from Nathan Associates Inc. any amount deemed unallowable."

Comment: Determination of allowability of the questioned costs will be pending and subject to a specific review of the procurement processes leading to the questioned amounts, and, if required, additional market research.

This action will be completed by September 30, 2016.

Recommendation 13. "We recommend that USAID/El Salvador issue written instructions to the contractor officer's representative on the proper procedures for contract approvals."

Comment: USAID/El Salvador agrees with this recommendation. It is important to clarify that the Contracting Officer Representative (COR) provided technical concurrence to the sub-contract, but not contracting approval. The statement "I concur with this firm fixed price purchase order agreement", written by the COR is included in an order agreement sheet prepared by the contractor. This document served to provide technical concurrence with the purpose and terms of a subcontract to People Link for a value of $19,800 to develop a balance scorecard monitoring system to support grantee organizations.

Specific written guidance, to complement the instructions outlined in the Contracting Officer's Representative Designation Memorandum issued at the time of contract award, will be issued to the COR outlining best practices for technical approvals/concurrences under the contract.

This action will be completed by June 30, 2016.

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