



# OIG HIGHLIGHTS

View Report [AUD-SI-16-05](#).

## What OIG Audited

OIG conducted this audit to determine whether the National Endowment for Democracy (NED) used annual grant funds from FY 2006 to FY 2014 provided by the Department of State (Department) in compliance with applicable laws and regulations.

## What OIG Recommends

OIG did not make any recommendations in this report. However, OIG made two recommendations to the Department regarding its grant oversight of NED in the *Management Assistance Report: Oversight of Grants to the National Endowment for Democracy* (AUD-SI-15-34, June 2015). In that report, OIG recommended that the Department take actions to implement a process to conduct the required audit of NED financial transactions and amend its annual grant agreement with NED to specifically include the audit requirement.

With respect to this report, NED concurred with the results of the audit and its comments are reprinted in their entirety as Appendix B.

UNCLASSIFIED

November 2015

OFFICE OF AUDITS

Security and Intelligence Division

## Audit of the National Endowment for Democracy Use of Department of State FY 2006 – FY 2014 Annual Grant Funds

### What OIG Found

Congress recognized and authorized funding for NED in 1983 through the National Endowment for Democracy Act (the Act). NED is a private, nonprofit corporation that is not an agency or establishment of the U.S. Government. NED was created to strengthen democratic institutions throughout the world by distributing funds through grants to private organizations. NED receives funding each year from Congress through amounts authorized in the Department's annual budget appropriations to accomplish its purposes. NED received more than \$960 million in grant funds from the Department from FY 2006 to FY 2014.

OIG found that NED used funds in compliance with applicable laws and regulations for the projects tested that were funded from Department FY 2006 to FY 2014 annual grants. Further, NED files reflected evidence to show adherence to the Act. This occurred because NED designed and implemented policies and procedures to help ensure grantee compliance, including detailed guidance provided to its grantees. In addition, NED's Compliance Department conducted annual reviews of core institutes to ensure that procedures were followed and made recommendations for improvement when issues were identified.

In the related *Management Assistance Report: Oversight of Grants to the National Endowment for Democracy*, OIG found that the Department had not conducted audits of NED financial transactions, as required by the Act. Further, the terms and conditions of the annual grant to NED did not include the language related to the audit requirement. The Department suggested alternatives to the two recommendations OIG made. In respect to OIG's recommendation that the Bureau of Administration implement a process to conduct required audits of NED financial transactions, OIG did not accept the alternative action suggested because it was non-responsive to the recommendation. OIG considers this recommendation "unresolved," and this matter will be addressed during the audit compliance process. However, OIG accepted the alternative action suggested for the timeframe for updating the terms and conditions of the grant, and considers this recommendation "resolved," pending further action.

\_\_\_\_\_  
Office of Inspector General  
U.S. Department of State • Broadcasting Board of Governors

UNCLASSIFIED



OIG

Office of Inspector General

U.S. Department of State • Broadcasting Board of Governors

---

AUD-SI-16-05

Office of Audits

November 2015

---

# Audit of the National Endowment for Democracy Use of Department of State FY 2006 – FY 2014 Annual Grant Funds

## SECURITY AND INTELLIGENCE DIVISION

---

~~**IMPORTANT NOTICE:** This report is intended solely for the official use of the Department of State or the Broadcasting Board of Governors, or any agency or organization receiving a copy directly from the Office of Inspector General. No secondary distribution may be made, in whole or in part, outside the Department of State or the Broadcasting Board of Governors, by them or by other agencies or organizations, without prior authorization by the Inspector General. Public availability of the document will be determined by the Inspector General under the U.S. Code, 5 U.S.C. 552. Improper disclosure of this report may result in criminal, civil, or administrative penalties.~~

---

# CONTENTS

---

OBJECTIVE.....	1
BACKGROUND .....	1
About the National Endowment for Democracy .....	1
Criteria .....	4
AUDIT RESULTS.....	7
National Endowment for Democracy Used Funds in Compliance With Applicable Laws and Regulations for Selected Projects.....	7
APPENDIX A: SCOPE AND METHODOLOGY .....	11
Prior Reports.....	12
Work Related to Internal Controls .....	13
Use of Computer-Processed Data.....	14
Detailed Sampling Methodology .....	15
APPENDIX B: NATIONAL ENDOWMENT FOR DEMOCRACY RESPONSE .....	19
ABBREVIATIONS .....	20
OIG AUDIT TEAM .....	21

## OBJECTIVE

---

The Office of Inspector General (OIG) conducted this audit to determine whether the National Endowment for Democracy (NED) used annual grant funds from FY 2006 to FY 2014 provided by the Department of State (Department) in compliance with applicable laws and regulations.

## BACKGROUND

---

### About the National Endowment for Democracy

Congress recognized and authorized funding for NED in 1983 through the National Endowment for Democracy Act (the Act).<sup>1</sup> NED is a private, nonprofit corporation that is not an agency or establishment of the U.S. Government. NED's operations and staff are managed by a President<sup>2</sup> that is selected by a bipartisan Board of Directors<sup>3</sup> of not fewer than 13 and not more than 29 members reflecting the diversity of American society. All major policy and funding decisions are made by the NED Board of Directors. The Board of Directors, as stated in the Act,<sup>4</sup> determines what projects to fund that are consistent with NED's purposes. The Act recognizes the following six purposes for NED.<sup>5</sup>

- (1) to encourage free and democratic institutions throughout the world through private sector initiatives, including activities which promote the individual rights and freedoms (including internationally recognized human rights) which are essential to the functioning of democratic institutions;
- (2) to facilitate exchanges between United States private sector groups (especially the two major American political parties, labor and business) and democratic groups abroad;
- (3) to promote United States nongovernmental participation (especially through the two major American political parties, labor, business, and other private sector groups) in democratic training programs and democratic institution-building abroad;
- (4) to strengthen democratic electoral processes abroad through timely measures in cooperation with indigenous democratic forces;

---

<sup>1</sup> National Endowment for Democracy Act, Pub. L. 98-164, 97 Stat. 1039 (1983) (codified, as amended, at 22 U.S.C. §§ 4411-4416).

<sup>2</sup> As of November 2015, Carl Gershman was the NED President.

<sup>3</sup> For a list of NED's current Board of Directors, see: <http://www.ned.org/about/board>.

<sup>4</sup> 22 U.S.C. § 4412(a), "Authorization; funding; grant agreement."

<sup>5</sup> 22 U.S.C. § 4411, "Findings; statement of purposes."

(5) to support the participation of the two major American political parties, labor, business, and other United States private sector groups in fostering cooperation with those abroad dedicated to the cultural values, institutions, and organizations of democratic pluralism; and

(6) to encourage the establishment and growth of democratic development in a manner consistent both with the broad concerns of United States national interests and with the specific requirements of the democratic groups in other countries which are aided by programs funded by the Endowment.

### *NED Annual Funding*

NED receives funding each year from Congress through amounts authorized in the Department's annual budget appropriations. As prescribed in the Act,<sup>6</sup> the funding is in the form of an annual grant. From FY 2006 to FY 2014,<sup>7</sup> the Department awarded more than \$963 million in annual grants to NED.<sup>8</sup> Table 1 shows the annual grant amounts for NED by fiscal year.

**Table 1. Annual Grant Funding to NED from FY 2006 to FY 2014**

<b>Fiscal Year</b>	<b>Grant Number</b>	<b>Amount</b>
2006	S-LMAQM-06-GR-009	\$ 74,042,100
2007	S-LMAQM-07-GR-019	\$ 74,042,100
2008	S-LMAQM-08-GR-0101	\$ 99,190,000
2009	S-LMAQM-09-GR-533	\$115,000,000
2010	S-LMAQM-10-GR-0501	\$118,000,000
2011	S-LMAQM-11-GR-503	\$118,199,163
2012	S-LMAQM-12-GR-1014	\$117,764,000
2013	S-LMAQM-13-GR-1060	\$112,171,805
2014	S-LMAQM-14-GR-1008	\$135,000,000
<b>Total</b>		<b>\$963,409,168</b>

**Source:** OIG generated from Department data.

<sup>6</sup> 22 U.S.C. § 4412, "Grants to the Endowment."

<sup>7</sup> This represents the timeframe since the previous OIG audit of NED financial transactions, which included transactions made through FY 2005, *Audit of the National Endowment for Democracy for Fiscal Years 2003-05* (AUD/CG-07-33, Sept. 2007, <http://www.oig.state.gov/reports/8058>).

<sup>8</sup> Congress authorized \$971,528,000 from FY 2006 to FY 2014 to NED; however, due to budgetary restrictions from Office of Management and Budget, the Department grant award amounts varied slightly. In addition, NED has received additional grants for specific projects identified by the Department, which are tracked separately from the annual grant funds.

### *Core Institutes*

NED, a Department grantee, is a grant-making organization and does not directly implement projects.<sup>9</sup> To achieve its purposes, a significant portion of funds provided to NED are executed through projects implemented by four affiliated institutes, known as the “core institutes.” The four core institutes are:

- American Center for International Labor Solidarity;
- Center for International Private Enterprise;
- International Republican Institute; and
- National Democratic Institute for International Affairs.

The core institutes have a special relationship with NED, and are considered to be part of the “NED family.” That includes collaborative planning for projects that NED will fund, which has led to annual grant agreements with approximately 3-year performance periods for the core institutes. Each quarter, the NED Board of Directors considers and approves a number of projects to be implemented by the core institutes. Rather than using a separate grant for each core institute project, projects are funded out of the balance of available grant funds. In addition, NED’s procedures for monitoring projects implemented by core institutes are different than procedures for its other grantees. For example, each year NED officials conduct compliance reviews of policies, procedures, and documentation, as well as Office of Management and Budget (OMB) Circular A-133 required audits of each core institute, in addition to individually monitoring each project.

### *Discretionary Grantees*

In addition to the core institutes, NED awards grants to other private sector organizations. Generally, these grants are for institutional support and specific projects that have a 1-year performance period. NED officials call these organizations “discretionary grantees.” The process for awarding grants to discretionary grantees differs from the core institute process as the discretionary grantees are not included in NED’s overall planning process. Potential discretionary grantees submit proposals for a project to NED directly; NED does not solicit for proposals. The discretionary projects are considered and approved by the Board of Directors on a quarterly basis—at the same time that core projects are approved. NED’s monitoring of discretionary grantees includes reviews of invoices and progress reports from the grantee, and occasional site visits.

---

<sup>9</sup> Because NED is a Department grantee, all organizations that NED awards grants to, from Department grant funds, are therefore considered “subgrantees” or “subrecipients” of the Department.

## Criteria

The Act and annual grant agreement with NED both include specific criteria NED must follow. For example, the Act states that NED may only provide funding for programs that are consistent with the six purposes set forth in the Act.<sup>10</sup>

### *National Endowment for Democracy Act Requirements*

#### *Audit Requirements*

The Act states that all NED accounts are to be “audited annually in accordance with generally accepted auditing standards by independent certified public accountants” (CPA)<sup>11</sup> and reported accordingly. The Act also states that the Government Accountability Office may audit the financial transactions of NED and a report of each audit should be provided to Congress by the Comptroller General.<sup>12</sup> In addition to the required annual audit by public accountants and the Government Accountability Office’s option to conduct audits, the Act requires that the Department<sup>13</sup> audit NED’s financial transactions for each fiscal year.<sup>14</sup>

#### *Audits by the Department*

During the audit, OIG found that the Department was not conducting audits of NED’s financial transactions for each fiscal year as required by the Act. OIG issued a Management Assistance Report<sup>15</sup> to address this issue in June 2015. In the report, OIG recommended that the Department take action to implement a process to conduct the required audit of NED financial transactions and amend its annual grant agreement with NED to specifically include the audit requirement.

#### *Other Act Provisions*

In addition to the audit requirements, there are other provisions in the Act to which NED must adhere, including restrictions on use of funds and conflicts of interest. Specifically, NED funds

---

<sup>10</sup> 22 U.S.C. § 4413(b), “Funding for private sector groups and covered programs only.”

<sup>11</sup> 22 U.S.C. § 4413(e), “Audit of accounts; reporting requirements.”

<sup>12</sup> 22 U.S.C. § 4413(f), “Audit of financial transactions; reporting requirements.”

<sup>13</sup> From 1983 to 1999, NED received funding through an annual grant from the United States Information Agency; however, in 1999 Congress abolished the agency and transferred its functions to the Department. As noted in 22 U.S.C. § 6532(a), “There are transferred to the Secretary of State all functions of the Director of the United States Information Agency and all functions of the United States Information Agency and any office or component of such agency, under any statute, reorganization plan, Executive order, or other provision of law, as of the day before the effective date of this subchapter.”

<sup>14</sup> 22 U.S.C. § 4413(g), “Audits by United States Information Agency.”

<sup>15</sup> *Management Assistance Report: Oversight of Grants to the National Endowment for Democracy* (AUD-SI-15-34, Jun. 2015), <https://oig.state.gov/system/files/aud-si-15-34.pdf>.

may not be used to support a political campaign for a candidate for public office or to finance activities of the Republican National Committee, Democratic National Committee, or organizations engaged in partisan politics on their behalf.<sup>16</sup> Further, the Act<sup>17</sup> prohibits NED Board members from being a member of the board of directors or an officer of any NED grantee that receives more than 5 percent of NED funds in any fiscal year, which encompasses the four core institutes. For example, in 2014 each core institute<sup>18</sup> received \$13.75 million from NED, which was more than 10 percent of NED's \$135 million grant from the Department.

### *Grant Agreement Requirements*

Additional criteria that NED must follow are included in the annual grant agreement between the Department and NED. Specifically, compliance with OMB Circulars A-110, A-122, and A-133 is required by provisions of the grant agreement.<sup>19</sup> In addition to OMB requirements, the annual grant agreement requires adherence with Executive Order 13224, the Victims of Trafficking and Violence Protection Act, and suspension and debarment regulations.

#### *OMB Circular A-110*

OMB Circular A-110<sup>20</sup> prescribes the procedures for administering grants and agreements with non-profit organizations, such as NED. The guidance includes pre-award, post-award (performance), and "after-award" (closeout) requirements. These regulations apply not only to NED, but also to the awards that NED makes to its grantees—both core institutes and discretionary grantees.

#### *OMB Circular A-122*

OMB Circular A-122<sup>21</sup> details cost principles for grants and other Federal awards to non-profit organizations. The principles are designed to provide that the Federal Government bears its fair share of costs. The guidance details how to determine allowability and allocability of costs, and defines direct and indirect costs, among others.

---

<sup>16</sup> 22 U.S.C. §4414(a), "Partisan politics."

<sup>17</sup> 22 U.S.C. 4413(j), "Grantee; conflict of interest."

<sup>18</sup> Annual grants from NED are not the sole source of funding for the core institutes. For example, core institutes may receive grants for specific projects in the same respect that NED receives additional grants from the Department for specific projects. In addition, core institutes may also receive funding from other government agencies, such as the U.S. Agency for International Development.

<sup>19</sup> Although these criteria applied to the grants OIG reviewed, new criteria from OMB has been issued that will apply to future grant agreements—2 CFR Chapter I, Chapter II, Part 200, et al., "Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards," Dec. 26, 2013.

<sup>20</sup> OMB Circular A-110, "Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations," Jan. 1, 2012.

<sup>21</sup> OMB Circular A-122, "Cost Principles for Non-Profit Organizations," Aug. 8, 2005.



*OMB Circular A-133*

OMB Circular A-133<sup>22</sup> requires that non-Federal entities, such as non-profit organizations, that expend \$500,000 or more in Federal awards a year have a single audit conducted by a CPA firm as described in the circular. The audit requirement does not limit the audit authority of Inspectors General or the Government Accountability Office to conduct additional audits. OMB Circular A-133 is similar to the annual audit requirement in the Act, and as a result, NED only has one audit conducted each year by a CPA firm.

*Executive Order 13224*

Executive Order 13224<sup>23</sup> provides a “means by which to disrupt the financial support network for terrorists and terrorist organizations by authorizing the U.S. government to designate and block the assets of foreign individuals and entities that commit, or pose a significant risk of committing acts of terrorism.”<sup>24</sup> Specifically, the annual grant agreement with NED “prohibits transactions with, and the provision of resources and support to, individuals and organizations associated with terrorism.” The grant agreement also gives the legal responsibility to NED to ensure compliance with the Executive Order and requires that the provision be included in all sub-awards.

*Victims of Trafficking and Violence Protection Act*

The Victims of Trafficking and Violence Protection Act<sup>25</sup> authorizes the Government to terminate a grant, contract, or cooperative agreement without penalty, “if the grantee or any subgrantee, or the contractor or any subcontractor (i) engages in severe forms of trafficking in persons or has procured a commercial sex act during the period of time that the grant, contract, or cooperative agreement is in effect, or (ii) uses forced labor in the performance of the grant, contract, or cooperative agreement.”<sup>26</sup>

*Debarment and Suspension Regulations*

To protect the public interest, the Federal government ensures the integrity of Federal programs by conducting business only with responsible persons as required by Federal regulations.<sup>27</sup> The

<sup>22</sup> OMB Circular A-133, “Audits of States, Local Governments, and Non-Profit Organizations,” Jun. 26, 2007.

<sup>23</sup> Executive Order 13224, Blocking Property and Prohibiting Transactions with Persons Who Commit, Threaten to Commit, or Support Terrorism, Sept. 23, 2001.

<sup>24</sup> Executive Order 13224 defines terrorism as an “activity that (1) involves a violent act or an act dangerous to human life, property, or infrastructure; and (2) appears to be intended to intimidate or coerce a civilian population; to influence the policy of a government by intimidation or coercion; or to affect the conduct of a government by mass destruction, assassination, kidnapping, or hostage-taking.”

<sup>25</sup> Victims of Trafficking and Violence Protection Act of 2000, Pub. L. 106-386, 114 Stat. 1466 (Oct. 28, 2000); 22 U.S.C. §§7101-7110.

<sup>26</sup> 22 U.S.C. §7104(g), “Termination of certain grants, contracts and cooperative agreements.”

<sup>27</sup> 2 C.F.R. §180.125. “What is the purpose of the nonprocurement debarment and suspension system?”

regulations further restrict subawards and contracts with “parties that are debarred, suspended or otherwise excluded from or ineligible for participation in Federal assistance programs.”<sup>28</sup>

## AUDIT RESULTS

---

### National Endowment for Democracy Used Funds in Compliance With Applicable Laws and Regulations for Selected Projects

OIG found that NED used funds in compliance with applicable laws and regulations for the projects OIG tested that were funded from Department FY 2006 to FY 2014 annual grants. Further, NED files reflected evidence of adherence to the Act. This occurred because NED designed and implemented policies and procedures to help ensure grantee compliance. Specifically, NED project files show that grantees were provided sufficient guidance. In addition, NED’s Compliance Department conducted annual reviews of core institutes to ensure that procedures were followed, and made recommendations for improvement when issues were identified.

#### *NED Compliance with Laws and Regulations*

OIG found that selected NED grant or project files or grant agreements with the core institutes contained sufficient evidence to demonstrate that NED used its funds in compliance with applicable laws and regulations. OIG selected a sample<sup>29</sup> of 118 project and grant files to review—97 core institute projects valued at \$53,155,428 and 21 discretionary grants valued at \$7,832,958. OIG used the information in the grant and project files and grant agreements with the core institutes to determine compliance with key requirements from OMB Circulars A-110, A-122, and A-133, as well as Executive Order 13224, Trafficking in Persons guidance, and debarment and suspension regulations.<sup>30</sup> Based on testing, OIG did not identify any instances where NED did not comply with the key requirements of laws and regulations.

For example audit reports on NED prepared by a CPA firm for FYs 2006-2013<sup>31</sup> required by OMB Circular A-133 were completed. The CPA firm generally did not identify any material weakness, with one exception. The audit for FY 2011<sup>32</sup> identified one material weakness<sup>33</sup> related to the lack

---

<sup>28</sup> 22 C.F.R. §518.13, “Debarment and suspension.”

<sup>29</sup> For additional details regarding the sample selection see Appendix A: Scope and Methodology.

<sup>30</sup> For additional details regarding requirements tested see Appendix A: Scope and Methodology.

<sup>31</sup> Due to the timing of OIG’s audit, OIG did not review NED’s A-133 audit reports for FY 2014.

<sup>32</sup> National Endowment For Democracy OMB Circular A-133 Supplementary Financial Report Year Ended September 30, 2011, McGladrey LLP, Jun. 28, 2012.

<sup>33</sup> According to the generally accepted auditing standards, a “material weakness” is defined as “a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis.”

of financial reconciliations between external grant activity and cash drawdowns. According to the FY 2012 audit report<sup>34</sup> NED corrected the deficiency and the CPA firm did not report any other material weaknesses in the FY 2012 and FY 2013 audits.<sup>35</sup>

OIG also found that each core institute complied with the requirement to have an A-133 audit performed during FYs 2006 to 2013.<sup>36</sup> The CPA firms that conducted the audits identified few issues in the reports on the core institutes and, according to the audit reports, the core institutes took action to resolve the issues. For example, the FY 2006 audit<sup>37</sup> identified a significant deficiency<sup>38</sup> at the International Republican Institute that had been detected by existing internal controls.<sup>39</sup> According to the FY 2007 A-133 audit report,<sup>40</sup> the International Republican Institute resolved the issue, and no other issues were reported.

In addition, OIG found that NED had checked and documented searches of the *Specially Designated Nationals*<sup>41</sup> list prior to awarding all grants tested, both core institute and discretionary, in accordance with Executive Order 13224 requirements. Further, in compliance with debarment and suspension regulations, OIG found that NED documented its searches of the *Excluded Parties List System*<sup>42</sup> prior to awarding all grants tested. Additionally, OIG found that the requirements for compliance with the Victims of Trafficking in Persons Act of 2000 were included in all of the agreements that NED had with its grantees.

With regard to the Act's requirements,<sup>43</sup> OIG found that NED did not award grants to either the Republican or Democratic National Committees from its FY 2006 to FY 2014 grant funding. Further, OIG compared the members of the NED Board of Directors with the boards of the four

---

<sup>34</sup> National Endowment For Democracy OMB Circular A-133 Supplementary Financial Report Year Ended September 30, 2012, McGladrey LLP, Jan. 11, 2013.

<sup>35</sup> National Endowment For Democracy OMB Circular A-133 Supplementary Financial Report Year Ended September 30, 2013, McGladrey LLP, Jan. 24, 2014.

<sup>36</sup> Due to the timing of OIG's audit, OIG did not review the core institutes' A-133 audit reports for FY 2014.

<sup>37</sup> International Republican Institute Report Required in Accordance with Office of Management and Budget Circular A-133 For the Year Ended September 30, 2006, McGladrey and Pullen, LLP, Nov. 11, 2006.

<sup>38</sup> According to the generally accepted auditing standards, a "significant deficiency" is defined as "a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance."

<sup>39</sup> The significant deficiency was associated with U.S. Agency for International Development grant funds.

<sup>40</sup> International Republican Institute Report Required in Accordance with Office of Management and Budget Circular A-133 For the Year Ended September 30, 2007, McGladrey and Pullen, LLP, Dec. 5, 2007.

<sup>41</sup> Executive Order 13224, Blocking Property and Prohibiting Transactions with Persons Who Commit, Threaten to Commit, or Support Terrorism, Sept. 23, 2001.

<sup>42</sup> 2 C.F.R. §180.500. "What is the purpose of the Excluded Parties List System (EPLS)?"

<sup>43</sup> 22 U.S.C. §4414(a) "Partisan Politics."

core institutes and found that no member of NED's board was on a board of a core institute, as required by the Act.<sup>44</sup>

### *NED Internal Compliance Procedures*

Selected projects complied with key requirements in Federal laws and regulations because NED developed and implemented internal policies and procedures to ensure compliance for grantees, both core institutes and discretionary grantees. Specifically, NED developed the "National Endowment for Democracy Grantee Guide" and its Compliance Department conducted annual reviews of core institutes to help ensure compliance.

### *NED Grantee Guide*

To help ensure its grantees complied with the Act and other requirements, NED developed a step-by-step guide for its grantees. The "National Endowment for Democracy Grantee Guide" comprises information that is applicable for all grants, but according to NED officials the guide is primarily designed for discretionary grantees. The guide includes details for the grant process, such as describing the meaning of various sections of the grant agreements, how to receive payments, the reporting requirements, and prohibited activities. The guide also explains terms and conditions of the grant such as details related to prohibitions for funding terrorism and trafficking in persons. Other sections of the guide include allowability of costs, including supporting documentation requirements, and financial management practices, which discuss accounting systems, internal controls, travel, and timekeeping, among others. The guide also includes examples of various documents that grantees may need such as subgrant agreements and samples of required financial reports. OIG analyzed the NED grantee guide and determined that it contained the requirements from the Act, additional NED administrative requirements, and other applicable regulations.

### *NED Annual Reviews of Core Institutes*

In addition to the grantee guide, NED's Compliance Department ensured that core institutes were following applicable laws and regulations, as well as, internal policies and procedures through annual reviews. According to NED compliance procedures, NED officials conduct annual reviews of core institutes that include evaluation of subgrant and field office monitoring procedures and a desk review of the A-133 audit. NED prepares two reports to summarize its findings and recommendations that are provided to the individual core institutes for implementation. OIG found that NED completed the reviews for each core institute for FYs 2006 to 2014 and prepared two reports with findings and recommendations, when applicable. For example, in its 2006 desk review of the International Republican Institute, NED noted that the CPA firm found a significant deficiency in internal controls even though deficiency identified was not associated with NED grant funds. NED officials also follow up on recommendations made in

---

<sup>44</sup>22 U.S.C. §4413(j) "Grantee; conflict of interest."

prior years during each review. For example, during FY 2006 NED made recommendations to each core institute to strengthen their processes for searching the terrorist database in accordance with Executive Order 13224 and debarment and suspension databases in accordance with regulations<sup>45</sup> prior to awarding subgrants. NED followed up the following year with each core institute and found that their procedures had been strengthened and closed the recommendations. From FYs 2006 to 2013, NED made various findings and recommendations to the core institutes; however, in FY 2014, NED found processes and procedures were adequate in all of the core institutes and did not make any recommendations.

**NED Response:** NED concurred with the results of the audit. NED's comments are reprinted in their entirety as Appendix B.

---

<sup>45</sup> 22 C.F.R. §518.13, "Debarment and suspension."

## APPENDIX A: SCOPE AND METHODOLOGY

---

The Office of Inspector General (OIG), Office of Audits conducted this audit to determine whether the National Endowment for Democracy (NED) used annual grant funds provided by the Department of State (Department) in compliance with applicable laws and regulations.

Initially, OIG planned to also determine whether NED had achieved desired results intended to strengthen democratic values and institutions around the world. However, during the course of the audit, OIG identified issues related to the Department's oversight of its annual grants to NED. Because the audit objectives were not designed to address Department oversight of grants to NED, OIG elected to report these findings separately to Department management using a Management Assistance Report.<sup>1</sup> As a result of issuing the Management Assistance Report, and in the interest of economy and efficiency, OIG determined that its audit fieldwork should be limited to compliance with applicable laws and regulations. Specifically, OIG limited its audit work to reviews of documents held by NED, which did not include reviewing supporting documentation at core institute or discretionary grantee locations for validation or verification. OIG did not conduct audit work to determine whether NED achieved desired results intended to strengthen democratic values and institutions around the world.

OIG conducted this audit from November 2014 to June 2015. Audit work was performed in Washington, DC, and Bogota, Colombia. OIG conducted this performance audit in accordance with generally accepted government auditing standards. Those standards requires that OIG plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for the findings and conclusions based on the audit objective. OIG believes that the evidence obtained provides a reasonable basis for the findings and conclusions based on the audit objective.

To obtain background information and criteria for the audit, OIG researched and reviewed Federal laws and regulations as well as prior OIG audit reports and Government Accountability Office decisions. OIG also reviewed the United States Code, the NED Act (the Act),<sup>2</sup> the Code of Federal Regulations, Executive Order 13224,<sup>3</sup> Office of Management and Budget (OMB)

---

<sup>1</sup> *Management Assistance Report: Oversight of Grants to the National Endowment for Democracy*, AUD-SI-15-34, Jun. 2015. <https://oig.state.gov/system/files/aud-si-15-34.pdf>.

<sup>2</sup> National Endowment for Democracy Act, Pub. L. 98-164, 97 Stat. 1039 (1983) (codified as amended at 22 U.S.C. §§ 4411-4416).

<sup>3</sup> Executive Order 13224, Blocking Property and Prohibiting Transactions with Persons Who Commit, Threaten to Commit, or Support Terrorism, Sept. 23, 2001.

Circulars,<sup>4</sup> and NED internal guidance. In order to gain an understanding of the administration and execution of grants to NED, OIG met with Department officials, including the grants officer and grants officer's representative. In addition, to understand NED operations, OIG met with key personnel from NED, including the Chief Operating Officer, Senior Director of Grants Administration, and Senior Director of Compliance. OIG also attended a Board of Directors quarterly meeting at NED to observe the grant approval process.

OIG reviewed hardcopy and electronic documentation maintained at the NED office in Washington, DC, including grant agreements, project files, narrative reports, and financial reports from NED core institutes and discretionary grantees. OIG also reviewed the grant agreements between the Department and NED for FYs 2006-2014, as well as independent audit reports of NED.

In addition to its domestic work, OIG planned to conduct audit work at several overseas posts.<sup>5</sup> OIG conducted its first site visit to Embassy Bogota in Colombia. While in Bogota, OIG met with two core institutes and several of their subgrantees<sup>6</sup> as well as Embassy Bogota officials. OIG did not identify any significant issues during its visit to Bogota, and also found that core institute subgrantees were required by the core institutes to send supporting documentation back to core institute headquarters in Washington, DC. Based on analysis of the results of its work in Bogota, OIG concluded that the identification of significant issues from further audit work at overseas posts would not be likely because in the professional judgment of the audit team, the work conducted in Bogota was representative of program operations that would be encountered at other overseas locations. The team determined that the benefits derived from additional overseas post visits did not outweigh the costs of the additional overseas travel. Further, OIG concluded that its audit work performed in Bogota, Colombia, and Washington, DC, had yielded sufficient, appropriate evidence to satisfy the requirements of generally accepted government auditing standards. Consequently, OIG did not perform the remainder of the planned overseas work in the interest of economy and efficiency per generally accepted government auditing standards.

## Prior Reports

- A June 2015 OIG report, *Management Assistance Report: Oversight of Grants to the National Endowment for Democracy*, AUD-SI-15-34, reported that the Department had

---

<sup>4</sup> OMB Circular A-110, "Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations," Jan. 1, 2012; OMB Circular A-122, "Cost Principles for Non-Profit Organizations," Aug. 8, 2005; and OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," Jun. 26, 2007.

<sup>5</sup> See Detailed Sampling Methodology and Table A.2 for details.

<sup>6</sup> The core institutes are grantees of NED, and therefore subgrantees of the Department. Any organizations that the core institutes then make additional awards to, from funds received through NED from Department grant funds, are also considered subgrantees. The organizations are subgrantees of both NED and the Department.

not conducted audits of NED financial transactions, as required. In addition, the terms and conditions of the annual grant to NED did not include the language related to the audit requirement. OIG also found that the Department did not comply with other requirements for monitoring NED to include reconciling submitted financial reports with the grant award and sufficiently maintaining grant files. OIG recommended that the Department take actions to conduct required audits of NED financial transactions and amend its grant agreement with NED to include the terms of the audit requirement. The Department suggested alternatives to the two recommendations. OIG did not accept the alternative action suggested for implementing a process to conduct required audits of NED financial transactions and considered this recommendation "unresolved." OIG accepted the alternative action suggested for updating the terms and conditions of the grant to include an audit of NED financial transactions for each fiscal year. OIG considered this recommendation "resolved," pending further action.

- In a September 2007 audit report, *Audit of the National Endowment for Democracy for Fiscal Years 2003-2005*, AUD/CG 07-33, OIG reviewed financial transactions of NED and its four core institutes for FYs 2003-2005 to determine whether they accounted for Federal funds; had adequate internal controls; and complied with applicable laws, regulations, policies, and terms of grant agreements. OIG found that generally NED accounted for Federal funds; however, OIG determined that NED should increase its oversight of the core institutes as they did not always comply with applicable requirements for grant administration. OIG classified \$215,885 as unallowable for expired grant funds and \$208,069 as unsupported funds. OIG made five recommendations for the core institutes to (1) return the unallowable \$215,885, (2) provide support for the \$208,069 in unsupported costs, (3) minimize cash on hand and limit requests to immediate needs, (4) properly document results of the terrorist database research, and (5) comply with subrecipient policies and procedures. All recommendations were closed in May 2009.

## Work Related to Internal Controls

To assess the adequacy of internal controls related to the policies, procedures, and processes related to the areas audited, OIG reviewed NED's internal Compliance Guide and the "National Endowment for Democracy Grantee Guide," as well as interviewed key individuals in the grant approval process. In addition, OIG reviewed the Act and OMB Circulars A-110, A-122, and A-133. Ultimately, OIG used this review of internal controls to develop discretionary grantee and core institute test questions for testing grants and files. Table A.1 summarizes OIG's analysis of applicable criteria, associated NED grantee guide coverage, and resulting OIG testing questions. Due to different approaches to discretionary grants and core institute projects and related grants, not all questions applied to both groups; this is also notated in the table. The results of audit testing are included in the Audit Results section of the report.



Table A.1: Crosswalk of Applicable Criteria, NED Grantee Guide, and OIG Test Questions

Criteria	NED Grantee Guide	OIG Test Question(s)
OMB A-110	Section 7 – Reporting	Did the project manager submit reports to NED documenting progress status in a narrative report? <sup>a</sup> Did NED monitor the project expenditures? <sup>b</sup> Did the grantee provide final financial reports as required? Did the grantee maintain the grant records for 3 years after the closeout letter? Did the project provide final narrative reports that included detailed information about activities and progress? <sup>a</sup>
OMB A-122	Section 5 – Banking and Payments Section 21 – Allowability of Costs Section 22 – Prior Approval Requirements Section 23 – Unallowability of Costs Section 24 – Financial Management Section 27 – Travel and Per Diem	Is there a separate bank account for the grantee? <sup>b</sup> Did the grantee provide an authorization to request payment form before NED provided payments? Did NED receive the request for payment form before sending grant funds to the grantee?
OMB A-133	Section 10 – Audits	Can the grantee account for Government funds to the specific grant? <sup>b</sup> Does the grantee accounting system provide the recording of expenditures for each project by required budget cost categories? <sup>b</sup>
Executive Order 13224	Section 18 – Executive Order 13224	Did NED check to see if the grantee was on the debarment/excluded/terrorist lists before making the award?
Trafficking in Persons	Section 19 – Trafficking in Persons	Did the project manager/core institute comply with Trafficking in Persons requirements?
Debarment and Suspension	Section 14 – Suspension and Termination Section 17 – Ineligibility	Did NED check to see if the grantee was on the debarment/excluded/terrorist lists before making the award?

<sup>a</sup> Core institute project test question only.

<sup>b</sup> Discretionary grant question only.

Source: OIG analysis

## Use of Computer-Processed Data

OIG used computer generated data obtained from NED to identify the sample of projects for audit testing. OIG received grant data from NED in a spreadsheet and loaded the data into an audit software program to conduct reliability testing and select the testing sample. The data in the spreadsheet is from the “GIFTS” database, which contains input by users at NED. GIFTS is a commercial off the shelf system that NED customized. The OIG statistician assisted the audit team to conduct the reliability testing and select the audit sample. OIG assessed the quality and

reliability of the data through preliminary testing as well as during testing and found the data to be of adequate quality and reliability for purposes of this report.

## Detailed Sampling Methodology

### *Identification of the Universe*

NED provided data for core institute<sup>7</sup> projects and discretionary grants, for FYs 2006-2014, which included 8,815 projects/grants valued at \$838,599,513.<sup>8</sup> Individually the projects/grants awarded by NED ranged in value from \$253 to \$1,954,006. Due to the large volume and wide range of values, OIG selected its sample from a revised universe of all projects/grants that were \$250,000 or greater. The revised universe contained 824 grants/projects (9 percent of the original universe), which totaled \$368,563,414 (44 percent of the original universe).

### *Sample Selection*

OIG combined two different methods to select a non-statistical sample for testing. The first method involved the selection of projects/grants that would be utilized during planned overseas post visits. The second method used the "status" of the projects/grants to ensure selection at various points in their life cycle. While two different methods were used in selecting the sample, all selected projects/grants were tested for supporting documentation at the NED office in Washington, DC.

### *Overseas Post Visit Sample Selection*

OIG used audit software to determine the top 25 "target" countries of the grants in the revised universe based on the total value of grants for the country. The target country is the location of the ultimate beneficiaries, although the grantee may not be located in that country. OIG selected its overseas post visit sample based on target countries with the intent to travel to those countries and conduct audit work to determine whether NED was achieving desired results.<sup>9</sup> After determining the top 25 target countries, OIG met with NED and core institute officials to discuss the feasibility of visiting each country. Many of the top 25 countries were excluded from possible visitation for reasons such as political deterioration, target country views of foreign funding (inability to meet with beneficiaries in country), the Ebola epidemic, and personal security of the audit team.

---

<sup>7</sup> The four core institutes are: (1) the American Center for International Labor Solidarity; (2) the Center for International Private Enterprise; (3) the International Republican Institute; and (4) the National Democratic Institute for International Affairs. Each core institute receives one grant from NED each year; however, each individual project to be conducted with NED grant funds is approved and tracked separately by NED.

<sup>8</sup> The projects and grants NED awarded comprised 87.05 percent of the annual grant funds NED received from the Department for FYs 2006 to 2014 (\$963,409,168). See the Background section of this report for details regarding the Department's annual grants to NED.

<sup>9</sup> As previously discussed, this objective was ultimately removed from the scope of the audit.

In making its sample selection, OIG also considered factors including the total value of grants/projects for the country, which equates to the top 25 rank; "age" of the grants/projects, which included whether there were current grants;<sup>10</sup> the NED assigned region;<sup>11</sup> and coverage of all four core institutes.<sup>12</sup> For example, Indonesia was ranked number five on the list of grants/projects, but of 15 grants/projects from FYs 2006 to 2014, only 2 were current; therefore, OIG did not select Indonesia. Table A.2 shows the countries selected for post visits.

**Table A.2: Overseas Post Visit Sample Selection**

Rank	Country	Total Grants (Current Grants)	Total Value	Region	Core Institutes
2	Pakistan	23 (5)	\$15,801,043	Asia	American Center for International Labor Solidarity, Center for International Private Enterprise, International Republican Institute
4	Turkey	18 (3)	\$10,670,927	MENA <sup>a</sup>	International Republican Institute, National Democratic Institute for International Affairs
10	Ukraine	16 (6)	\$ 6,219,692	Europe	American Center for International Labor Solidarity, Center for International Private Enterprise, International Republican Institute, National Democratic Institute for International Affairs
20	Thailand	9 (4)	\$ 4,132,469	Asia	International Republican Institute, National Democratic Institute for International Affairs
21	Colombia	6 (2)	\$ 4,040,750	LAC <sup>b</sup>	International Republican Institute, National Democratic Institute for International Affairs
<b>Total</b>		<b>72 (20)</b>	<b>\$40,864,881</b>	<b>4 of 7</b>	<b>4 of 4</b>

<sup>a</sup> Middle East and North Africa.

<sup>b</sup> Latin America and Caribbean.

**Source:** OIG generated from NED data.

<sup>10</sup> The scope of the audit included FYs 2006 to 2014, and many of NED's grants are only 1-year grants. Therefore, OIG wanted to ensure that it would be able to meet with current participants or beneficiaries of NED grants in the country visited.

<sup>11</sup> NED identifies seven regions for its grants/projects: Africa, Asia, Eurasia, Europe, Middle East and North Africa, Latin America and Caribbean, and Global. OIG included regions as a selection factor to potentially identify any differences occurring among regions.

<sup>12</sup> The core institutes work at various locations around the world, and OIG wanted to ensure each core institute was included as part of at least one site visit.

*“Status” Sample Selection*

The second method OIG used to select the sample was by using the “status” field included in the data received from NED. OIG chose the “status” field, which identifies the corresponding point in each project/grant life cycle, because Federal criteria provides specific actions that must be taken and documented at various points in a grant life cycle. Thus, OIG ensured that it selected projects/grants at all points in the life cycle for testing. Table A.3 shows a description of each status category that was identified in the NED data. Table A.4 shows the revised universe (projects/grants over \$250,000), by status category and each category’s relative dollar value as a percentage of the total.

**Table A.3: Status Category Description**

<b>Status*</b>	<b>Description</b>
Active	Discretionary grants that have been awarded and are not closed
Approved (core)	Core institute projects that have been awarded and are not closed
Approved (csup)	Core institute supplemental – previous project that may have been extended or renewed
Closed	Discretionary grants that have been completed and closed
Closed (csup)	Core institute supplemental projects that are completed and closed
Expired	Discretionary grants where the period of performance has expired, but the grants are not closed
Pending Grant	Discretionary grants that have been awarded but the grant agreement is not finalized
Project Completed (core)	Core institute projects that are completed and closed
Sent	Discretionary grants that have been prepared but not fully executed.

\* “Status” as identified in the data received from NED.

**Source:** OIG generated from NED data.

**Table A.4: Revised Universe Categorized by Status**

<b>Status</b>	<b>Grants/Projects</b>	<b>Value (Percent)</b>
Active	12	\$ 4,044,405 (1.10)
Approved (core)	180	\$ 81,775,912 (22.19)
Approved (csup)	1	\$ 250,000 (0.07)
Closed	43	\$ 15,601,210 (4.23)
Closed (csup)	9	\$ 2,975,430 (0.81)
Expired	2	\$ 924,868 (0.25)
Pending Grant	1	\$ 344,600 (0.09)
Project Completed (core)	574	\$261,936,689 (71.07)
Sent	2	\$ 710,300 (0.19)
<b>Total</b>	<b>824</b>	<b>\$368,563,414 (100)</b>

**Source:** OIG analysis of NED data.

Generally, OIG attempted to sample grants/projects approximately proportional to the dollar value per status category. However, various factors overrode this consideration. For example, the Active category is only 1.10 percent of the total value of the grants/projects, but this category is the only one that contained active discretionary institute grants, so OIG tested all the grants in this category. Table A.5 shows the theoretical sample size for each category based on a planned sample size of approximately 100 grants/projects and the actual sample size for each category.

**Table A.5: Theoretical and Actual Sample Size for Grants and Projects Over \$250,000**

Status	Grants/Projects	Value (Percent)	Theoretical Sample Size	Actual Sample Size
Active	12	\$ 4,044,405 (1.10)	2	12
Approved (core)	180	\$ 81,775,912 (22.19)	23	23
Approved (csup)	1	\$ 250,000 (0.07)	1	1
Closed	43	\$ 15,601,210 (4.23)	5	5
Closed (csup)	9	\$ 2,975,430 (0.81)	1	1
Expired	2	\$ 924,868 (0.25)	1	2
Pending Grant	1	\$ 344,600 (0.09)	1	1
Project Completed (core)	574	\$261,936,689 (71.07)	72	72
Sent	2	\$ 710,300 (0.19)	1	1
<b>Total</b>	<b>824</b>	<b>\$368,563,414 (100)</b>	<b>107</b>	<b>118</b>

**Source:** OIG analysis of NED data.

### *Final Sample*

OIG identified the corresponding categories of the 72 previously identified grants and projects (see Table A.2), and used random numbers to select an additional 46 grants and projects by category to achieve our overall sample size of 118 items. Although OIG did not travel as planned during the audit, the sample selected was used for testing files at the NED office as planned. The final sample of 118 (14.32 percent of the revised universe) grants and projects valued at \$60,988,386 (16.55 percent of the revised universe) for all status categories, consisted of 97 core institute projects valued at \$53,155,428, and 21 discretionary grants valued at \$7,832,958.

# APPENDIX B: NATIONAL ENDOWMENT FOR DEMOCRACY RESPONSE



**National Endowment  
for Democracy**  
*Supporting freedom around the world*

1105 P Street, NW | Suite 500 | Washington, DC 20004-1400  
(202) 379-0300 | (202) 379-0400 fax | E-mail: info@ned.org | www.ned.org

October 19, 2015

Mr. Norman P. Brown  
Assistant Inspector General for Audits  
U.S. Department of State  
Office of Inspector General  
1700 N. Moore Street  
Arlington VA 22209

Dear Mr. Brown:

We have reviewed the draft report *Audit of the National Endowment for Democracy Use of Department of State FY 2006- FY 2014 Annual Grant Funds* and concur with the report as written.

We appreciate the effort and professionalism of the audit team as well as the positive comments on the Endowment's handling of State Department funds.

Sincerely,

Carl Gershman  
President  
National Endowment for Democracy

Maria Poon  
Chairman  
Vin Weber  
Vice Chairman  
Robert Peck  
Treasurer  
Kathryn Carlson Nelson  
Secretary

Elbert Abrams  
Karen Bass  
James Bevel  
Michelle Dumas  
Francis Fukuyama  
William Garrison  
Thompson Osoff  
Zalmay Khalilzad

Jürgen Kuttman  
Karin Lechow  
Primitivo Luján  
Will Marshall  
Acar Nalim  
Mehdi Nahn  
Andrew Nathan  
Mark Osoff

Fred Rossouw  
Felix Ruckman  
Stephen Schatzovich  
Margaret Spellings  
Melanne Verveer  
George Weigel  
Robert Zarillo

Donna D. Fosell (1977-1998)  
John Richardson (1921-2014)  
William E. Droell  
Winston Lord  
John Brademas  
Vin Weber  
Richard Gephart  
*Gloria Steinem*  
Carl Gershman, President



## ABBREVIATIONS

---

CPA	certified public accountant
NED	National Endowment for Democracy
OIG	Office of Inspector General
OMB	Office of Management and Budget

## OIG AUDIT TEAM

---

Regina Meade, Director  
Security and Intelligence Division  
Office of Audits

Beverly J.C. O'Neill, Audit Manager  
Security and Intelligence Division  
Office of Audits

Mary S. Charuhas, Senior Auditor  
Security and Intelligence Division  
Office of Audits

Karen E. Crue, Senior Auditor  
Financial Management Division  
Office of Audits

Laura G. Miller, Senior Management Analyst  
Security and Intelligence Division  
Office of Audits

Phillip Ropella, Senior Auditor  
Security and Intelligence Division  
Office of Audits



UNCLASSIFIED



# HELP FIGHT

FRAUD. WASTE. ABUSE.

1-800-409-9926

[OIG.state.gov/HOTLINE](https://oig.state.gov/HOTLINE)

If you fear reprisal, contact the  
OIG Whistleblower Ombudsman to learn more about your rights:

[OIGWPEAOmbuds@state.gov](mailto:OIGWPEAOmbuds@state.gov)

[oig.state.gov](https://oig.state.gov)

Office of Inspector General • U.S. Department of State • P.O. Box 9778 • Arlington, VA 22219

UNCLASSIFIED