

SIGAR

**Special Inspector General for
Afghanistan Reconstruction**

SIGAR 14-32 Audit Report

**Direct Assistance: USAID Has Taken Positive Action to
Assess Afghan Ministries' Ability to Manage Donor Funds,
but Concerns Remain**



**JANUARY
2014**

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Special Inspector General for
Afghanistan Reconstruction

WHAT SIGAR REVIEWED

The U.S. government has committed to providing at least 50 percent of its development aid to Afghanistan through on-budget assistance to the Afghan government. On-budget assistance includes (1) direct assistance, which is comprised of host country contracts and government-to-government awards and is the focus of this audit; (2) contributions to multi-donor trust funds; and (3) direct budget support. As of August 2013, the U.S. Agency for International Development (USAID) had commitments of \$1.6 billion in direct assistance to 18 programs across 10 Afghan ministries and other government entities. Since 2010, both Congress and USAID have strengthened policies to regulate direct assistance.

In an effort to improve accountability and meet congressional requirements, USAID contracted with Ernst & Young and KPMG in late 2010 and early 2011 to assess 16 Afghan ministries' abilities to manage U.S. funds. In addition, to help ensure the proper management and implementation of direct assistance worldwide, USAID developed *Automated Directives System 220: Use of Reliable Partner Country Systems for Direct Management and Implementation of Assistance* in August 2011.

JANUARY 2014

Direct Assistance: USAID Has Taken Positive Action to Assess Afghan Ministries' Ability to Manage Donor Funds, but Concerns Remain

SIGAR 14-32 AUDIT REPORT

WHAT SIGAR FOUND

From January 2011 to August 2013, Ernst & Young and KPMG completed public financial management assessments of 16 Afghan ministries. Both contractors, who met almost all contract requirements, concluded that all of the 16 ministries assessed were unable to manage and account for funds unless they implemented recommendations included in the public financial management assessment reports. In the 16 public financial management assessments, Ernst & Young and KPMG identified 696 total recommendations for corrective action, ranging from 24 for Da Afghanistan Breshna Sherkat (Afghanistan's national power utility) to 63 for the Ministry of Public Health. Of these, the contractors rated 41 percent of the recommendations as "critical" or "high risk."

Following the completion of these assessment reports, USAID/Afghanistan completed internal risk reviews of 7 of the 16 Afghan ministries—the Ministry of Public Health; the Ministry of Mines and Petroleum; the Ministry of Agriculture, Irrigation, and Livestock; the Ministry of Communication and Information Technology; the Ministry of Education; the Ministry of Finance; and Da Afghanistan Breshna Sherkat. These 7 ministries all have planned or active direct assistance programs. The risk reviews found 104 major risks—such as "concealing vital monitoring and evaluation information" and "misappropriation of cash arising from payment of salaries in cash"—with 99 of the risks rated either critical or high. USAID/Afghanistan prescribed 333 total mitigating measures to address the identified risks. Although USAID/Afghanistan concluded in each of the seven risk reviews that the ministry was unable to manage direct assistance funds without a risk mitigation strategy in place and that the mission would not award direct assistance to the ministry "under normal circumstances," USAID/Afghanistan signed agreements with each of the reviewed ministries to approve direct assistance programs.

In addition, in 2012, USAID waived Automated Directives System (ADS) 220 requirements in Afghanistan for all direct assistance funds through fiscal year 2013. ADS 220 established the Public Financial Management Risk Assessment Framework—a multi-stage, risk-based methodology that USAID uses to assess partner country systems' suitability for receiving direct assistance. The agency justified the waiver by stating the U.S. foreign policy objectives were to provide direct assistance to Afghanistan, thus rendering the initial macro-level review of Afghanistan's risk environment

The objectives of this audit were to (1) assess the extent to which Ernst & Young and KPMG adhered to USAID contract requirements when conducting the ministry assessments, (2) describe assessment findings and conclusions about the ability of the Afghan ministries to manage U.S. funds and analyze how USAID has used, or plans to use, the assessments to inform its direct assistance to the Afghan government, and (3) examine the U.S. Department of State's certification and USAID's notification provided to Congress, pursuant to congressional requirements for providing direct assistance to the Afghan government.

unnecessary. Despite the waiver, agency officials stated they still complied with the spirit of the remaining ADS 220 requirements. However, USAID did not conduct quality control reviews of the public financial management assessments, USAID/Afghanistan's risk reviews, or any risk mitigation strategies, as required under ADS 220.

Although all Afghan ministries receiving direct assistance met conditions precedent—actions USAID requires ministries to take prior to the initial disbursement of funds—before USAID disbursed money to them, SIGAR found that USAID/Afghanistan has only required the ministries to implement 24 of the 333 recommended risk mitigation measures prior to receiving funds. USAID takes additional external measures intended to mitigate risks associated with providing direct assistance to the ministries, such as establishing separate bank accounts and providing funds on a reimbursement basis. However,

these measures do not address the underlying problems within the ministries and, as such do little to build ministries' organic capabilities to manage donor funds—one of the primary purposes of providing on-budget assistance to the Afghan government. Moreover, the effectiveness of USAID's external risk mitigation measures may be limited by ongoing problems within the ministries. For example, one of USAID's additional risk mitigation measures is developing a written monitoring and evaluation plan for each of its direct assistance programs with the ministries. However, if, as was found in the Ministry of Public Health, there is a risk of the ministry "concealing vital monitoring and evaluation information," this external measure will be ineffective in safeguarding funds.

After a preliminary briefing on SIGAR's findings, USAID/Afghanistan provided documentation delineating how it has or will mitigate each of the risks identified in its review of Da Afghanistan Breshna Sherkat. This is a positive development, but USAID/Afghanistan has not developed similar mitigation plans that identify how it will address the remaining risks for the other ministries it reviewed.

The State Department and USAID complied with the statutory requirements for fiscal years 2011 and 2012 to inform Congress that they (1) have assessed Afghan ministries designated to receive direct assistance and (2) consider the ministries qualified to manage the assistance prior to disbursing any fiscal year 2011 or fiscal year 2012 funds. However, some of the information in the fiscal year 2011 certification by the Secretary of State and USAID's fiscal year 2012 notification was inaccurate or, at least, incomplete. Specifically, the fiscal year 2011 certification and fiscal year 2012 notification stated that the Ministries of Finance and Higher Education had been assessed, even though USAID was still reviewing the assessment reports and Ernst & Young had not yet finalized them. Further, USAID notified Congress in November 2012 that, with the "successful implementation" of risk mitigation strategies, the Afghan ministries were qualified to manage direct assistance funds. However, neither the 2011 certification nor the 2012 notification to Congress disclosed the full extent of the risks identified at each of the ministries or that over 90 percent of the mitigating measures identified in the risk reviews had not been implemented. For example, USAID's notification did not disclose that the majority of measures intended to mitigate the identified risks had not been implemented at the time of the notification, even though the 2012 limitation on direct assistance states that funds may be made available for direct assistance to an Afghan government ministry only if "any identified vulnerabilities or weaknesses of such agency or ministry *have been addressed.*" The decision to continue with direct assistance seemingly conflicts with the 2012 congressional requirement, which mandates that funds be made available "only if...no level of acceptable fraud is assumed." Without full information on the ministries' capabilities and the risks associated with providing direct assistance to these ministries, Congress's oversight of the over \$600 million in U.S. funds that USAID has obligated to date is compromised.

WHAT SIGAR RECOMMENDS

SIGAR recommends that the USAID Administrator (1) require compliance with all parts of ADS 220—except for the Stage 1 macro-level review—for the use of all direct assistance funds for fiscal year 2014 and beyond. SIGAR also recommends that USAID/Afghanistan (2) fully inform Congress of the status of ministry assessments USAID or its contractors have completed, the mitigating measures Afghan ministries have implemented, and the level of risk to U.S. funds; and (3) develop a risk mitigation plan, similar to the one created for Da Afghanistan Breshna Shekat, for each Afghan ministry that has a completed USAID risk review that defines how each of the risks identified are being or will be mitigated, and suspend direct assistance disbursements to these ministries until these plans are completed.

USAID agreed with all three recommendations, but also indicated that it has already complied with each. SIGAR disagrees with USAID’s assertion. For example, while USAID states that it has complied with all parts of ADS 220—except for the Stage 1 macro-level review—SIGAR found that USAID headquarters staff did not conduct quality control reviews of the public financial management assessments, risk reviews, or any risk mitigation strategies, as called for under ADS 220. SIGAR will continue to monitor USAID’s efforts to determine whether the agency has fully implemented the recommendations.

USAID commented that it has designated the ministry assessments and the internal risk reviews as “Sensitive But Unclassified” (SBU), and requested SIGAR to withhold this information and the related portions of this audit report from public release because “release of these materials will likely result in reduced cooperation from the Afghan Government.” However, the State Department’s Foreign Affairs Manual provides that if public release of this information would harm foreign relations, then it must be classified to be exempt from disclosure and “[t]he SBU label cannot be used instead of classification to protect such information.” Therefore, since USAID has specifically designated this information as “unclassified,” SIGAR will not withhold it from public release.

Timeline of Ministry Assessments and USAID Stage 2 Risk Reviews



Source: SIGAR Analysis of USAID direct assistance contracts, agreements, assessments, and risk reviews.



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January 30, 2014

The Honorable John Kerry
Secretary of State

The Honorable James B. Cunningham
U.S. Ambassador to Afghanistan

Dr. Rajiv Shah
Administrator, U.S. Agency for International Development

Mr. William Hammink
USAID Mission Director for Afghanistan

This report discusses the results of SIGAR's audit of the U.S. Agency for International Development's (USAID) process for conducting and using ministerial assessments when awarding U.S. direct assistance to the Afghan government.

The U.S. government has committed to providing at least 50 percent of development aid to Afghanistan through on-budget assistance—funding that is channeled through the Afghan government's core budget and that is designed to allow the Afghans more freedom to manage their own budget and to build their capacity for doing so. The cornerstone of this effort is USAID's direct government-to-government assistance program. Congress has taken a strong interest in this program and, in the interest of protecting the taxpayer's money, has stated very clearly that funds may be made available for direct assistance "only if . . . each implementing agency or ministry to receive assistance has been assessed and is considered to have the systems required to manage such assistance and any identified vulnerabilities or weaknesses of such agency or ministry have been addressed."

We found in this audit that, although USAID has taken positive steps to assess Afghan ministries' capabilities to manage donor funds, it has not required the ministries to fix most of the risks identified through these assessments. Specifically, USAID determined it could not rely on the ministries it assessed to manage donor funds without a host of mitigation measures in place and that, under normal circumstances, the results of the assessments would lead USAID not to engage in direct assistance with the ministries. However, USAID proceeded to sign direct assistance agreements with seven ministries, only requiring them to implement less than eight percent of identified risk mitigation measures prior to receiving funds. While we are aware that USAID has additional external measures intended to mitigate the risks associated with providing direct assistance funds to these ministries, these measures do not directly address all of the very serious problems within the ministries and could well be exploited or circumvented, given the high risk of corruption revealed through USAID's assessments.

In an effort to strengthen USAID's direct assistance program, we are making three recommendations in this report. Specifically, SIGAR recommends that the USAID Administrator require compliance with all parts of ADS 220—except for the Stage 1 macro-level review—for the use of all direct assistance funds for fiscal year 2014 and beyond. SIGAR also



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recommends that the Mission Director for USAID/Afghanistan fully inform Congress of the status of ministry assessments USAID or its contractors have completed, the mitigating measures Afghan ministries have implemented, and the level of risk to U.S. funds. SIGAR further recommends that the Mission Director develop a risk mitigation plan, similar to the one created for Da Afghanistan Breshna Shekat, for each Afghan ministry that has a completed USAID risk review that defines how each of the risks identified is or will be mitigated, and suspend direct assistance disbursements to these ministries until these plans are completed.

We appreciate USAID's written comments on a draft of this report, as well as the close cooperation that we received throughout the course of this audit. From the very beginning of this audit, we have taken extraordinary measures to ensure that the information provided by USAID is thoroughly, accurately, and responsibly represented. Therefore, I want to directly address one of the points made in USAID's comment letter—our treatment of SBU information.

USAID designated the ministry assessments and the internal risk reviews as "Sensitive But Unclassified" (SBU), and requested SIGAR to withhold this information and the related portions of our audit report from public release because "release of these materials will likely result in reduced cooperation from the Afghan Government." In the very same written comments, USAID also asserted that those same ministry assessments and internal risk reviews "were generated for the internal use of the US Government *and the entities that are the subject of the assessments.*" Moreover, when USAID provided copies of the ministry assessments to SIGAR auditors, every one of those assessments bore a cover sheet requesting SIGAR to "not distribute . . . these documents . . . outside the executive branch."

In other words, USAID's view is that this information can be given to the Afghan government, but not to Congress or the American public. I simply cannot find any support for this proposition in the law or as a matter of good public policy.

USAID also asserted that "parts of the Afghan government provided unprecedented access for the independent auditors to complete the risk assessments based on understandings that the results of the risk assessments would not be made public." However, despite repeated requests from SIGAR, USAID has not provided any documentary evidence that it promised the Afghan government that this information would be withheld from the public.

The State Department's own regulations, as contained in the Foreign Affairs Manual, provide that if the release of information obtained from a foreign government would harm foreign relations, "then it must be classified in order to be exempt from release The SBU label cannot be used instead of classification to protect such information." Since USAID has specifically designated this information as "unclassified," SIGAR will not censor or otherwise withhold portions of our audit report from the public.

Frankly, USAID's continued insistence that SIGAR withhold this information from Congress and the public may undermine the credibility of its assertions that it has appropriately mitigated the risks uncovered by the ministry assessments and its internal risk reviews.

USAID's comments, along with our responses, are reproduced in appendix XVI. In its comments, the agency agreed with the recommendations. However, the agency also indicated it is already complying with the each of the recommendations and requested that SIGAR close them. We disagree with the agency's assertion that it has fully complied with the recommendations, and we will continue to monitor USAID's efforts to determine whether the agency has fully implemented our recommendations.



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We conducted this performance audit under the authority of Public Law No. 110-181, as amended, and the Inspector General Act of 1978, as amended, and in accordance with generally accepted government auditing standards.

A handwritten signature in black ink, appearing to read "John F. Sopko". The signature is stylized and fluid.

John F. Sopko
Special Inspector General
for Afghanistan Reconstruction

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ABBREVIATIONS

ADS	Automated Directive System
AUPCS	Approval of Use of Partner Country Systems
CUI	Controlled Unclassified Information
FOIA	Freedom of Information Act
SBU	Sensitive but Unclassified
USAID	U.S. Agency for International Development
USAID/Afghanistan	USAID Mission for Afghanistan

ABBREVIATIONS FOR AFGHAN MINISTRIES AND GOVERNMENT ENTITIES

AIHRC	Afghanistan Independent Human Rights Commission
DABS	Da Afghanistan Breshna Sherkat
IARCSC	Independent Administrative Reform and Civil Service Commission
MAIL	Ministry of Agriculture, Irrigation, and Livestock
MEW	Ministry of Energy and Water
MOCIT	Ministry of Communication and Information Technology
MOE	Ministry of Education
MOEC	Ministry of the Economy
MOF	Ministry of Finance
MOHE	Ministry of Higher Education
MOIC	Ministry of Information and Culture
MOMP	Ministry of Mines and Petroleum
MOPH	Ministry of Public Health
MOPW	Ministry of Public Works
MOTCA	Ministry of Transport and Civil Aviation
MRRD	Ministry of Rural Rehabilitation and Development

At the 2010 London Conference, the international community, including the United States, stated its commitment to providing at least 50 percent of development aid to Afghanistan through on-budget assistance—funding that is channeled through the Afghan government’s core budget. On-budget assistance is designed to allow the Afghans more freedom to manage their own budget and to build their capacity for doing so. On-budget assistance can take many forms, including direct bilateral assistance, contributions to multi-donor trust funds, and direct budget support. Direct bilateral assistance—hereafter referred to as direct assistance—includes government-to-government funding and host country contracts.¹ As of August 1, 2013, the U.S. Agency for International Development (USAID) had committed \$1.6 billion in direct assistance to the Afghan government.² On-budget assistance raises a number of concerns, in part because funds provided on-budget are typically subject to less U.S. and international donor control and oversight than funds provided through projects implemented by the United States and other international donors, leaving them particularly vulnerable to waste, fraud, and abuse. In order to assess Afghan ministries’ ability to manage U.S. funds, USAID contracted with Ernst & Young and KPMG in late 2010 and early 2011 to assess 16 Afghan ministries.³

The objectives of this audit were to (1) assess the extent to which Ernst & Young and KPMG adhered to USAID contract requirements when conducting the ministry assessments, (2) describe the assessment findings and conclusions about the ability of the Afghan ministries to manage U.S. funds and analyze how USAID has used, or plans to use, the assessments to help inform its assistance to the Afghan government, and (3) examine the U.S. Department of State’s certification and USAID’s notification provided to Congress, pursuant to congressional requirements. We did not intend for this audit to examine the implementation of USAID-funded direct assistance programs, assess the effectiveness of USAID’s methods for safeguarding U.S. direct assistance funds, or determine whether fraud and misuse of funds existed within these programs.⁴

To accomplish these objectives, we reviewed congressional requirements for providing direct assistance as defined in the Fiscal Year 2010 Consolidated Appropriations Act, the Fiscal Year 2011 Department of Defense and Full-Year Continuing Appropriations Act, and the Fiscal Year 2012 Consolidated Appropriations Act.⁵ We also reviewed USAID’s policies governing direct assistance in Afghanistan. We analyzed Ernst & Young’s and KPMG’s public financial management assessments of 16 ministries and their associated contracts with USAID, as well as USAID’s risk reviews of seven Afghan ministries and implementation letters for eight ongoing direct assistance programs. We reviewed Ernst & Young’s and KPMG’s working papers, including draft reports, internal control testing documentation, and correspondence with the ministries and USAID. We also reviewed USAID’s contractor performance assessment reports for Ernst & Young and KPMG, as well as correspondence between the agency and the contractors. We met with officials in USAID’s Office of Afghanistan and Pakistan Affairs and USAID/Afghanistan’s Office of Financial Management, Office of Program and Project Development, and on-budget monitors. In addition, we met with Afghan officials at the Ministry of Agriculture, Irrigation, and Livestock; the Ministry of Finance; the Ministry of Mines and Petroleum; and Da Afghanistan Breshna Sherkat—Afghanistan’s national power utility. We conducted our work in Washington, D.C. and Kabul, Afghanistan, from

¹ Under a host country contract, USAID is not a party to contractual arrangements between the host country and suppliers of goods and services.

² This \$1.6 billion represents commitments to ongoing direct assistance programs for which USAID has not confirmed program completion dates. In commenting on a draft of this report, USAID stated that its commitments for direct assistance have dropped to \$1.06 billion.

³ In this report, we refer to all Afghan government entities as “ministries,” including Da Afghanistan Breshna Sherkat (Afghanistan’s national power utility), the Independent Administrative Reform and Civil Service Commission, and the Independent Directorate of Local Governance. As of September 1, 2013, assessments for the Ministry of Justice and the Supreme Court were still in progress.

⁴ SIGAR currently has an audit examining the safeguards that various U.S. agencies, including USAID, have in place to protect on-budget funds provided to the Afghan government from waste, fraud, and abuse. That audit will result in a final report in early 2014.

⁵ Consolidated Appropriations Act, 2010, Pub. L. No. 111-117, 123 Stat. 3034, 3329 (2009); Department of Defense and Full-Year Continuing Appropriations Act, 2011, Pub. L. No. 112-10, § 2121(b), 125 Stat. 38, 184 (2011); Consolidated Appropriations Act, 2012, Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

April 2013 to January 2014, in accordance with generally accepted government auditing standards. A more detailed discussion of our scope and methodology is in appendix I.

BACKGROUND

At the 2010 London Conference, the United States and other members of the international community stated their commitment to providing 50 percent of development aid to Afghanistan through on-budget assistance and reaffirmed this commitment at the 2010 Kabul and 2012 Tokyo Conferences. USAID's Performance Management Plan and its 2013 progress report, *USAID Forward*, both reiterate the U.S. government's intent to provide more than 50 percent of its assistance through Afghan government systems.

In line with these commitments, a major component of the U.S. government's approach to reconstruction in Afghanistan involves supporting the Afghan government, as appropriate, so it can take increasing ownership for development and sustain any reconstruction gains over the past decade. On-budget assistance to the Afghan government can encompass several types of funding mechanisms, including donations to multi-donor trust funds, direct budget support, and direct assistance. USAID officials stated that the agency does not award direct budget support, which it defines as "funds provided directly to a foreign government to be used by that government at its discretion and without further U.S. oversight."⁶ Instead, USAID awards on-budget assistance in Afghanistan exclusively through donations to multi-donor trust funds and direct assistance agreements. Direct assistance includes host country contracting and government-to-government assistance. Direct assistance is aid that the agency implements through bilateral agreements with an Afghan government entity and under national arrangements covering public financial management systems at both national and ministerial or sectoral levels.

When USAID first committed in 2005 to increasing the amount of on-budget assistance it planned to provide the Afghan government, the USAID Mission for Afghanistan (USAID/Afghanistan) used host country contracting, which is one method for financing and implementing projects.⁷ USAID used host country contracting for direct assistance agreements for only two programs—one with the Ministry of Public Health and one with the Ministry of Communication and Information Technology.⁸ As of August 2013, USAID had obligated almost \$659 million to seven ministries for eight active direct assistance programs and planned to commit an additional \$237 million to these programs.⁹ The agency had committed another \$780.7 million for 10 planned programs, for a total of \$1.6 million in commitments for the 18 active and planned direct assistance programs.¹⁰

⁶ USAID information provided to SIGAR, September 2013. USAID's *ADS Glossary* does not contain a definition of on-budget, direct assistance, and budget support.

⁷ USAID Automated Directives System 301 *Procurement Responsibilities* and Automated Directives System 305 *Host Country Contracts*. USAID's host country contracting policies require reviews of all recipient ministries' procurement systems.

⁸ USAID officials told us that host country contracting was used before the development of ADS 220, and USAID is moving away from host country contracting and toward cost-reimbursable direct assistance, the latter of which is the focus of this report. The Ministry of Public Health is the only ministry with an active program funded as a host country contract. Funding for the Ministry of Communication and Information Technology's program ended in fiscal year 2004.

⁹ USAID has disbursed an additional \$25.2 million to five completed direct assistance programs and one suspended direct assistance program at five ministries. See appendix III for information on these completed and suspended direct assistance programs. According to USAID's *ADS Glossary*, an obligation is a legal liability of the government for the payment of funds for specific goods or services ordered or received. It includes a range of transactions, such as contracts, grants, and loans. In contrast, a commitment is an administrative reservation of funds in anticipation of their obligation.

¹⁰ See appendix III for more information on USAID's direct funding and active programs.

Limitations on USAID's Direct Assistance to the Afghan Government

USAID and the government of Afghanistan signed a memorandum of understanding in December 2010 in support of the goals, objectives, and mechanisms for effective assistance to Afghanistan. The memorandum of understanding focused on maximizing opportunities presented by USAID-funded assistance to increase capacity, institutional growth, and public ownership of the development process in Afghanistan. The memorandum also laid out 13 financial requirements to ensure that direct assistance funds are used as intended. For example, the requirements specified that the Afghan government return unspent funds to USAID, grant USAID access rights to any special bank accounts established for direct assistance programs, and maintain accounting records in accordance with agreed-upon standards for 3 years after the last disbursement. Additionally, the memorandum required that the Afghan government work with USAID to both design satisfactory responses to recommendations by USAID for any pre-award assessments and to establish a monitoring and evaluation plan specific to each activity for which direct assistance funds will be used. Furthermore, under the memorandum, USAID reserved the right to suspend or terminate a direct assistance-funded activity or obtain a refund should terms of the activity be breached; to carry out third party evaluations of direct assistance activities; and to only release funds when adequate supporting documentation is submitted to USAID.¹¹

In 2011, USAID issued *Automated Directives System (ADS) 220: Use of Reliable Partner Country Systems for Direct Management and Implementation of Assistance* to provide internal policy directives and required procedures for managing and implementing direct assistance.¹² ADS 220 established the Public Financial Management Risk Assessment Framework—a multi-stage, risk-based methodology that USAID uses to assess partner country systems suitability for receiving direct assistance. Stage 1 of this framework is a macro-level analysis of the risk environment of the partner country that provides a USAID mission with a high-level perspective of the risks associated with use of the partner country's systems. Stage 2 is a more in-depth ministry-level review undertaken to gain a detailed understanding of an individual ministry. The Stage 2 assessment concludes with a determination by the USAID mission of whether that ministry is capable of handling U.S. direct assistance funding. If the USAID mission concludes that a ministry is capable of handling direct assistance funding, then the USAID mission grants an "Approval of Use of Partner Country Systems" (AUPCS). An AUPCS constitutes formal approval for the use of a partner country's public financial management system, but is not an agreement to actually disburse funds.

Once the ministry has been approved to receive direct assistance, the USAID mission then completes the remaining stages of ADS 220's public financial management risk assessment framework. During Stages 3, 4, and 5, the mission determines an appropriate program design; negotiates and prepares a funding agreement with the partner country; and implements, monitors, and evaluates the direct assistance program.

In addition to USAID's internal requirements defined in ADS 220, USAID is required to respect the limitations Congress has placed on direct assistance to Afghanistan. For fiscal year 2010, Congress conditioned the availability of funds for direct assistance on the Secretary of State certifying that the U.S. and Afghan governments have agreed to clear and achievable goals and objectives for the use of direct assistance, and have established mechanisms within each implementing agency to ensure funds are used for their intended purpose.¹³ In fiscal year 2011, Congress added the condition that the Secretary of State also certify that "the relevant implementing [Afghan ministries] have been assessed and considered qualified to manage such funds."¹⁴ For fiscal year 2012, Congress conditioned the availability of funds for direct assistance to

¹¹ This audit did not assess USAID's compliance with all of these requirements. We initiated a separate audit in June 2013 to examine the process by which U.S. agencies provide direct assistance funds to the Afghan government and the internal controls put in place to safeguard these funds, including many of the requirements contained in the December 2010 memorandum of understanding between USAID and the government of Afghanistan.

¹² USAID finalized ADS 220 in August 2011, and updated it in March 2012.

¹³ Pub. L. No. 111-117, 123 Stat. 3034, 3329 (2009).

¹⁴ Pub. L. No. 112-10, § 2121(b), 125 Stat. 38, 184 (2011).

Afghanistan on a detailed notification to Congress concerning efforts to protect direct assistance funds from waste, fraud, and abuse.¹⁵ For example, the 2012 limitation on direct assistance specified that funds may be made available for direct assistance “only if . . . each implementing agency or ministry to receive assistance has been assessed and is considered to have the systems required to manage such assistance and any identified vulnerabilities or weaknesses of such agency or ministry have been addressed.”¹⁶ Furthermore, the limitation states that funds be made available only if “effective monitoring and evaluation systems are in place to ensure that such assistance is used for its intended purposes and no level of acceptable fraud is assumed.”¹⁷ The 2012 limitation also included a requirement to ensure that each ministry adopts competitive procurement policies and systems. Appendix II contains more information on the requirements for direct assistance.

USAID’s Ministry Assessments and Risk Review Processes

Beginning in 2010, USAID/Afghanistan issued contracts for third-party firms to conduct public financial management assessments of Afghan ministries’ abilities to manage and administer direct assistance funds. Between January 2011 and August 2013, Ernst & Young and KPMG completed public financial management assessments of 16 Afghan ministries under contracts with USAID/Afghanistan.¹⁸ Using these assessments, USAID/Afghanistan then conducted internal risk reviews of seven ministries in order to inform its decision of whether to provide direct assistance funds to those ministries.¹⁹ These risk reviews include the mission’s conclusions and interpretations of the Ernst & Young and KPMG public financial management assessments. The risk reviews also identify major risks and mitigating strategies deemed necessary for ensuring that the ministries are able to manage U.S. direct assistance.²⁰

ERNST & YOUNG AND KPMG MET ALMOST ALL CONTRACT REQUIREMENTS

USAID’s contracts with Ernst & Young and KPMG to conduct the public financial management assessments required them to comply with between 19 and 27 reporting requirements.²¹ Among other things, the contracts required Ernst & Young and KPMG to provide conclusions on each ministry’s financial management capacity and accounting systems and to include the ministry management’s response to these conclusions. The contracts also required that Ernst & Young and KPMG recommend actions for correcting any identified weaknesses. Based on our review of the 16 completed public financial management assessment reports, we determined that Ernst & Young and KPMG met almost all of the contract requirements.²² However, the

¹⁵ Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

¹⁶ Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

¹⁷ Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

¹⁸ The 16 ministries assessed were the Afghanistan Independent Human Rights Commission, Da Afghanistan Breshna Sherkat, the Independent Administrative Reform and Civil Service Commission, and the Ministries of Agriculture, Irrigation, and Livestock; Communication and Information Technology; Education; Energy and Water; Economy; Finance; Higher Education; Information and Culture; Mines and Petroleum; Public Health; Transport and Civil Aviation; and Rural Rehabilitation and Development.

¹⁹ USAID completed risk reviews for Da Afghanistan Breshna Sherkat and the Ministries of Agriculture, Irrigation, and Livestock; Communication and Information Technology; Education; Finance; Mines and Petroleum; and Public Health.

²⁰ Appendix II includes additional information on the public financial management assessments and risk reviews.

²¹ The first contract with Ernst & Young, awarded in November 2010, to assess the Independent Administrative Reform and Civil Service Commission had 19 deliverables. The most recent contract with Ernst & Young, awarded in June 2012, to assess Da Afghanistan Breshna Sherkat has 27 deliverables.

²² See appendix IV for a full list of contract deliverables and the extent to which Ernst & Young and KPMG met these deliverables.

contractors did not fully meet the contract requirements related to assessing program costs because USAID/Afghanistan did not provide sufficient information to complete the requirement.

In 2010, USAID's Office of Inspector General reported that USAID ministry assessments should include an analysis of each ministry's capability to implement specific proposed programs, as well as increased measures to verify testing of internal controls.²³ In line with this recommendation, USAID's contracts with Ernst & Young and KPMG required the contractors to express their "conclusions on USAID's proposed [program] costs." In particular, the contractors were to identify findings and conclusions on proposed program costs and provide a summary of their program cost findings.

However, Ernst & Young officials told us USAID/Afghanistan did not provide any proposed program cost information that would have allowed them to analyze program costs. Therefore, with the exception of the Ministry of Transport and Civil Aviation assessment, none of the public financial management assessments contained an evaluation of proposed program costs, as required by the contracts' statements of work. According to USAID/Afghanistan officials, they had not proposed program costs because they first wanted to obtain information about the ministries' capabilities through the assessment process. They added that this requirement was included in the contracts by mistake due to a template error.

In addition to not providing program cost information to Ernst & Young and KPMG, USAID/Afghanistan took limited steps to verify the contractors' internal controls testing. In its 2010 report, USAID's Inspector General recommended that USAID/Afghanistan require contractors to reference the specific documentation that supports their assessments of the ministries. The USAID Inspector General also recommended that USAID supervisors approve contractor testing plans. Consistent with this recommendation, USAID/Afghanistan developed a public financial management risk assessment checklist with detailed steps for the contractors to use when conducting the ministerial assessments. The checklist included a field for "references" next to each step in the checklist that was intended to be used to refer to supporting documentation. The contracts required Ernst & Young and KPMG to complete the checklists. We found that Ernst & Young and KPMG completed this checklist for each of the 13 assessments when it was required and submitted the completed checklist to USAID/Afghanistan with the assessments.²⁴ However, rather than referring to detailed supporting documentation in the "references" field of the checklist, Ernst & Young and KPMG simply cited the corresponding section of their final reports.

We reviewed Ernst & Young's and KPMG's working papers and saw evidence that the contractors conducted walkthroughs and internal control testing and reviews to support their assessments of the Afghan ministries. Nevertheless, USAID/Afghanistan officials told us they did not request Ernst & Young's and KPMG's working papers to verify the responses on these checklists because agency officials were only concerned with the final report. Furthermore, USAID/Afghanistan did not implement the USAID Inspector General's recommendation that USAID supervisors approve contractor testing plans for the 16 assessments we reviewed. The only step USAID/Afghanistan officials reported taking to verify Ernst & Young's and KPMG's work was to meet with the contractors on a case-by-case basis to discuss their findings.

USAID/Afghanistan's limited verification of the contractors' testing reduced, to some extent, its ability to make fully informed decisions using the 16 public financial management assessments completed between January 2011 and August 2013. USAID/Afghanistan officials informed us in September 2013, after we completed our fieldwork, that they are now verifying contractor testing for assessments completed after August 1, 2013.

²³ USAID Office of Inspector General, *Review of USAID/Afghanistan's Ministerial Assessment Process*, F-306-11-001-S, November 6, 2010.

²⁴ USAID/Afghanistan's contracts with KPMG for the Afghanistan Independent Human Rights Commission, Independent Administrative and Civil Service Commission, and the Ministry of Transport and Civil Aviation assessments did not require the contractor to complete risk assessment checklists.

ALL MINISTRY ASSESSMENTS CONCLUDED THAT AFGHAN MINISTRIES ARE UNABLE TO MANAGE U.S. DIRECT ASSISTANCE FUNDS UNTIL IDENTIFIED RISKS ARE MITIGATED

Ernst & Young and KPMG completed public financial management assessments of 16 Afghan ministries between January 2011 and August 2013. In these assessments, the contractors evaluated the ministries' financial management and accounting systems, procurement and purchasing capabilities, human resources procedures, and governance and internal controls. Both contractors concluded that all ministries assessed were unable to manage and account for funds unless they implemented recommendations included in the public financial management assessment reports. Both contractors also stated that the material weaknesses identified in their reports "must be addressed as pre-award disbursement conditions."

Ernst & Young and KPMG identified 696 total recommendations for corrective action across the 16 ministries assessed.²⁵ For example, Ernst & Young recommended that the Ministry of Mines and Petroleum develop and implement a financial management and accounting system to enhance efficiency and reduce the risk of "intentional and unintentional errors." In another instance, KPMG recommended to the Ministry of Rural Rehabilitation and Development that variances between recorded and physical inventories should be reported to top management, and differences should be investigated and resolved. The number of recommendations for each ministry ranged from 24 for Da Afghanistan Breshna Sherkat to 63 for the Ministry of Public Health.

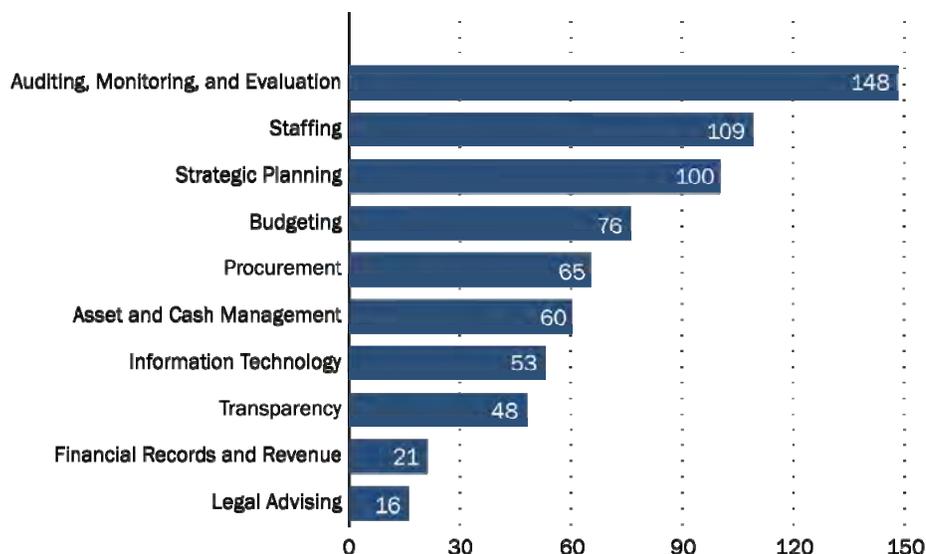
As part of their reviews, Ernst & Young and KPMG assigned risk ratings to these recommendations—rating them low, medium, high, or critical risk—based on the severity of the identified weaknesses.²⁶ Of the 696 recommendations, the contractors rated 239—or 41 percent—as critical or high risk. Furthermore, in the four KPMG assessments—completed for the Ministries of Communication and Information Technology, Energy and Water, Rural Rehabilitation and Development, and Transport and Civil Aviation—KPMG concluded that the ministries would still be "high risk" even if all recommendations in the report were implemented, and that funds provided to these ministries would need to be monitored as such.

Our analysis of Ernst & Young's and KPMG's recommendations identified persistent weaknesses, which we categorized into 10 major themes. The most common theme was "auditing, monitoring, and evaluation," with recommendations for improving audit procedures and monitoring reporting policies. Other prevalent themes were "staffing," "strategic planning," and "budgeting." Figure 1 shows the full breakdown of common weaknesses identified in Ernst & Young's and KPMG's recommendations.

²⁵ We analyzed recommendations, rather than key findings, because recommendations present both problems and methods for addressing these problems with a greater level of detail about each issue, allowing more accuracy when identifying common themes.

²⁶ Eleven of the 16 assessments did not include critical as a possible risk rating. Three ministries had instances where no risk rating was assigned, totaling 110 recommendations.

Figure 1 - Number of Weaknesses Found across Ernst & Young's and KPMG's Public Financial Management Assessments, by Theme



Source: SIGAR analysis of Ernst & Young's and KPMG's public financial management assessments.

USAID's Risk Reviews Found that the Afghan Ministries Were Unable to Manage Donor Funds and Lacked the Capability to Combat Corruption

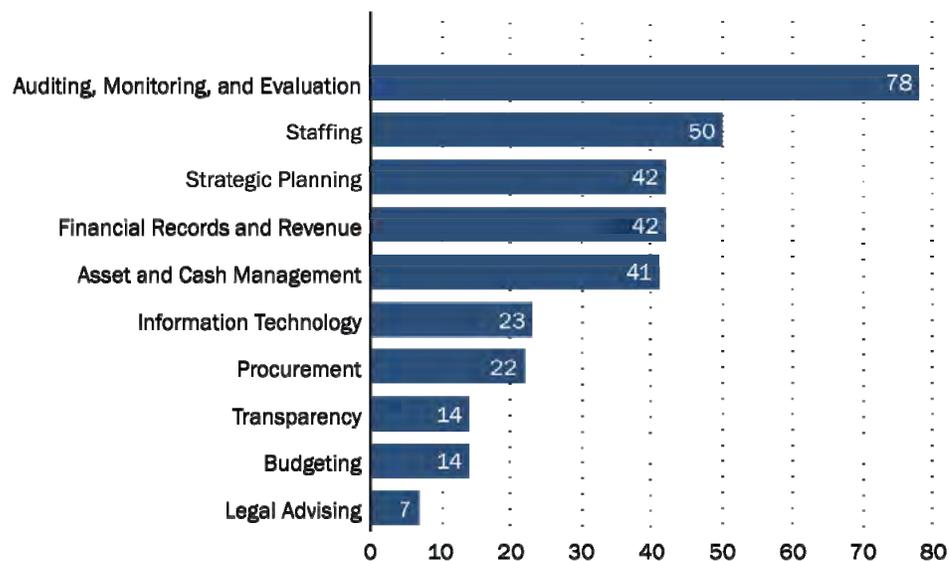
USAID/Afghanistan used Ernst & Young's and KPMG's public financial management assessments to complete risk reviews of the seven ministries that had active or planned direct assistance programs as of August 2013.²⁷ In its risk reviews, USAID/Afghanistan identified 104 major risks associated with relying on the ministries to manage donors' direct assistance funds. Risks for individual ministries ranged from 11 for the Ministry of Agriculture, Irrigation, and Livestock to 26 for the Ministry of Finance. Although the risks varied by ministry, they generally identified problems with the ministries' management and governance structures, financial management and accounting systems, personnel procedures, procurement and purchasing systems, and program management. For example, USAID/Afghanistan found that the Ministry of Public Health was at risk of "concealing vital monitoring and evaluation information" and "misappropriation of cash arising from payment of salaries in cash." In its review of the Ministry of Mines and Petroleum, USAID/Afghanistan noted that "waste, fraud, and abuse may go undetected" and identified the risk of "paying higher prices for commodities and services to finance kickbacks and bribes." Each risk review noted similar types of weaknesses. The mission rated 99 of the 104 risks, or about 95 percent, as "critical" or "high."²⁸

²⁷ The Independent Administrative Reform and Civil Service Commission has an active program, but USAID/Afghanistan had not completed a risk review of the commission or planned to do one, as of August 2013. The Supreme Court and Ministry of Justice have planned programs, and the contractors are still conducting public financial management assessments of these two ministries.

²⁸ USAID/Afghanistan assigned risk ratings based on the probability of an "adverse event associated with [a] risk" occurring, ranging from remote to frequent, combined with the adverse event's potential impact, ranging from negligible to catastrophic. Appendix V includes a matrix of how USAID/Afghanistan assigns risk ratings.

For every risk listed in its risk reviews, USAID/Afghanistan proposed corresponding mitigation measures that should be taken to address the problems found.²⁹ In total, USAID/Afghanistan identified 333 mitigating measures. These mitigating measures included, for example: conducting periodic inventory of fixed assets, developing written policies and procedures for monitoring and evaluation and disseminating notices to all staff, paying salaries through the banking system (instead of in cash), and clearly defining system access and implementing controls to restrict access to key functions. Figure 2 demonstrates that—similar to the public financial management assessment recommendations—the most prevalent theme of the risk reviews’ mitigation measures was “auditing, monitoring, and evaluation.”

Figure 2 - Number of Weaknesses Found across USAID's Risk Reviews, by Theme



Source: SIGAR analysis of USAID risk reviews.

Some of USAID/Afghanistan’s risk reviews also discussed each ministry’s ability and willingness to combat corruption. Specifically, USAID/Afghanistan found that Da Afghanistan Breshna Sherkat and the Ministries of Agriculture, Irrigation, and Livestock; Communication and Information Technology; Education; Mines and Petroleum; and Public Health had control environments that were “not adequate to mitigate risk of corruption.”³⁰ Of those ministries, USAID/Afghanistan only identified Da Afghanistan Breshna Sherkat as demonstrating, “to a certain degree, the will to address concerns that could lead to corrupt acts.” Risk reviews of the Ministries of Agriculture, Irrigation, and Livestock and of Mines and Petroleum stated it was unclear whether these ministries were willing to combat corruption; risk reviews of the Ministries of Communication and Information Technology, Education, and Public Health did not address willingness to combat corruption at all.

In its risk reviews, USAID/Afghanistan concluded that the U.S. government cannot rely—or, in the instance of the Ministry of Finance, “cannot fully rely”—on any of the seven reviewed ministries’ systems and internal controls to manage donor funds. With the exception of Da Afghanistan Breshna Sherkat and the Ministry of Finance, USAID/Afghanistan’s risk reviews stated that USAID would not award direct assistance to these ministries under normal circumstances because of these results. However, because “the determination [had] already been made” to engage in direct assistance with the ministries, USAID/Afghanistan determined that it

²⁹ Appendix VI indicates how many risks and mitigating measures USAID/Afghanistan identified for each ministry in its risk reviews.

³⁰ Unlike USAID’s other six risk reviews of Afghan ministries, USAID’s risk review of the Ministry of Finance does not discuss corruption.

could reasonably mitigate the identified risks by “approaching direct assistance with caution and conditions,” and proceeded to sign an AUPCS for each of the seven reviewed ministries.³¹

Although the AUPCS is not the final step in USAID’s process for providing direct assistance and does not constitute a funding agreement, it does constitute approval to use Afghan government systems to provide direct assistance. The USAID/Afghanistan Mission Director signed these seven approvals despite USAID/Afghanistan (1) concluding that it could not rely on these ministries to manage donor funds; (2) determining that six of the reviewed ministries did not have the ability to mitigate the risk of corruption; and (3) having specific questions about whether the Ministries of Mines and Petroleum and of Agriculture, Irrigation, and Livestock had the will to combat corruption. Appendices VII through XIII provide a more detailed overview of each of the ministries assessed, including a description of the ongoing and planned direct assistance programs at each ministry, the recommendations and conclusions of the contracted assessment of the ministry, the findings and conclusions of the ministry’s Stage 2 risk review, where applicable, and a list of the risk mitigation measures identified for the ministry through the risk review, where applicable.

USAID Waived Its Primary Internal Requirement for Providing Direct Assistance

ADS 220 requires USAID to take multiple steps before disbursing direct assistance funds to ensure that partner country systems are able to adequately manage direct assistance, including: (1) complete a Stage I rapid appraisal and a democracy, human rights and governance review, if a country does not meet the “democracy threshold” established by USAID, to determine whether direct assistance would empower a government at the expense of its people; (2) complete ministry level risk assessments and authorize an AUPCS for a particular ministry; (3) design and approve the program to be funded and select the funding mechanism; (4) negotiate and prepare a bilateral agreement with the partner country and develop a plan to address any identified risks; and (5) implement, monitor, and evaluate the direct assistance program.³² ADS 220 also states that “If the Public Financial Management assessment reveals clear evidence of vulnerabilities to corruption, but the partner country government fails to respond with appropriate policies and actions such as a code of government ethics and procurement integrity, robust financial controls, and prosecution of wrongdoers, use of partner country systems must not be authorized.”

In 2012, the USAID Administrator waived all ADS 220 requirements for all agency funds made available to USAID/Afghanistan through fiscal year 2013 appropriations.³³ According to USAID officials, this is the only waiver of its kind made by the agency. In its justification for waiving the ADS 220 requirements, the waiver states that fulfilling every step of the ADS 220 process “would undermine the U.S. Government’s foreign assistance and foreign policy objectives and is also unnecessary.” The waiver goes on to explain that it is unnecessary because the decision to provide direct assistance to Afghanistan “was made several years ago at the very highest levels of the U.S. Government.”³⁴

Because of the USAID waiver of ADS 220, USAID is only required to determine whether an Afghan ministry is capable of receiving U.S. direct assistance because of the funding conditions imposed by Congress in the annual appropriations acts. Although agency officials told us they are working to comply with the spirit of ADS 220, USAID headquarters staff did not conduct quality control reviews of the contracted public financial management assessments, USAID/Afghanistan’s risk reviews, or any risk mitigation strategies, as called for under ADS 220.³⁵ As a result, USAID does not have reasonable assurance that the ministries will be able to

³¹ USAID’s Stage 2 assessment of the Ministry of Mines, September 2012.

³² ADS 220 requires the Mission Director to sign an AUPCS for each ministry that is approved for direct assistance.

³³ A copy of the USAID waiver is included in Appendix XV.

³⁴ The waiver of ADS 220 states this decision was affirmed by the Secretary of State and the USAID Administrator at the Kabul Conference in July 2010.

³⁵ Quality control reviews would be conducted by the Global Partner Country Risk Assessment Team.

effectively manage and account for direct assistance. In August 2013, USAID officials told us they were considering whether to extend the ADS 220 waiver for fiscal year 2014 funds and beyond.

With the waiver in place, USAID/Afghanistan authorized AUPCSs, granting formal approval of the use of partner country systems for the seven ministries that had a completed risk review through fiscal year 2015.

USAID Required Afghan Ministries to Implement Less than Eight Percent of Identified Risk Mitigation Measures before Receiving Direct Assistance Funds

Following issuance of the AUPCSs, USAID/Afghanistan set the terms and conditions of its direct assistance agreements with the Afghan government through implementation letters.³⁶ In these letters, USAID/Afghanistan established “conditions precedent”—actions USAID requires ministries to take prior to the initial disbursement of funds—and “ongoing conditions”—actions USAID requires ministries to take after the initial disbursement of funds and prior to subsequent disbursements. These conditions precedent and ongoing conditions are USAID/Afghanistan’s primary method for addressing the underlying problems within the ministries identified through the risk reviews and, therefore, for strengthening the ministries’ capabilities to manage donor funds.

Definitions	
Conditions Precedent	Actions USAID requires ministries to take prior to the initial disbursement of funds
Ongoing Conditions	Actions USAID requires ministries to take after the initial disbursement of funds and prior to subsequent disbursements
Implementation Letter	Formal correspondence between USAID and another party following a formal agreement that obligates funding. Implementation letters also provide more detailed implementation procedures, providing details on terms of agreement, recording the completion of conditions precedent to disbursements, and approving funding commitments and mutually agreed upon modifications to program descriptions

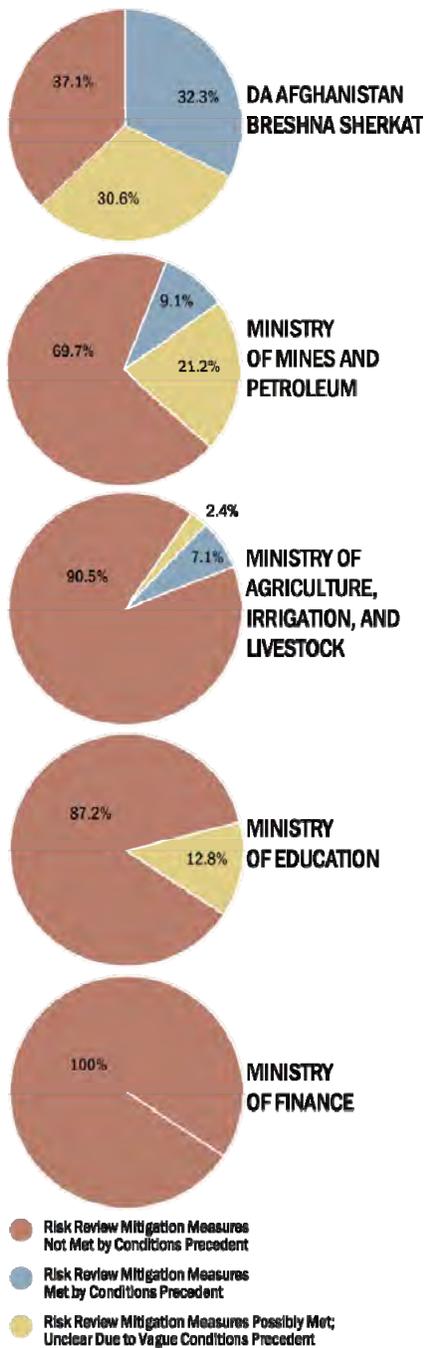
As noted above, for the 104 risks identified in USAID/Afghanistan’s risk reviews, the mission developed 333 possible mitigating measures that would address the identified problems within the seven ministries: Da Afghanistan Breshna Sherkat; Agriculture, Irrigation, and Livestock; Communication and Information Technology; Education; Finance; Mines and Petroleum; and Public Health. However, we determined that USAID/Afghanistan has only included 24—less than 8 percent—of the mitigation measures as conditions precedent in its implementation letters with those ministries.

To conduct our analysis, we compared each mitigation measure against each condition precedent. If the mitigation measure was to be carried out as a condition precedent, we counted the measure as being included. In some cases, the conditions precedent were too vague to be counted as having satisfied specific risk mitigation measures. In addition, while conditions precedent are program specific, USAID/Afghanistan’s identified mitigation measures often addressed the ministry as a whole. For example, one mitigation measure for the Ministry of Education called upon the ministry to establish a formal legal department. However, conditions precedent for the ministry’s active program were designed to safeguard funds for a textbook printing project and did not address the ministry’s lack of a legal department. Overall, we determined that the majority of mitigating measures were not satisfied by the conditions precedent.

As figure 3 on the following page illustrates, USAID/Afghanistan included 20, or 32 percent, of the 62 identified risk mitigation measures as conditions precedent in its implementation letters with Da Afghanistan Breshna

³⁶ All official communication with the ministries regarding these agreements is done through implementation letters.

Figure 3 - Risk Reviews Compared against Conditions Precedent, by Ministry



Note: The Ministry of Public Health and the Ministry of Communications and Information Technology currently have no conditions precedent because their programs were implemented as host country contracts.

Source: SIGAR analysis of USAID direct funding contracts, agreements, assessments, and risk reviews.

Sherkat. Based on our analysis, it is unclear whether an additional 19 mitigation measures for Da Afghanistan Breshna Sherkat were met due to the vague wording of the conditions precedent.

Of the six remaining ministries to receive an AUPCS, our analysis showed:

- The Ministry of Mines and Petroleum had three mitigating measures addressed by conditions precedent in its program implementation letters. It is unclear if an additional seven measures were addressed.
- The Ministry of Agriculture, Irrigation, and Livestock had one mitigating measure addressed by conditions precedent in its program implementation letters. It is unclear if an additional three measures were addressed.
- It is unclear if conditions precedent for the Ministry of Education addressed five mitigating measures USAID/Afghanistan identified in its risk review.
- Conditions precedent for the Ministry of Finance did not address any of the mitigating measures USAID/Afghanistan identified in its risk review.
- The Ministries of Communication and Information Technology’s and of Public Health’s implementation letters did not contain any conditions precedent. However, USAID/Afghanistan provided funding for these programs under the agency’s host country contract requirements.³⁷

Agency officials told us it would take substantial time and resources for the U.S. and Afghan governments to address all of the risks identified in the risk reviews before disbursing funds, which would delay execution of the U.S. government’s commitment to providing direct assistance and thereby the opportunity to increase Afghan ministerial capability.

We also analyzed the “ongoing conditions” to determine which, if any, of the mitigating measures would be addressed through these ongoing conditions. This analysis found that an additional 46, or 13.8 percent, of the risk mitigation measures were covered as ongoing conditions in the implementation letters. In other words, the ministries were required to implement these 46 measures *after* the initial disbursement of funds. Thirty-nine of the 46 mitigation measures that were covered as ongoing conditions were for Da Afghanistan Breshna Sherkat. Of the remaining seven risk mitigation measures:

³⁷ The active program at the Ministry of Public Health and a completed Ministry of Communications and Information Technology program were both implemented as host country contracts. While implementation letters for government-to-government direct assistance use conditions precedent, those for host country contracts do not because host country contracts are not subject to ADS 220. As a result, implementation letters for the Ministry of Public Health’s Partnership Contracts for Health Services program and the Ministry of Communications and Information Technology’s District Communication Network program do not contain conditions precedent.

- three were made requirements for the Ministry of Mines and Petroleum,
- three were made requirements for the Ministry of Education, and
- one was made a requirement for the Ministry of Agriculture, Irrigation, and Livestock.

In all, taking into account both conditions precedent and ongoing measures, USAID/Afghanistan only incorporated 70, or 21 percent, of the 333 mitigating measures into its agreements with the Afghan ministries. Appendices VII through XIII list the risk mitigating measures for each ministry and identify which were satisfied as conditions precedent or ongoing conditions.

As discussed above, conditions precedent are actions that a ministry must take before USAID/Afghanistan will disburse funds. These conditions are project specific. USAID/Afghanistan usually requires the ministries to complete the conditions precedent within 30 to 90 days after the implementation letter is signed. In addition, USAID/Afghanistan requires ministries to submit proof of completion and verifies that the conditions precedent are complete. It then communicates this verification via an implementation letter prior to disbursing funds. USAID has certified that:

- The Ministry of Finance met all conditions precedent for the Civil Service Technical Assistance Program prior to the first disbursement of funds in October 2009.
- The Ministry of Agriculture, Irrigation, and Livestock met all conditions precedent for the Agriculture Development Fund prior to the first disbursement of funds in February 2012.
- Da Afghanistan Breshna Sherkat met all of the conditions precedent for the Power Transmission Expansion and Connectivity and Kajaki Dam programs.³⁸
- The Ministry of Mines and Petroleum met all conditions precedent for the Shebergan Gas Development Project.³⁹

For the Ministry of Education’s Basic Education and Literacy and Vocational Education and Training Textbook Printing program, USAID/Afghanistan issued an implementation letter stating that the ministry had met all conditions precedent prior to the first disbursement of funds for this program in February 2012. However, USAID/Afghanistan subsequently determined that the ministry had not met all conditions satisfactorily. USAID/Afghanistan, therefore, withheld the remaining funding for this program from the ministry until it met all of the outstanding conditions precedent, as well as some additional ones. In June 2013, USAID/Afghanistan verified that the ministry had met all conditions precedent for the program.

Although the seven ministries met all conditions precedent before USAID disbursed funds, we find it concerning that USAID/Afghanistan included less than eight percent of the mitigation measures it identified in its risk reviews as conditions precedent in the program implementation letters.

Best Practice: USAID Created a Detailed Risk Mitigation Plan for One Ministry

After we briefed USAID on the preliminary results of our work and raised concerns that it did not have detailed plans in place to address the problems identified through the risk reviews, USAID/Afghanistan provided us a plan showing how it has mitigated or will mitigate each of the risks identified in its risk review of Da Afghanistan Breshna Sherkat. The risk mitigation plan for Da Afghanistan Breshna Sherkat is a best practice because it delineates how the risks associated with relying on ministries to manage direct assistance will be mitigated using existing conditions precedent, ongoing conditions, and agreements with the Afghan government. The AUPCS for Da Afghanistan Breshna Sherkat also states “all identified risks” deemed as “high” by USAID will be “implemented prior to or concurrent with the disbursing [of] U.S. government funds to assure maximum protection of U.S. taxpayer dollars.”

However, USAID/Afghanistan did not provide us with similar documentation demonstrating how it is mitigating the risks identified for the other six ministries with a USAID risk review. By not ensuring that similar plans are in

³⁸ As of August 1, 2013, USAID had not disbursed any funds for these programs.

³⁹ As of August 1, 2013, USAID had not disbursed any funds for this program.

place to mitigate the risks associated with vulnerabilities identified in the remaining six risk reviews, USAID is not doing everything it could to ensure the proper use of over \$600 million in direct assistance obligations.

USAID Reports Taking Additional Steps to Ensure Ministries Use Direct Assistance Funds for Intended Purposes

According to agency officials, USAID/Afghanistan relies on alternative means to safeguard direct assistance funds, which vary depending on the specific type of direct assistance used, such as government-to-government assistance or host-country contracting. These methods include building ministry capability through off-budget programs USAID directly funds and manages, rather than through direct assistance to the ministry; providing funds on a reimbursable basis; establishing separate bank accounts to be used solely for specific programs; and maintaining the legal authority to audit any financial records and documents related to the direct assistance program.

In addition, consistent with the 2010 memorandum of understanding between USAID and Afghanistan, both parties confirmed they would establish a monitoring and evaluation plan specific to each program receiving direct assistance funds.⁴⁰ As of August 1, 2013, four of the seven ministries with active direct assistance programs—the Ministry of Finance, Ministry of Education, Ministry of Public Health, and the Ministry of Agriculture, Irrigation and Livestock—had developed written monitoring and evaluation plans specific to their direct assistance program. USAID/Afghanistan plans to rely primarily on the conditions precedent for the three ministries—Da Afghanistan Breshna Sherkat, Ministry of Mines and Petroleum, and Independent Administrative Reform and Civil Service Commission—that do not have monitoring and evaluations plans. For these three ministries, USAID/Afghanistan also intends to use construction management consultants and quality assurance contractors, as well as USAID on-budget monitors and contracting officers and representatives to monitor and evaluate those ministries' programs.

While these additional steps are intended to safeguard direct assistance funds from waste, fraud, and abuse, it is important to note that they are primarily external measures and, as such, do not directly address the underlying problems within the ministries identified through the risk reviews. In other words, they do little to build ministries' organic capabilities to manage donor funds—one of the primary purposes of providing on-budget assistance to the Afghan government. To illustrate, the risk mitigation measures included in USAID's risk review of the Ministry of Agriculture, Irrigation, and Livestock identified several concrete actions that the ministry could take to address its internal problems. These actions included, among others, "define and restrict systems access to staff according to their roles and functions," "develop a policy for accounting for revenue," and "verify that adequate reference checks have been made on every prospective employee and properly documented." None of USAID's external measures—whether it be creation of separate bank accounts or distribution of funds on a reimbursement basis—would require the ministry to implement these basic and important steps. Notably, USAID's seven AUPCSs state that "*all* [emphasis added] identified risks will be mitigated."

Moreover, the effectiveness of USAID's external risk mitigation measures may be limited by ongoing problems within the ministries. For example, although USAID has developed a written monitoring and evaluation plan specific to its direct assistance program with the Ministry of Public Health—as it has with a number of other ministries—USAID's risk review of that ministry found there was a serious risk of the ministry "concealing vital monitoring and evaluation information."

In June 2013, we initiated an audit to examine the internal controls that USAID and other U.S. government agencies have put in place to safeguard U.S. on-budget funds to the Afghan government. We plan to issue this audit report in early 2014.

⁴⁰ The 2010 memorandum of understanding between USAID and Afghanistan was signed by the Acting Mission Director on behalf of USAID and the Minister of Finance on behalf of the Afghan government.

USAID AND STATE DID NOT FULLY DISCLOSE TO CONGRESS THE RISKS ASSOCIATED WITH PROVIDING DIRECT ASSISTANCE TO THE AFGHAN MINISTRIES

The State Department and USAID complied with the statutory requirements for fiscal years 2011 and 2012 to inform Congress that they (1) have assessed Afghan ministries designated to receive direct assistance and (2) consider the ministries qualified to manage the assistance prior to disbursing any fiscal year 2011 or fiscal year 2012 funds.⁴¹ In the fiscal year 2011 certification, the Deputy Secretary of State certified that nine ministries had been assessed, including the seven ministries with a Stage 2 risk review, specifically stating that “USAID has completed [public financial management risk assessments] of the following [Afghan] ministries and agencies, and with the necessary risk mitigation strategy in place as identified appropriately for each individual ministry or agency, considers each qualified to manage funds provided as direct government-to-government assistance.”⁴² In its fiscal year 2012 notification, USAID informed Congress that all nine previously-certified ministries, as well as the Ministry of Communications and Information Technology, had been assessed.⁴³ The 2012 notification stated that “USAID has completed [public financial management risk assessments] of ten [Afghan] ministries and agencies, and, with the successful implementation of a risk mitigation strategy to address identified vulnerabilities or weaknesses, considers each as having the systems required to manage [U.S. government] funds provided as direct [government-to-government] assistance.”

However, some of the information in the fiscal year 2011 certification by the Secretary of State and USAID’s fiscal year 2012 notification was inaccurate or, at least, incomplete. Specifically, the fiscal year 2011 certification and fiscal year 2012 notification stated that the Ministries of Finance and Higher Education had been assessed, even though USAID was still reviewing the assessment reports and Ernst & Young had not yet finalized them.⁴⁴ The Deputy Secretary of State signed the certification for fiscal year 2011 on September 21, 2012. Ernst & Young did not finalize the Ministry of Finance assessment until January 2013, and the Ministry of Higher Education until March 2013.⁴⁵ In addition, USAID officials told us they have not provided Congress with copies of their internal risk reviews of Afghan ministries’ ability to manage donors’ direct assistance funds.⁴⁶ Figure 4 on the following page shows the date that each ministry assessment was completed and certified, the overall finding of the assessment, and when the congressional notifications occurred.

Further, the memorandum of justification accompanying the fiscal year 2011 certification stated that, “with the necessary risk mitigation strategy in place as identified appropriately for each individual ministry or agency,” USAID considered each of the nine assessed Afghan ministries “qualified to manage funds provided as direct government-to-government assistance.”⁴⁷ The 2012 notification to Congress stated that “with the successful implementation of a risk mitigation strategy to address identified vulnerabilities or weaknesses, USAID

⁴¹ Pub. L. No. 112-10, § 2121(b), 125 Stat. 38, 184 (2011); Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

⁴² Memorandum of Justification for Certification Related to Funds Provided as Government-to-Government Assistance to Afghanistan Under the Full-Year Continuing Appropriations, 2011 (Div. B., P.L. 112-110).

⁴³ The Secretary of State and USAID did not include all of the 16 ministries that were assessed between 2011 and 2013 in the congressional certification and notification; however, USAID did include the seven ministries with a Stage 2 risk review in its fiscal year 2012 notification.

⁴⁴ In the past, USAID sent drafts back to the contractors to add clarifying information, make charts more readable, correct grammatical or typing errors, and question any noted inconsistencies.

⁴⁵ In its comments on a draft of this report, USAID stated that it is reviewing the circumstances surrounding the receipt and completion of these assessments.

⁴⁶ In commenting on a draft of this report, USAID stated Congress has not requested access to these internal risk reviews, but USAID is “prepared and ready to appropriately respond to any requests from Congress for additional information” on its Afghanistan direct assistance program.

⁴⁷ Memorandum of Justification for Certification Related to Funds Provided as Government-to-Government Assistance to Afghanistan Under the Full-Year Continuing Appropriations, 2011 (Div. B., P.L. 112-110).

considers each [assessed Afghan ministry] as having the systems required to manage USG funds provided as direct [government-to-government] assistance.”⁴⁸

These statements are concerning because the 2011 certification and the 2012 notification to Congress did not disclose the full extent of the risks identified at each of the ministries or that over 90 percent of the mitigating measures identified in the risk reviews had not been implemented. For instance, while USAID informed Congress that the Ministry of Finance was considered qualified “with the necessary risk mitigation strategy in place,” USAID did not fully disclose in the 2012 notification that it had identified 46 risks within the ministry, including risks such as “the performance outcome will be lower than expected standards or long term goals will not be achieved,” there is a “lack of accountability of public officials,” and there is a “risk of unauthorized/inappropriate practices and undetection [sic] of differences between the amount of cash recorded and actual amount of cash held.” USAID’s notification also did not disclose that the majority of measures intended to mitigate these risks had not been implemented at the time of the notification, even though the 2012 limitation on direct assistance states that funds may be made available for direct assistance to an Afghan government ministry only if “*any* identified vulnerabilities or weaknesses of such agency or ministry *have been addressed*.”⁴⁹ The decision to continue with direct assistance seemingly conflicts with the 2012 congressional requirement, which, as previously stated, mandates that funds be made available “only if...no level of acceptable fraud is assumed.”⁵⁰

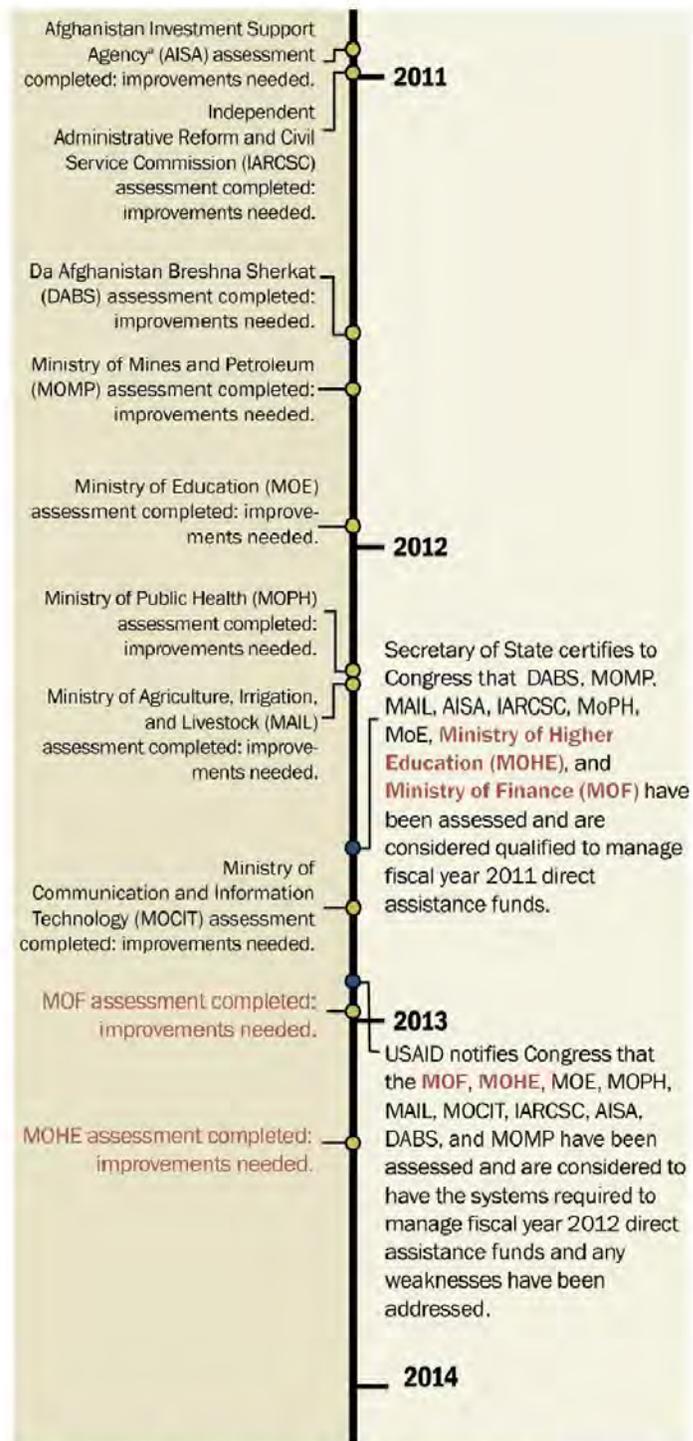
USAID maintains that if the identified risks *could* be mitigated, then the agency considers the ministries qualified to manage U.S. direct assistance funds. However, as discussed, our analysis shows that the risk reviews and public financial management assessment identified numerous weaknesses and risks within the assessed ministries, and USAID has not developed plans to fully mitigate the risks it identified or to implement those plans. Without full information on the ministries’ capabilities and the risk associated with providing direct assistance to these ministries, Congress’s oversight of the over \$600 million in U.S. funds that USAID has obligated to date is compromised.

⁴⁸ USAID Congressional Notification Afghanistan (FY 2012 Country Narrative).

⁴⁹ Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011) (emphasis added).

⁵⁰ Notably, the AUPCSs state that direct assistance activities “are expected to show positive development outcomes, *even if a manageable risk of loss exists and risk mitigation is sub-optimal*” (emphasis added). It is difficult to understand how this conclusion is consistent with a determination that no level of acceptable fraud is assumed.

Figure 4 - Timeline of Certified Ministry Assessments and Congressional Contact



*AISA was included in these communications with Congress, but we did not include it in the scope of our audit because its assessment was conducted in 2010.

Source: SIGAR Analysis of USAID direct assistance contracts, agreements, assessments, and risk reviews.

CONCLUSION

Since 2010, USAID has taken steps to enhance its safeguards over direct assistance funds for the Afghan government. USAID/Afghanistan's efforts have detailed significant financial management risks and identified appropriate risk mitigation measures for each Afghan government ministry that has been reviewed by USAID/Afghanistan. However, a number of troubling issues remain. USAID's decision to waive its primary internal requirement for providing direct assistance exempted its mission in Afghanistan, the only mission in the world to receive a waiver to date, from reviews that would have provided additional assurances that direct assistance funds would be used properly. While we agree that there is likely little benefit at this time from the Stage 1 macro-level review that ADS 220 requires, exempting the mission from the remaining parts of the requirement exposes U.S. funds to a seemingly unnecessary level of risk. Moreover, identifying financial management risks and developing mitigation measures is of little use if minimal action is taken to implement them. USAID's reluctance to make direct assistance to ministries contingent upon them fixing many of the underlying problems identified through the risk reviews does little to support the development of an Afghan government capable of functioning independently and sustaining the programs it manages. Moreover, allowing weaknesses within the ministries to persist raises the likelihood that, should one of USAID's external measures or safeguards be exploited or circumvented, U.S. government funds provided to the Afghan government will be wasted or stolen. For example, providing direct assistance funds on a reimbursement basis will not help protect those funds if the invoices and other documentation submitted by the ministry to obtain the funds were falsified in any way.

Perhaps most troubling is the nature of USAID's official communications with Congress regarding the Afghanistan direct assistance program. Not only did USAID fail to fully disclose to Congress that none of the ministries it assessed was capable of managing direct assistance funds, it also did not reveal that it only included a small number of risk mitigation measures identified through its risk reviews as conditions that Afghan ministries must meet prior to receiving funds. We believe it was and is incumbent upon USAID to share this information with Congress.

Giving the Afghan government the ultimate responsibility to allocate, manage, and track funds through the increased use of direct assistance is an important step in the reconstruction of Afghanistan, because it will largely be up to the Afghan government to sustain the reconstruction effort in the long run. Nevertheless, the pervasiveness of corruption in Afghanistan makes it critical that the U.S. government use every safeguard at its disposal to ensure that the over \$1 billion in open-ended commitments that USAID intends to provide to Afghanistan in direct assistance is not subject to identified vulnerabilities and weaknesses in the ministries.

RECOMMENDATIONS

To ensure more robust quality control of the process for assessing ministries and implementing risk mitigation measures prior to providing direct assistance funds to the Afghan government, we recommend that the Administrator for USAID:

- 1. Require compliance with all parts of ADS 220—except for the Stage 1 macro-level review—for the use of all direct assistance funds for fiscal year 2014 and beyond.**

To improve accountability and oversight of direct assistance to the Afghan government, we recommend that the Mission Director for USAID/Afghanistan:

- 2. Fully inform Congress of the status of ministry assessments USAID or its contractors have completed, the risk mitigation measures Afghan ministries have implemented, and the level of risk to U.S. funds.**
- 3. Develop a plan, similar to the one created for Da Afghanistan Breshna Shekat, for each Afghan ministry that has a completed USAID risk review that defines how each of the risks identified are being**

or will be mitigated, and suspend direct assistance disbursements to these ministries until these plans are completed.

AGENCY COMMENTS

In commenting on a draft of this report, USAID agreed with our three recommendations, but stated it is already complying with recommendations and requested that we consider them closed. We disagree with the agency's assertion that it has fully complied the recommendations, and we will continue to monitor USAID's efforts to determine whether the agency has implemented the recommendations.

Regarding our first recommendation, USAID agreed and stated that it already complies with all Stage 2 requirements of ADS 220. However, as we note in our report, USAID headquarters officials from the Global Partner Country Systems Risk Management Team told us they did not perform quality control reviews of the contracted public financial management assessments, USAID/Afghanistan's risk reviews, or any risk mitigation strategies, as required by ADS 220. To date, USAID has not provided evidence that these quality control reviews have occurred.

With regard to our second recommendation, USAID wrote that it is regularly updating Congress and providing "extensive" documentation on direct assistance in Afghanistan. However, as discussed in our report, the 2011 certification and the 2012 notification to Congress did not disclose the full extent of the risks identified at each of the ministries or that over 90 percent of the mitigating measures identified in the risk reviews had not been implemented. Moreover, USAID officials told us the agency has not provided Congress copies of or access to its crucial Stage 2 risk reviews.

Finally, USAID agreed with our third recommendation to develop a plan, similar to the one created for Da Afghanistan Breshna Shekat, that defines how each of the risks identified are being or will be mitigated. In its comments, USAID asserted that this information is already included in the narrative risk review reports for the six remaining ministries, even though it is not in the matrix format like the one for Da Afghanistan Breshna Shekat. We disagree that the information in the risk mitigation matrix is included in the narrative reports. The narrative reports USAID/Afghanistan provided us do not explicitly state what actions USAID is currently taking, or will be taking in the near future, to mitigate each of the identified risks. Elsewhere in its comments, USAID stated it has prepared risk mitigation plans for the other six ministries to which it provides direct assistance. It is unclear whether the agency is referring to the narrative risk review reports we obtained during our audit or to new risk mitigation matrices. We request that USAID provide the risk mitigation plans for the other six ministries that it believes satisfy our recommendation. Based on our review of that documentation, we will determine if recommendation 3 can be closed.

In its comments, USAID also disagreed with some of our findings and conclusions and suggested that our report did not demonstrate an accurate understanding of its direct assistance program in Afghanistan. For example, USAID wrote that "the audit report focuses on conditions precedent as if they are the only available risk mitigation measure, incorrectly assuming that vulnerabilities can only be addressed in advance by using a single corresponding condition precedent at the program level for each condition or weakness." We appreciate and acknowledge that USAID has additional methods for addressing vulnerabilities. For example, as we explain in our report, USAID uses what are called "ongoing conditions" to address problems within the ministries after the initial disbursement of funds and prior to subsequent disbursements. We also note in our report that USAID uses other methods, such as establishing separate bank accounts for specific programs, to safeguard funds from waste, fraud, and abuse.

However, with the exception of conditions precedent and "ongoing conditions," these additional methods do not directly address the underlying problems within the ministries that limit their ability to manage donor funds. As stated earlier in our report, external measures do little to build ministries' organic capabilities to manage donor funds—one of the primary purposes of providing on-budget assistance to the Afghan government. Moreover, these external measures could well be exploited or circumvented by ongoing problems within the

ministries, including “cronyism and nepotism,” the “likelihood for kickbacks and collusion,” and an “unwillingness or inability to enforce the most ordinary ethical conducts.”

Finally, in its comments, USAID expressed concern that our report includes information designated by it and the Department of State as “Sensitive but Unclassified (SBU).” Specifically, USAID has designated the ministry assessments and the internal risk reviews as SBU and requested SIGAR to withhold this information and unspecified, but related portions of our audit report from public release because “release of these materials will likely result in reduced cooperation from the Afghan Government” and release “could damage our bilateral relationships with the Government of the Islamic Republic of Afghanistan.”

USAID asserts that the ministry assessments and internal risk reviews “were generated for the internal use of the US Government and the entities that are the subject of the assessments” (*i.e.*, the Afghan ministries). USAID also asserts that “parts of the Afghan government provided unprecedented access for the independent auditors to complete the risk assessments based on understandings that the results of the risk assessments would not be made public.”

Despite repeated requests from SIGAR, USAID has not provided any documentary evidence that it promised the Afghan government that this information would be withheld from the public. In any case, the fact that USAID specifically decided to designate the ministry assessments and the risk reviews as “unclassified” means that this information cannot be withheld from public release on the basis of that rationale.

The State Department’s Foreign Affairs Manual addresses this issue very clearly:

“Information obtained from or exchanged with a foreign government or international organization as to which public release would violate conditions of confidentiality or otherwise harm foreign relations *must be classified in order to be exempt from release under FOIA or other access laws. The SBU label cannot be used instead of classification to protect such information.*”⁵¹

Notwithstanding the Foreign Affairs Manual, USAID’s comments define SBU as a designation for “information that warrants a degree of protection and administrative control and meets *legal or regulatory criteria for exemption from public disclosure*” (emphasis added). However, USAID has not articulated any basis in law or regulation that would require SIGAR to censor all or part of this report.

USAID’s mention of “legal or regulatory criteria for exemption from public disclosure” appears to be an oblique reference to the discretionary exemptions under the Freedom of Information Act, 5 U.S.C. § 552, (FOIA) that permit an agency to withhold certain information under narrowly defined circumstances. However, USAID has not explained how any part of SIGAR’s audit report might fall within any of those discretionary exemptions or explained why those exemptions should be asserted.

Moreover, there is a strong presumption in law and policy in favor of public disclosure. The main purpose of FOIA is to ensure public disclosure, not to prevent it. In addition, the SBU designation is a subcategory of “Controlled Unclassified Information” (CUI).⁵² Executive Order No. 13,556 established “an open and uniform program” for managing CUI.⁵³ In describing the reasons for establishing this program, the order states that:

“[E]xecutive departments and agencies . . . employ ad hoc, agency-specific policies, procedures, and markings to safeguard and control this information This inefficient, confusing patchwork has resulted in inconsistent marking and safeguarding of documents, led to unclear or *unnecessarily restrictive* dissemination policies, and created impediments to authorized information sharing. *The*

⁵¹ 12 FAM 543(f) (emphasis added). This provision applies to both USAID and the State Department. See 12 FAM 511.1(a).

⁵² Presidential Memorandum for Heads of Executive Departments and Agencies Concerning Classified Information and Controlled Unclassified Information, 74 Fed. Reg. 26,277 (May 27, 2009).

⁵³ Exec. Order No. 13,556, 75 Fed. Reg. 68,675 (November 9, 2010).

fact that these agency-specific policies are often hidden from public view has only aggravated these issues.”⁵⁴

The Department of Justice and the National Archives and Records Administration have issued joint guidance implementing Executive Order No. 13,556, which states that “FOIA should not be cited as a safeguarding or dissemination control authority for [CUI].”⁵⁵ This is because “[t]he purpose of the FOIA is to open agency activities to the public.”⁵⁶ Similarly, the President has stated that departments and agencies should not “keep information confidential merely because public officials might be embarrassed by disclosure, because errors and failures might be revealed, or because of speculative or abstract fears.”⁵⁷

Therefore, in the absence of any basis in law or regulation articulated by USAID for withholding this information from public scrutiny, SIGAR will publish this audit report in full.

USAID’s comments on our report, and our detailed response to them, are included in Appendix XVI. USAID also provided technical comments on our draft report, which we incorporated, as appropriate.

⁵⁴ *Id.* (emphasis added).

⁵⁵ Memorandum from John P. Fitzpatrick, Director, Controlled Unclassified Information Office, National Archives and Records Administration, and Melanie Ann Pustay, Director, Office of Information Policy, U.S. Department of Justice, to Senior Agency Officials for Executive Order No. 13556, “Controlled Unclassified Information” (November 22, 2011).

⁵⁶ *Id.*

⁵⁷ Presidential Memorandum for Heads of Executive Departments and Agencies Concerning the Freedom of Information Act, 74 Fed. Reg. 4,683 (Jan. 21, 2009).

APPENDIX I - SCOPE AND METHODOLOGY

This review examined the U.S. Agency for International Development's (USAID) process for conducting and using ministerial assessments when awarding direct bilateral assistance to the Afghan government. We focused specifically on Ernst & Young's and KPMG's public financial management assessments of 16 ministries completed from January 2011 to August 2013 under contracts with USAID, and USAID's mission for Afghanistan's (USAID/Afghanistan) internal risk reviews of seven of those ministries. The objectives of this audit were to (1) assess the extent to which Ernst & Young and KPMG adhered to USAID contract requirements when conducting the ministry assessments, (2) describe the assessment findings and their conclusions about the ability of the Afghan ministries to manage U.S. direct assistance funds and analyze how USAID has used, or plans to use, the assessments to help inform its assistance to the Afghan government, and (3) examine the Department of State's fiscal year 2010 and fiscal year 2011 certifications and USAID's FY 2012 notification to Congress, pursuant to statute. We did not examine the implementation of USAID-funded direct assistance programs, assess the effectiveness of USAID's methods for safeguarding U.S. direct assistance funds, or determine whether fraud and misuse of funds existed within these programs.

To assess the extent to which Ernst & Young and KPMG adhered to USAID contract requirements when conducting the ministry assessments, we analyzed all contracts and final reports for the 16 ministries the contractors assessed:

1. Afghanistan Independent Human Rights Commission (AIHRC)
2. Da Afghanistan Breshna Sherkat (DABS)
3. Independent Administrative Reform and Civil Service Commission (IARCSC)
4. Ministry of Agriculture, Irrigation, and Livestock (MAIL)
5. Ministry of Communication and Information Technology (MOCIT)
6. Ministry of Education (MOE)
7. Ministry of Energy and Water (MEW)
8. Ministry of Economy (MOEC)
9. Ministry of Finance (MOF)
10. Ministry of Higher Education (MOHE)
11. Ministry of Information and Culture (MOIC)
12. Ministry of Mines and Petroleum (MOMP)
13. Ministry of Public Health (MOPH)
14. Ministry of Public Works (MOPW)
15. Ministry of Rural Rehabilitation and Development (MRRD)
16. Ministry of Transport and Civil Aviation (MOTCA)

We reviewed completed public financial management risk assessment framework checklists, risk assessment checklists, and control environment checklists. We reviewed the contractors' working papers, including draft reports, internal control testing documentation, and correspondence with the ministries and USAID. We reviewed USAID's contractor performance assessment reports for Ernst & Young and KPMG, as well as correspondence between the agency and the contractors. We also reviewed the USAID Office of Inspector General's November 2010 report on pre-award ministerial assessments for direct assistance in Afghanistan, and compared the associated recommendations with actions USAID had taken since the issuance of that report.⁵⁸ We reviewed prior SIGAR work on DABS⁵⁹ and USAID's direct assistance to MOPH.⁶⁰ We obtained answers to various questions on contract monitoring from USAID/Afghanistan. In addition, we interviewed officials with USAID/Afghanistan's Office of Financial Management, Ernst & Young, and KPMG.

⁵⁸ USAID Office of Inspector General, *Review of USAID/Afghanistan's Ministerial Assessment Process*, F-306-11-001-S, November 6, 2010.

⁵⁹ SIGAR Audit 13-7, *Afghanistan's National Power Utility: Commercialization Efforts Challenged by Expiring Subsidy and Poor USFOR-A and USAID Project Management*, April 18, 2013, and SIGAR 14-7-AL on Kajaki Dam Direct Assistance Oversight Provisions, December 31, 2013.

⁶⁰ SIGAR Audit 13-17, *Health Services in Afghanistan: USAID Continues Providing Millions of Dollars to the Ministry of Public Health despite the Risk of Misuse of Funds*, September 5, 2013.

To identify the assessment findings and their conclusions about the ability of the Afghan ministries to manage U.S. funds, we analyzed Ernst & Young's and KPMG's public financial management assessment reports for the 16 identified ministries. We also analyzed USAID/Afghanistan's risk reviews for DABS, MAIL, MOCIT, MOE, MOF, MOMP, and MOPH. We transposed data from the 16 assessments and seven risk reviews to create Excel databases of all the recommendations and risk mitigation measures. We then classified each recommendation and measure into one of ten themes:

1. Strategic planning
2. Procurement
3. Lack of legal advisors
4. Staffing
5. Auditing, evaluation, and monitoring
6. Information technology
7. Transparency
8. Asset and cash management
9. Financial records and revenue
10. Budgeting

When we identified a recommendation for monitoring within one of the themes, we classified the recommendation under the auditing, evaluation, and monitoring theme. We used this information to compare themes across the 16 contracted public financial management assessments and the seven USAID risk reviews. We analyzed recommendations, rather than key findings, because recommendations present both problems and methods for addressing these problems with a greater level of detail about each issue, allowing more accuracy when identifying common themes. In addition, we attempted to interview officials from each ministry for which USAID/Afghanistan had completed a risk review. We interviewed officials with DABS, MAIL, MOF, and MOMP; the security environment during our fieldwork in Kabul, Afghanistan prevented us from conducting interviews with officials from MOPH, MOCIT, and MOE. We also interviewed officials from USAID/Afghanistan's Office of Financial Management.

To analyze how USAID has used, or plans to use, the ministerial assessments in the context of providing direct assistance to the Afghan government, we analyzed implementation letters between USAID/Afghanistan and DABS, IARCSC, MAIL, MOCIT, MOE, MOF, MOMP, and MOPH for all eight active direct assistance programs. We created an Excel spreadsheet of the conditions precedent and ongoing conditions from these letters for our analysis. Using this data and the risk mitigation measures we transposed from the seven USAID/Afghanistan risk reviews, we compared conditions precedent to the mitigation measures contained in the risk reviews to determine whether USAID included the pre-disbursement mitigation measures in conditions precedent, ongoing conditions, or not at all. One condition precedent or ongoing condition could incorporate multiple mitigation measures. In some cases it was unclear if the mitigation measure was to be carried out by the condition precedent due to the vague wording of the condition precedent. We also examined monitoring and evaluation plans for MAIL, MOCIT, MOE, MOF, and MOPH. We obtained answers to questions about monitoring and evaluation plans, the risk assessment frameworks, and conditions precedent from USAID. We also reviewed the Strategic Objective Grant agreements between the U.S. and Afghan governments. We reviewed the December 21, 2010, memorandum of understanding in support of goals, objectives, and mechanisms for effective assistance to Afghanistan between USAID/Afghanistan and the Ministry of Finance, on behalf of the Afghan government. We analyzed data from USAID on the current status of its direct assistance in Afghanistan. We reviewed USAID's *Automated Directives System (ADS) 220: Use of Reliable Partner Country Systems for Direct Management and Implementation of Assistance*,⁶¹ *ADS 301 Responsibility for Procurement*, *ADS 305 Host Country Contracts*, and the agency's November 2012 waiver of ADS 220, as well as USAID/Afghanistan's *Mission Order 220.02: Implementation of Programs Using On-Budget Assistance*.⁶² We reviewed the U.S. Government Accountability Office's July 2011 report on USAID's assistance in Afghanistan.⁶³ In addition, we analyzed USAID/Afghanistan's risk reviews and Approval of Use of Partner Country Systems for DABS, MAIL, MOCIT, MOE, MOF, MOMP, and MOPH. We also reviewed memoranda of USAID's reviews of conditions precedent for IARCSC, MAIL, MOE, and MOMP. In addition, we interviewed USAID headquarters officials from the Office of Afghanistan and Pakistan Affairs and the Chief Financial Officer's Global Partner Country Systems Risk Assessment Team. We also interviewed USAID/Afghanistan officials from the Office

⁶¹ USAID established ADS 220 in August 2011 and updated it in March 2012.

⁶² Mission Order 220.02 was approved November 19, 2012.

⁶³ U.S. Government Accountability Office, *Actions Needed to Improve Accountability of U.S. Assistance to Afghanistan Government*, GAO-11-710, July 20, 2011.

of Financial Management and Office of Program and Project Development. We also met with USAID officials designated as on-budget monitors for active programs at DABS, IARCSC, MAIL, MOE, MOF, and MOPH.

To examine the Department of State's certifications and USAID's notification to Congress, pursuant to annual appropriations acts, we reviewed the fiscal year 2010 Consolidated Appropriations Act, the fiscal year 2011 Department of Defense and Full-Year Continuing Appropriations Act, and the fiscal year 2012 Consolidated Appropriations Act.⁶⁴ We reviewed the Secretary of State certifications and memorandums of justification for fiscal years 2010 and 2011 for providing Economic Support Funds and Global Health and Child Survival Funds directly to the Afghan government. We reviewed USAID's November 2012 notification to Congress of the agency's intent to obligate fiscal year 2012 Economic Support Funds and Global Health Programs Funds for direct assistance to the Afghan government. We compared the dates and findings of Ernst & Young and KPMG's public financial management assessments and USAID/Afghanistan's internal risk reviews to what the Secretary of State and USAID provided Congress in their 2011 certification and 2012 notification, respectively. We also sent inquires about what assessments USAID provided to the House of Representatives Committee on Oversight and Government Reform's majority staff. In addition, we interviewed USAID headquarters officials from the Office of Afghanistan and Pakistan Affairs.

We did not use or rely on computer-processed data for the purposes of the audit objectives. With respect to internal controls, we reviewed ADS 220 to determine the extent to which the agency complied with its own policy directives and required procedures for direct assistance. We also reviewed Ernst & Young's and KPMG's compliance with the terms of their contracts with USAID to conduct the public financial management assessments, as well as USAID's compliance with congressional requirements for direct assistance. The results of our assessment are included in the body of this report.

We conducted work in Washington, D.C. and Kabul, Afghanistan, from April 2013 to January 2014, in accordance with generally accepted government auditing standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The audit was conducted by the Office of Special Inspector General for Afghanistan Reconstruction under the authority of Public Law No. 110-181, as amended, and the Inspector General Act of 1978, as amended.

⁶⁴ Consolidated Appropriations Act, 2010, Pub. L. No. 111-117, 123 Stat. 3034, 3329 (2009), Department of Defense and Full-Year Continuing Appropriations Act, 2011, Pub. L. No. 112-10, § 2121(b), 125 Stat. 38, 184 (2011); Consolidated Appropriations Act, 2012, Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

APPENDIX II - ADDITIONAL INFORMATION ON USAID'S DIRECT ASSISTANCE FUNDING, REQUIREMENTS, AND MINISTRY ASSESSMENTS

On-budget assistance became an international focus in the early 2000s, when countries from the Organization for Economic Co-operation and Development, including the United States, and the organization's Development Co-operation Directorate met with developing nations to discuss ways to increase the effectiveness of foreign aid. These meetings culminated in the Paris Declaration on Aid Effectiveness, signed in March 2005, whereby countries pledged to make changes in the way they give and receive foreign assistance.⁶⁵ The Paris Declaration emphasizes on-budget assistance and states that successful development depends largely on a host government's capacity to implement policies and manage public resources through its own institutions and systems.⁶⁶ At the Paris conference, donors agreed to use host country systems as the preferred option for their aid programs.

At the 2010 London Conference, the United States and other members of the international community stated their commitment to providing 50 percent of development aid to Afghanistan through on-budget assistance and reaffirmed this commitment at the 2010 Kabul and 2012 Tokyo Conferences. The U.S. Agency for International Development's (USAID) Performance Management Plan and its 2013 progress report, *USAID Forward*, both reiterate the U.S. government's intent to provide more than 50 percent of its assistance through Afghan government systems.

In line with these commitments, a major component of the U.S. government's approach to reconstruction in Afghanistan involves supporting the Afghan government, as appropriate, so it can take increasing ownership for development and sustain the gains made over the past decade. On-budget assistance to the Afghan government can encompass several types of funding mechanisms, including donations to multi-donor trust funds, direct budget support, and direct assistance. USAID officials stated that the agency does not award direct budget support, which it defines as "funds provided directly to a foreign government to be used by that government at its discretion and without further U.S. oversight." Instead, USAID awards on-budget assistance in Afghanistan exclusively through donations to multi-donor trust funds and direct assistance agreements. Direct assistance is aid that the agency implements through bilateral agreements with an Afghan government entity and under national arrangements covering public financial management systems at both national and ministerial or sectoral levels. Direct assistance includes host country contracting and government-to-government assistance.⁶⁷

When USAID first committed in 2005 to increasing the amount of on-budget assistance it planned to provide the Afghan government, the USAID Mission for Afghanistan (USAID/Afghanistan) used host country contracting, which is one method USAID uses to finance and implement projects.⁶⁸ USAID used host country contracting for direct assistance agreements for only two programs—one with the Ministry of Public Health and one with the Ministry of Communication and Information Technology.

A February 2013 report commissioned by the German Federal Ministry for Economic Cooperation and Development, provided to us by USAID officials, shows that although only 11 percent of 2011, U.S. government development aid was given as on-budget assistance to the Afghan government, USAID's direct assistance

⁶⁵ The governments of the United States and Afghanistan have agreed to adhere to the Paris Declaration.

⁶⁶ *The Paris Declaration on Aid Effectiveness*, Organization for Economic Cooperation and Development (2006). Signatories of the Paris Declaration reaffirmed and strengthened the commitments of that declaration in September 2008 (see *The Accra Agenda for Action*, Organization for Economic Cooperation and Development (2008).

⁶⁷ We do not include funds USAID contributes to the Afghanistan Reconstruction Trust Fund in this review. The World Bank, as the fund's administrator, serves as an intermediary for USAID and other donors by disbursing money from the fund directly to the Afghan government and overseeing its use. We have previously reported on the World Bank's and Afghan government's ability to monitor and account for U.S. and donor funds contributed to the fund (see SIGAR Audit-11-14, *The World Bank and the Afghan Government Have Established Mechanisms to Monitor and Account for Funds Contributed to the Afghanistan Reconstruction Trust Fund, but Some Limitations and Challenges Should Be Addressed*, July 22, 2011).

⁶⁸ USAID Automated Directives System 301 *Procurement Responsibilities* and Automated Directives System 305 *Host Country Contracts*. USAID's host country contracting policies require reviews of all recipient ministries' procurement systems.

obligations have been increasing.⁶⁹ For example, from 2010 to 2011 USAID’s direct assistance obligations increased by 200 percent—from \$144 million to \$434.7 million.⁷⁰ As of August 2013, USAID had obligated almost \$659 million to seven ministries for eight active direct assistance programs, and planned to commit an additional \$237 million to these programs.⁷¹ The agency has committed another \$780.7 million for 10 planned programs, for a total of 18 active and planned direct assistance programs.⁷² Table 1 lists all active USAID direct assistance programs. See appendix IV for a full list of the agency’s completed, active, and planned direct assistance programs.

Table 1 - Active Direct Assistance Programs in Afghanistan, as of August 2013

Ministry	Program	Total Estimated Commitments(millions \$)	Total Obligations (millions \$)	Total Disbursements (millions \$)
Da Afghanistan Breshna Sherkat	Power Transmission Expansion and Connectivity	\$342.0	\$263.3	\$0.0
Ministry of Public Health	Partnership Contracts for Health Services	236.5	190.3	141.3
Ministry of Mines and Petroleum	Sheberghan Gas Development Program	90.0	30.0	0.0
Da Afghanistan Breshna Sherkat	Kajaki Dam	75.0	75.0	0.0
Ministry of Agriculture, Irrigation, and Livestock	Agriculture Development Fund	75.0	29.0	9.0
Ministry of Finance	Civil Service Technical Assistance Program	36.3	36.3	28.8
Ministry of Education	Basic Education and Literacy and Vocational Education and Training, textbook printing	26.7	20.0	11.8
Independent Administrative Reform and Civil Service Commission	USAID Grant Agreement to Support Civil Service Reform	15.0	15.0	10.8
TOTAL		\$896.4	\$658.9	\$201.7

Source: USAID/Afghanistan Office of Program and Project Development data, as of August 1, 2013.

⁶⁹ Ted Dinklo, *Putting Aid on Budget: Final draft*, ECORYS, February 2013. *Putting Aid on Budget* was commissioned by the German Federal Ministry for Economic Cooperation and Development.

⁷⁰ The Department of Defense also provides direct assistance to the Afghan government. We reported in December 2013 on our evaluation of the department’s assessments of the Ministries of Defense and Interior (see SIGAR-14-12-SP, *Comprehensive Risk Assessments of MOD and MOI Financial Management Capacity Could Improve Oversight of Over \$4 Billion In Direct Assistance Funding*, December 3, 2013).

⁷¹ USAID has disbursed an additional \$25.2 million to five completed direct assistance programs and one suspended direct assistance program at five ministries. See appendix III for information on these completed and suspended direct assistance programs.

⁷² According to USAID’s ADS Glossary, an obligation is a legal liability of the government for the payment of funds for specific goods or services ordered or received. It includes a range of transactions, such as contracts, grants, and loans. In contrast, a commitment is an administrative reservation of funds in anticipation of their obligation.

Prior Assessments of Afghan Ministries and Requirements for USAID's Direct Assistance to the Afghan Government

USAID and the government of Afghanistan signed a memorandum of understanding in December 2010 in support of the goals, objectives, and mechanisms for effective assistance to Afghanistan. The memorandum of understanding focused on maximizing opportunities presented by USAID-funded assistance to increase capacity, institutional growth, and public ownership of the development process in Afghanistan. The memorandum also laid out 13 financial requirements to ensure that direct assistance funds are used as intended. For example, the requirements specified that the Afghan government return unspent funds to USAID, grant access rights to USAID for any special bank accounts established for direct assistance programs, and maintain accounting records in accordance with agreed upon standards for 3 years after the last disbursement. Additionally, the memorandum required that the Afghan government work with USAID to both design satisfactory responses to recommendations by USAID for any pre-award assessments and to establish a monitoring and evaluation plan specific to each activity for which direct assistance funds will be used. Furthermore, there are also requirements that USAID reserve the right to suspend or terminate a direct assistance funded activity or obtain a refund should terms of the activity be breached, to carry out third party evaluations of direct assistance activities, and to only release funds when adequate supporting documentation is submitted to USAID.⁷³

At about the same time USAID signed the memorandum of understanding with the Afghan government, USAID's Office of Inspector General conducted an audit of USAID/Afghanistan's assessments of Afghan ministries.⁷⁴ That audit reviewed eight assessments of six ministries that USAID/Afghanistan completed between 2007 and 2010. USAID's Inspector General found weaknesses in USAID/Afghanistan's assessment process, including limited internal control testing and a lack of program-level information in the assessments. The Inspector General also proposed ways to strengthen the assessment process. Specifically, the Inspector General recommended that the mission implement policies, procedures, and practices that would provide assurance that significant vulnerabilities in ministries would be identified during the assessment process.⁷⁵

USAID's Office of Inspector General also recommended that the mission implement 10 changes to the statements of work for the public financial management assessments, including more stringent reporting requirements.⁷⁶ USAID/Afghanistan implemented 8 of the 10 recommended changes for contracts signed since January 2011. Table 2 outlines the USAID Office of Inspector General's recommended changes and indicates whether USAID/Afghanistan implemented each change.

⁷³ This audit did not assess USAID's compliance with all of these requirements. We initiated a separate audit in June 2013 to evaluate the process by which U.S. agencies provide direct assistance funds to the Afghan government and the internal controls put in place to safeguard these funds, to include many of the requirements included in the December 2010 memorandum of understanding.

⁷⁴ See USAID Office of Inspector General, *Review of USAID/Afghanistan's Ministerial Assessment Process*, F-306-11-001-S. November 6, 2010. When the USAID Office of Inspector General issued its report, there was no agency-wide guidance on direct assistance. The Inspector General's report reviewed a variety of USAID's prior assessments of Afghan ministries, including public financial management assessments, direct assistance analyses, and reviews of procurement systems for host country contracts. However, the recommendations focused on USAID/Afghanistan's future ministerial assessments, which, as defined through agency policy, are primarily the public financial management assessments.

⁷⁵ In July 2011, the U.S. Government Accountability Office recommended that USAID establish and implement a policy requiring risk assessments before awarding direct assistance funds to the Afghan government (see U.S. Government Accountability Office, *Actions Needed to Improve Accountability of U.S. Assistance to Afghanistan Government*, GAO-11-710 July 20, 2011.)

⁷⁶ See USAID Office of Inspector General, F-306-11-001-S.

Table 2 - USAID Office of Inspector General Recommended Contract Changes

Contract Change	
Implemented	Provide reviewer a questionnaire to show how review is completed
	Consider the effect of the control environment on control procedures
	Identify applicable laws related to human resources, financial management, and procurement and test for compliance
	Ask reviewers to cross index reports to completed documentation and evidence
	Require testing of internal controls to verify they are effective and consistently adhered to
	Provide draft reports to ministries and other interested parties for comment
	Identify weaknesses in the ministry and provide recommendations to correct them
	Rely and joint assessments and prevent duplication of work where applicable
Not Implemented	Focus contractor reviews on proposed direct assistance programs
	Supervisors should approve testing plans

Source: SIGAR analysis of USAID Office of Inspector General’s 2010 audit report F-306-11-001-S.

In 2011, USAID issued *Automated Directives System (ADS) 220: Use of Reliable Partner Country Systems for Direct Management and Implementation of Assistance* to provide internal policy directives and required procedures for managing and implementing direct assistance.⁷⁷ ADS 220 established the Public Financial Management Risk Assessment Framework—a multi-stage, risk-based methodology that USAID uses to assess partner country systems’ suitability for receiving direct assistance. Stage I of this framework is a macro-level analysis of the risk environment of the partner country that provides a USAID mission with a high-level perspective of the fiduciary risks associated with use of the partner country’s systems. In Stage 1, a USAID mission conducts a macro-level review, and, depending on a country’s “democracy threshold,” a democracy and governance review which “seeks to determine whether a [direct assistance] investment could empower a government at the expense of its people.” The mission determines if there is an unacceptable or unmitigated country-level fiduciary risk, political constraints, or other insurmountable barriers to the use of partner country systems. During this stage, the mission reviews governance structures and helps inform the decision as to whether the mission should continue considering the country for direct assistance.

If, after analyzing the results of the Stage I macro-level review, the USAID mission decides to continue pursuing direct assistance, it then conducts a Stage 2 assessment. This assessment is an in-depth ministry-level review undertaken to gain a detailed understanding of an individual ministry. The Stage 2 assessment concludes with a determination by the USAID mission of whether that ministry is capable of handling U.S. direct assistance funding. If the USAID mission concludes that a ministry is capable of handling direct assistance funding, then the USAID mission grants an “Approval of Use of Partner Country Systems” (AUPCS). An AUPCS constitutes formal approval for the use of a partner country’s public financial management system, but is not an agreement to actually disburse funds.

Once the ministry has been approved to receive direct assistance, the USAID mission then completes the remaining stages of ADS 220’s public financial management risk assessment framework. During Stages 3, 4, and 5, the mission determines an appropriate program design; negotiates and prepares a funding agreement with the partner country; and implements, monitors, and evaluates the direct assistance program. USAID’s guidance also calls for additional protections to be implemented during these stages in order to safeguard funds, such as creating separate bank accounts to which USAID has full access and joint control with the Afghan government and maintaining audit rights and the authority to recover ineligible expenditures.

In addition to USAID’s internal requirements defined in ADS 220, USAID is required to comply with congressional requirements for direct assistance. In fiscal year 2010, Congress required the Secretary of State to certify that the U.S. and Afghan governments have agreed to clear and achievable goals and objectives for the use of direct

⁷⁷ USAID finalized ADS 220 in August 2011 and updated it in March 2012.

assistance, and have established mechanisms to ensure funds are used for their intended purpose.⁷⁸ In fiscal year 2011, Congress added the requirement that the Secretary of State certify that “the relevant implementing [Afghan ministries] have been assessed and considered qualified to manage such funds.”

In fiscal year 2012, Congress further specified that funds may be made available for direct assistance “only if—

- (A) each implementing agency or ministry to receive assistance has been assessed and is considered to have the systems required to manage such assistance and any identified vulnerabilities or weaknesses of such agency or ministry have been assessed; and
 - (i) the recipient agency or ministry employs and utilizes staff with the necessary technical, financial, and management capabilities;
 - (ii) the recipient agency or ministry has adopted competitive procurement policies and systems;
 - (iii) effective monitoring and evaluation systems are in place to ensure that such assistance is used for its intended purposes; and
 - (iv) no level of acceptable fraud is assumed.”⁷⁹

The fiscal year 2012 limitation also conditioned the availability of funds for direct assistance on the Government of the United States and the government of Afghanistan agreeing, in writing: “(i) on clear and achievable objectives for the use of such assistance; and (ii) that such assistance should be made on a cost-reimbursable basis.”⁸⁰

The 2012 limitation omitted the condition in fiscal years 2010 and 2011 that funds would only be available if certification was made by the Secretary of State. Instead, the 2012 limitation required that no funds may be made available for direct assistance “without prior consultation with, and notification to, the Committees on Appropriations.”⁸¹ The notification required under the 2012 limitation must “contain an explanation of how the proposed activity meets the [assessment requirements listed above].”⁸² The limitations placed on the availability of funds for direct assistance in fiscal year 2012 are only applicable to direct assistance “in excess of \$10,000,000 and all funds available for cash transfer, budget support, and cash payments to individuals.”⁸³ Therefore, under the 2012 limitation USAID is required to directly notify the Committees on Appropriations prior to making funds in excess of \$10 million available for direct assistance to Afghanistan.

Table 3 shows the congressional requirements for fiscal years 2010 through 2012.

⁷⁸ Consolidated Appropriations Act, 2010, Pub. L. No. 111-117, 123 Stat. 3034, 3329 (2009).

⁷⁹ Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

⁸⁰ Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

⁸¹ Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

⁸² Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

⁸³ Pub. L. No. 112-74, § 7031(a), 125 Stat. 786, 1209-10 (2011).

Table 3 - Congressional Requirements for the Use of Direct Assistance Funds in Afghanistan

Requirement	FY 2010	FY 2011	FY 2012
U.S. Afghan governments have agreed, in writing, to clear and achievable goals and objectives for the use of funds	●	●	●
Establish mechanisms within each implementing ministry to ensure that direct assistance funds are used for the purposes for which they were intended	●	●	
Secretary of State must certify to Congress that [USAID] has met congressional requirements for using direct assistance funds in Afghanistan	●	●	
Relevant implementing ministries have been assessed and considered qualified to manage funds		●	●
Assistance is made on a cost-reimbursable basis			●
No level of acceptable fraud is assumed			●
Effective monitoring and evaluation systems are in place to ensure that direct assistance is used for intended purposes			●
Recipient ministry has adopted competitive procurement policies and systems			●
Recipient ministry uses staff with the necessary technical, financial, and management capabilities			●
[USAID] must notify Congress it has met all FY2012 congressional requirements for using direct assistance funds in Afghanistan			●

Note: FY = fiscal year.

Source: Pub. L. No. 111-117, 123 Stat. 3034, 3329; Pub. L. No. 112-10 § 2121(b), 125 Stat. 38, 184; Pub. L. No. 112-74 § 7031(a), 125 Stat. 786, 1209-10.

USAID's Ministry Assessments and Risk Review Processes

USAID has relied on different types of assessments and reviews to determine whether Afghan ministries have the ability to receive and manage U.S. direct assistance funds. Table 4 shows a breakdown of the different types of assessments completed for Afghan ministries, including who completed the assessments and their purposes.

Table 4 - Ministry Assessment Descriptions

Completed by	Assessment	Description
USAID	Assessments conducted prior to the 2010 USAID Inspector General Report	<ul style="list-style-type: none"> • Focused on reviews of procurement systems for host country contracts, financial management, and direct assistance analyses. • USAID Inspector General concluded that these assessments were unreliable and recommended improvements. • USAID stopped conducting these assessments in 2010.
Contractors	Public financial management assessments	<ul style="list-style-type: none"> • Began in 2010, after the USAID Inspector General report, and are still ongoing. • Review ministries' ability to manage and administer U.S. funds. • 16 completed as of August 2013, with additional assessments currently being conducted.
USAID	Risk reviews	<ul style="list-style-type: none"> • Informed by the public financial management assessments. • Identify risks within a ministry, suggest risk mitigation measures, and conclude whether USAID can rely on the ministry to manage donor funds.

Source: SIGAR analysis of USAID's public financial management assessments, risk reviews, and other Afghan ministerial assessments.

Following the USAID Office of Inspector General's 2010 finding that USAID's assessments were not sufficient to detect vulnerabilities, USAID/Afghanistan issued contracts for third-party firms to conduct public financial management assessments of Afghan ministries' abilities to manage and administer direct assistance funds. Between January 2011 and August 2013, Ernst & Young and KPMG completed public financial management assessments of 16 Afghan ministries under contracts with USAID/Afghanistan.

Using these assessments, USAID/Afghanistan then conducted internal risk reviews of seven ministries in order to inform its decision of whether to provide direct assistance funds to those ministries. These risk reviews include the mission's conclusions and interpretations of the Ernst & Young and KPMG public financial management assessments. The risk reviews also identify major risks and mitigating strategies deemed necessary for ensuring that the ministries reviewed are able to manage U.S. direct assistance. Table 5 outlines which ministries were assessed and by whom.

Table 5 - Contractor Public Financial Management Assessments and USAID Risk Reviews, as of August 2013

Ministry	Active or Planned Direct Assistance Program(s)	Year Assessment Completed	Contractor	USAID Risk Review	Year Review Completed
Da Afghanistan Breshna Sherkat	Yes	2013	Ernst & Young	Yes	2012
Ministry of Mines and Petroleum	Yes	2011	Ernst & Young	Yes	2012
Ministry of Agriculture, Irrigation and Livestock	Yes	2012	Ernst & Young	Yes	2012
Ministry of Public Health	Yes	2012	Ernst & Young	Yes	2012
Ministry of Education	Yes	2011	Ernst & Young	Yes	2013
Ministry of Finance	Yes	2013	Ernst & Young	Yes	2013
Ministry of Communication and Information Technology	Yes	2012	KPMG	Yes	2013
Independent Administrative Reform and Civil Service Commission	Yes	2011	Ernst & Young	No	N/A
Ministry of Justice	Yes	In Progress	Ernst & Young	No	N/A
Supreme Court	Yes	In Progress	KPMG	No	N/A
Afghanistan Independent Human Rights Commission	No	2011	KPMG	No	N/A
Ministry of Public Works	No	2012	Ernst & Young	No	N/A
Ministry of Information and Culture	No	2013	Ernst & Young	No	N/A
Ministry of Economy	No	2013	Ernst & Young	No	N/A
Ministry of Higher Education	No	2013	Ernst & Young	No	N/A
Ministry of Transport and Civil Aviation	No	2011	KPMG	No	N/A
Ministry of Energy and Water	No	2013	KPMG	No	N/A
Ministry of Rural Rehabilitation and Development	No	2013	KPMG	No	N/A

Note: PricewaterhouseCoopers completed an assessment of the Independent Directorate of Local Governance in January 2011; however, the format of this assessment varied from the others, and we did not include it in our analysis.

Source: SIGAR analysis of USAID public financial management assessments and risk reviews.

APPENDIX III - LIST OF USAID DIRECT ASSISTANCE TO AFGHANISTAN SINCE 2004

The U.S. Agency for International Development (USAID) has obligated \$688 million and disbursed \$227 million in direct assistance funds to Afghan government ministries since 2004. Six programs have been completed or suspended, but the majority of obligated funds stem from on-going programs. USAID currently has eight active programs. Although USAID has obligated most of the estimated commitment for these programs, there is still an outstanding estimated commitment of \$237.6 million in upcoming years. In addition, USAID has 10 planned programs to which it plans to commitment \$780.7 million in upcoming years. Table 6 provides an overview of each direct assistance program, including its status and total estimated commitments, obligations, and disbursements as of August 1, 2013.

Table 6 - USAID Direct Assistance in Afghanistan since 2004, as of August 2013

Ministry	Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursements (millions \$)
Independent Directorate of Local Governance	District Delivery Program	suspended	N/A	4.9	2.3
Ministry of Communication and Information Technology	District Communication Network	completed	N/A	14.2	14.2
Ministry of Transport and Civil Aviation	Regional Airports Rehabilitation Program	completed	N/A	6.0	4.8
Ministry of Finance	Salary Support Program	completed	N/A	1.7	1.7
National Independent Commission for Peace and Reconciliation	Program Tahkim-e-Solh - Peace and Reconciliation Program	completed	N/A	1.3	1.2
Ministry of Communication and Information Technology	District Communication Network, Policy Capacity Initiative	completed	N/A	1.0	1.0
Da Afghanistan Breshna Sherkat	Power Transmission Expansion and Connectivity	active	342.0	263.3	0.0
Ministry of Public Health	Partnership Contracts for Health Services	active	236.5	190.3	141.3
Ministry of Mines and Petroleum	Shebergan Gas Development Program	active	90.0	30.0	0.0
Da Afghanistan Breshna Sherkat	Kajaki Dam	active	75.0	75.0	0.0

Table 6 - USAID Direct Assistance in Afghanistan since 2004, as of August 2013

Ministry	Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursements (millions \$)
Ministry of Agriculture, Irrigation, and Livestock	Agriculture Development Fund	active	75.0	29.0	9.0
Ministry of Finance	Civil Service Technical Assistance Program	active	36.3	36.3	28.8
Ministry of Education	Basic Education and Literacy and Vocational Education and Training, textbook printing	active	26.7	20.0	11.8
Independent Administrative Reform and Civil Service Commission	USAID Grant Agreement to Support Civil Service Reform	active	15.0	15.0	10.8
Ministry of Public Health	Integrated Health Services Systems Strengthening Program	planned	326.8	0.0	0.0
Ministry of Education	Basic Education and Literacy and Vocational Education and Training	planned	158.5	0.0	0.0
Ministry of Agriculture, Irrigation, and Livestock	Irrigation Watershed Management Program	planned	100.0	0.0	0.0
Ministry of Education	Afghanistan Workforce Development Program	planned	47.6	0.0	0.0
Ministry of Mines and Petroleum	Mining Investment and Development for Afghanistan	planned	45.0	0.0	0.0
Ministry of Agriculture, Irrigation, and Livestock	Agriculture Research and Extension Development	planned	40.0	0.0	0.0
Ministry of Justice	Rule of Law Program	planned	25.0	0.0	0.0
Supreme Court	Rule of Law Institutions Strengthening Program	planned	25.0	0.0	0.0
Ministry of Agriculture, Irrigation, and Livestock	Land Reform in Afghanistan	planned	8.9	0.0	0.0

Table 6 - USAID Direct Assistance in Afghanistan since 2004, as of August 2013

Ministry	Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursements (millions \$)
Ministry of Communication and Information Technology	E-Government Resource Center	planned	3.9	0.0	0.0
TOTAL			\$1,677.1	\$688.0	\$226.9

Source: USAID/Afghanistan Office of Program and Project Development data, as of August 1, 2013.

Note: USAID suspended the Independent Directorate of Local Governance's District Delivery Program after the agency had already disbursed \$2.3 million. USAID's Office of Inspector General is currently auditing this program. A USAID official stated that USAID is awaiting audit findings to de-obligate funds. For the purposes of our report, we consider this program complete since the agency is not currently obligating funds.

APPENDIX IV - ERNST & YOUNG AND KPMG CONTRACT REQUIREMENTS

The statements of work for the U.S. Agency for International Development’s (USAID) contracts with Ernst & Young and KPMG to conduct the public financial management assessments required the contractors to comply with between 19 to 27 reporting requirements. USAID signed statements of work with Ernst & Young and KPMG from November 2010 through May 2012, and earlier contracts included fewer requirements. Figure 5 depicts the contract requirements for each ministry assessment. The requirement is green if the contractor met it, yellow if a requirement was not met for a justifiable reason, and red if a requirement was not met without a justifiable reason. A requirement is marked “N/A” if USAID did not require that particular requirement in the statement of work.

Figure 5 - Contract Requirements for Public Financial Management Assessments

	IARCSC	MOTCA	AIHRC	MOPW	MOMP	MOE	MAIL	MOPH	MEW	MOCIT	MOHE	MOIC	MOF	MOEC	MRRD	DABS
Executive summary answering objectives and providing overall conclusion	N/A															
Background section describing USAID activity, period covered, project and program objectives; identifying all entities mentioned in report	N/A															
Objectives and scope of agreed-upon procedures performed in report																
Summary: firm's conclusions on accounting system																
Summary: firm's conclusions on recipient's financial management capacity																
Findings concerning deficiencies, including internal controls (what should be), the cause (why it happened) and effect (what harm was caused by not complying with the criteria), if it can be easily determined																
Corrective or compensating actions for each identified weakness																
Pertinent views regarding each recommendation from responsible entity officials and entity actions taken to implement recommendations, in writing																
Firm's findings and conclusions: accounting system																
Firm's findings and conclusions: entity's financial management capacity																
Overview of entity within the larger Afghan government operations																
Entity organizational chart																
Flow charts of major business processes																
Summary: Afghan government forms with descriptions																
Description or flow chart of budget cycle with dates																
Description of IT systems used by entity																
Actions taken to mitigate previously identified risks																
Description of actions taken by management to address previously identified risks																
Address entity capability to perform Host Country Contracting and Sector Program Assistance in accordance with USAID regulations																
Summary: firm's conclusions on entity procedures for ensuring compliance with agreement terms and applicable laws and regulations																
When entity comments oppose findings, conclusions, or recommendations, firm should modify conclusion or state reasons for rejecting them																
Firm's findings and conclusions: status of prior audit recommendations, with agreement terms and applicable laws and regulations																
Firm's findings and conclusions: entity procedures to ensure compliance with agreement terms and applicable laws and regulations																
Summary: firm's conclusions on status of prior audit recommendations																
Summary: comments from entity management regarding their views on the firm's findings and conclusions																
Summary: firm's conclusions on proposed project costs																
Firm's findings and conclusions: proposed project costs																

Key: Deliverable met. Deliverable partially met or unmet with justification accepted by SIGAR and USAID. Deliverable not met. Deliverable not required.

Source: SIGAR analysis of USAID contracts with Ernst & Young and KPMG.

APPENDIX V - USAID RISK RATING MATRIX

Figure 6 shows how the U.S. Agency for International Development (USAID) assigns risk ratings based on potential impact and probability of occurrence of an identified risk. The impact measures the severity of an adverse event associated with the risk and is measured as negligible, marginal, serious, and catastrophic. Conversely, probability measures the likelihood of the occurrence of the adverse event associated with the risk and is expressed as remote, occasional, probable, and frequent. Combining impact and probability factors categorize risk clusters of critical, high, medium and low categories. Although subjective, it is nonetheless the basis for the USAID’s risk mitigation plan for a particular ministry.

Figure 6 - USAID Risk Rating Matrix

IMPACT	Catastrophic	High	Critical	Critical	Critical
	Serious	High	High	Critical	Critical
	Marginal	Medium	Medium	High	High
	Negligible	Low	Low	Medium	Medium
		Remote	Occasional	Probable	Frequent
		PROBABILITY			

Source: USAID risk reviews.

APPENDIX VI - RISKS AND MITIGATION MEASURES IDENTIFIED IN USAID’S RISK REVIEWS

Table 7 identifies the number of risks and corresponding mitigating measures the U.S. Agency for International Development’s Mission for Afghanistan (USAID/Afghanistan) identified in its internal risk reviews of seven Afghan ministries. These seven ministries all have active or planned direct assistance programs.

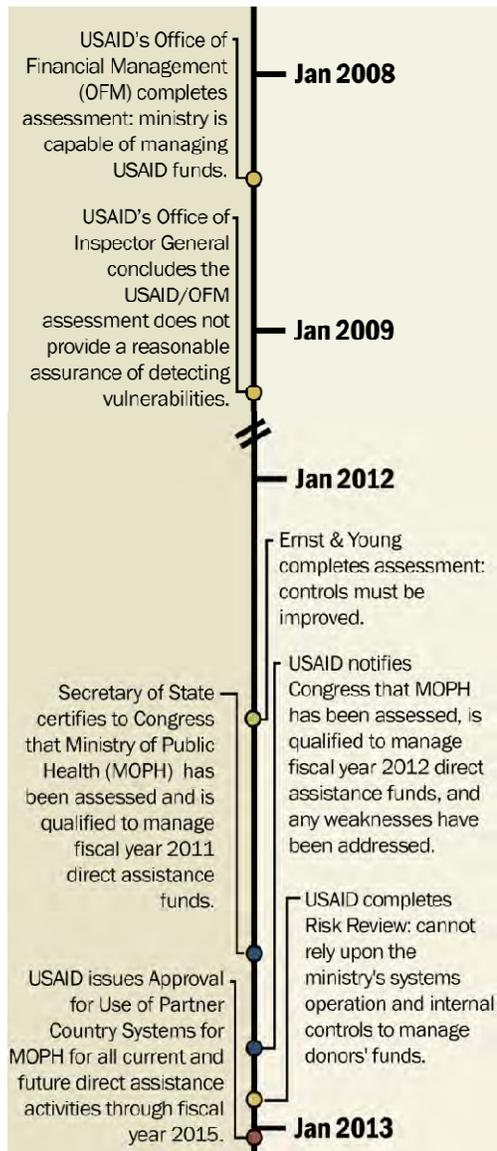
Table 7 - Number of Risks and Mitigation Measures Identified in USAID/Afghanistan’s Risk Reviews

Ministry	Number of Risks	Number of Mitigation Measures
Ministry of Finance	26	46
Ministry of Mines and Petroleum	16	33
Ministry of Public Health	14	55
Ministry of Communications and Information Technology	13	56
Da Afghanistan Breshna Sherkat	12	62
Ministry of Education	12	39
Ministry of Agriculture, Irrigation, and Livestock	11	42
TOTAL	104	333

Source: USAID internal risk reviews.

APPENDIX VII - MINISTRY OF PUBLIC HEALTH OVERVIEW

Figure 7 - Assessment and Certification Timeline of MOPH



Source: SIGAR analysis of USAID public financial management assessments, risk reviews, approval of use of partner country systems, and congressional contact.

The Ministry of Public Health (MOPH) is responsible for the healthcare of all Afghans as guaranteed in the Constitution of Afghanistan. MOPH does not directly implement health services; instead, it oversees the contracting of a Basic Package of Health Services and an Essential Package of Hospital Services through non-governmental organizations. Table 8 provides an overview of the U.S. Agency for International Development's (USAID) direct assistance programs and funding for MOPH, as of August 2013.

Table 8 - USAID's Direct Assistance Programs and Funding for MOPH, as of August 2013

Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursements (millions \$)
Partnership Contracts for Health Services	active	236.5	190.3	141.3
Total Active		236.5	190.3	141.3
Integrated Health Services Systems Strengthening Program	planned	326.8	0.0	0.0
Total Planned		326.8	0.0	0.0

Source: USAID funding data, as of August 1, 2013.

Partnership Contracts for Health Services (Active)

The Partnership Contracts for Health Services are contracts with non-governmental organizations to provide the Basic Package of Health Services and the Essential Package of Hospital Services to the citizens of Afghanistan. The program seeks to improve MOPH's ability to contract these packages out and to assess contractor performance.

Integrated Health Services Systems Strengthening Program (Planned)

The Integrated Health Services Systems Strengthening Program encourages participation in, and attempts to improve access to, the Basic Package of Health Services and the Essential Package of Hospital Services. The Integrated Health Services Systems Strengthening Program intends to strengthen the capacity of MOPH at the provincial level. The program will also enhance MOPH's ability to administer, plan, and procure necessary services.

Summary of Assessment Conclusion and Results

Public Financial Management Assessment (Ernst & Young)

- MOPH should strengthen its Internal Audit Directorate.
- MOPH should enhance its information and communication technology capacity.
- MOPH should improve its controls related to payroll management.
- MOPH should improve its controls related to fixed asset management.
- MOPH should strengthen its procurement management controls.

Ernst & Young's Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

Risk Review (USAID)

- MOPH's financial management and accounting system is not adequate to properly manage and account for donors' funds.
- MOPH's internal controls are not adequate to manage donors' funds.
- MOPH's procurement management units do not have sufficient systems and management capacity to implement activities and manage donors' funds.
- MOPH did not fully comply with Afghan procurement laws and regulations.
- MOPH's internal control environment is not adequate to mitigate the risk of corruption and it is unclear if the ministry has the capacity to combat corruption.
- With only basic controls, such as comparing expenses to allotted budget, the MOPH public financial management system is weak and highly vulnerable to errors and misconduct.
- Due to the pervasive nature of the internal control weaknesses, MOPH is unable to adequately manage and safeguard donor funds against loss or misappropriations.
- Management's lack of consistent commitment to program outcome could impact program results and put donor funds at risk.

USAID's Conclusion: The U.S. government cannot rely on the MOPH's systems operation and internal controls to manage donor funds.

Summary of Conditions Precedent for MOPH Programs

Partnership Contracts for Health program: There are no conditions precedent for this program because this is a host country contract and not subject to *Automated Directives System 220: Use of Reliable Partner Country Systems for Direct Management and Implementation of Assistance*, which requires the use of conditions precedent.

Integrated Health Services Systems Strengthening Program: This is a planned program; no conditions precedent currently exist.

Summary of Suggested Mitigation Measures USAID Identified for MOPH

The following table lists the risks USAID identified in its risk review of MOPH. Due to the Partnership Contracts for Health program being funded as a host country contract there are no conditions precedent to compare the suggested mitigation measures to.

Table 9 - USAID's Stage 2 Suggested Risk Mitigation Measures for MOPH

Risk Mitigation Measures
Develop a policy which requires the Ministry to compare actual results to strategic plan
Prepare management Accounts that compares periodic actual results against budget
Submit quarterly management accounts to USAID which compares actual results against strategic plan
Establish an audit committee with an oversight responsibility over the Internal audit department
Provide relevant training to internal audit personnel
Develop a policy to include disaster recovery plan
Back up information technology systems regularly on the off site
Put information technology (IT) server under locked doors and provide access only to authorized personnel
Install fire extinguishers in the IT server room
Users of the information systems should have unique user ID and password to log into the system
Systems access should be clearly defined or restricted according to roles and functions
Segregate duties among accounting staff
Rotate assignments within the staff to ensure all staff know and understand different levels of responsibility
Instate computerized financial management system with in-built controls
Link the computerized financial management system used by MOPH to the AFMIS maintained by MOF
Submit audited financial statement to USAID
Develop a policy to ensure that all revenues accruing to MOPH have been properly accounted for
Deposit all cash receipts into the bank account without delay
Perform monthly reconciliation on the revenue account
Develop revenue projection and compare projections to actual receipts and investigate the differences
Pay all salaries through the banking system
Reconcile payroll for discrepancies on monthly basis
Modify the payroll system and include the option for reviewing the payroll exception and limit the rights of the users
Tag all fixed assets with an identification number
Update fixed assets register on regular basis to reflect: date of purchase , asset type, location, serial number, tagged number
Provide USAID a list of all fixed assets funded with USAID money
Develop clear organization policies, mission, and vision statements
Distribute copies of the policies to all employees

Develop a plan to automate attendance system

Document time and attendance for all employees

Link employees pay benefits to the time and attendance register and reconcile regularly

Supervisors approval required for all time and attendance before salaries are paid to employees

Conduct compliance audit

Update employees code of conduct and distribute it to all staff

Conduct ethics training for all employees

Develop procedures for conducting exit interviews

Supervisors and employees clear on exit interview clearance forms

Retrieve all assets in the custody of the employees

Develop annual work objectives for all staff

Perform personal needs assessment to determine the areas of improvement

Develop written policies and procedures for the procurement process

Request OAA's involvement in all critical procurements

Obtain signed conflict of interest from personnel who are involved in the procurement processes

Develop a plan to introduce procurement reforms

Develop written policies and procedures for monitoring and evaluation

Convene regular audit committee meetings and document meeting minutes

Audit all USAID projects annually

Submit interim risk based audit reports to USAID

Conduct annual financial statement audit

Submit annual audited financial statement on USAID program funds

Conduct annual payroll audits

Conduct periodic inventory of fixed assets, possibly every six months

Conduct regular performance audit to include asset verification

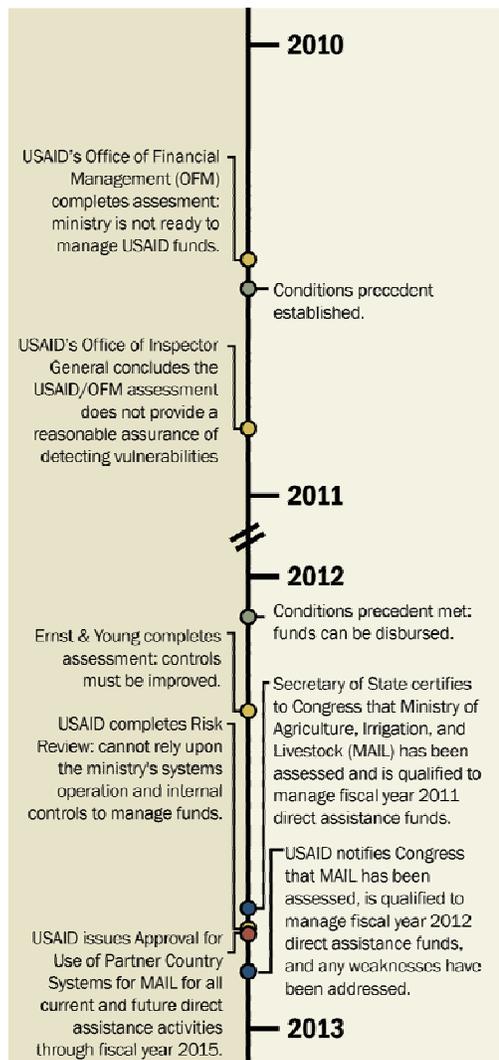
Send monitoring and evaluation reports to the M&E Directorate at the head office and copies to the provincial offices

Submit copies of M&E reports to USAID

Source: SIGAR analysis of USAID risk reviews and implementation letters.

APPENDIX VIII - MINISTRY OF AGRICULTURE, IRRIGATION, AND LIVESTOCK OVERVIEW

Figure 8 - Assessment and Certification Timeline of MAIL



Source: SIGAR analysis of USAID public financial management assessments, risk reviews, approval of use of partner country systems, and congressional contact.

The Ministry of Agriculture, Irrigation, and Livestock's (MAIL) mission is to enhance Afghanistan's agricultural economy. The ministry aims to increase productivity and production, while improving resource management, physical infrastructure, and developing agricultural markets. Table 9 provides an overview of the U.S. Agency for International Development's (USAID) direct assistance programs and funding for MAIL, as of August 2013.

Table 10 - USAID's Direct Assistance Programs and Funding for MAIL, as of August 2013

Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursement (millions \$)
Agriculture Development Fund	active	75.0	29.0	9.0
Total Active		75.0	29.0	9.0
Agriculture Research and Extension Development	planned	40.0	0.0	0.0
Irrigation Watershed Management Program	planned	100.0	0.0	0.0
Land Reform in Afghanistan	planned	8.9	0.0	0.0
Total Planned		148.9	0.0	0.0

Source: USAID funding data, as of August 1, 2013.

Agricultural Development Fund (Active)

The objective of the Agricultural Development Fund is to establish a credit union for Afghan farmers and agri-businesses. USAID provides technical assistance and is one of the only sources of credit to farmers in Afghanistan.

Agricultural Research and Extension Development (Planned)

The Agricultural Research and Extension Development program seeks to support private sector agri-business development. The program focuses on public education and outreach, improved research infrastructure, training for technical staff members, and providing research grants.

Irrigation and Watershed Management Program (Planned)

The Irrigation and Watershed Management Program is designed to improve water governance to reduce conflict. The program also aims to improve irrigation infrastructure to reduce water loss and on-farm water demands.

Land Reform in Afghanistan Program (Planned)

The Land Reform in Afghanistan program intends to formalize land right holdings in Afghanistan by formalizing many informal settlements and their accompanying land rights. The program also looks to provide assistance to the Afghanistan Land Office, the Afghanistan Geodesy and Cartography Head Office, and the Ministry of Urban Development as these offices work to draft, update, and amend laws for land use and management.

Summary of Assessment Conclusions and Results

Public Financial Management Assessment (Ernst & Young)

- MAIL should strengthen its Internal Audit Department.
- MAIL should strengthen its Finance department.
- MAIL should improve its controls related to fixed asset management.
- MAIL should strengthen its program monitoring.

Ernst & Young's Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

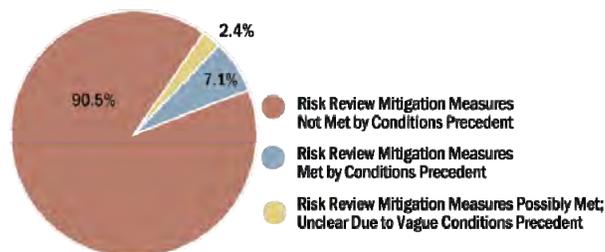
Risk Review (USAID)

- MAIL's financial management/accounting system is not adequate to properly manage and account for donors' funds.
- MAIL does not have the financial management capacity to manage proposed activities.
- MAIL's internal controls are not adequate to manage donors' funds.
- MAIL's procurement management unit does not have sufficient systems and management capacity to implement activities and manage donors' funds.
- MAIL's internal controls environment is not adequate to mitigate the risk of corruption and it is unclear if there is the will to combat corruption.
- The lack of attention to basic employment procedures, and the unwillingness or inability to enforce the most ordinary ethical conducts in the organization expose donors' fund[s] to cronyism and nepotism.

USAID's Conclusion: The U.S. government cannot rely on MAIL's systems operation and internal controls to manage donor funds.

Summary of Conditions Precedent for MAIL Programs

Agricultural Development Fund: Of the 42 mitigating measures that USAID/Afghanistan identified in its risk review of MAIL, the mission only listed one of these measures—the requirement to transfer all assistance funding into an escrow bank account—as a pre-award condition precedent in the fund implementation letter. Three more mitigations may have been implemented, but the conditions precedent are too vague and could allow for the mitigation measure to not be fully implemented.



Agricultural Research and Extension Development: This is a planned program; no conditions precedent currently exist.

Irrigation and Watershed Management Program: This is a planned program; no conditions precedent currently exist.

Land Reform in Afghanistan Program: This is a planned program; no conditions precedent currently exist.

Summary of Suggested Mitigation Measures USAID Identified for MAIL

The following table lists the risks USAID identified in its risk review of MAIL and identifies whether each risk was included in the program implementation letter as a condition precedent, an ongoing condition, or not included in the implementation letter at all.

Table 11 - USAID's Stage 2 Suggested Risk Mitigation Measures for MAIL

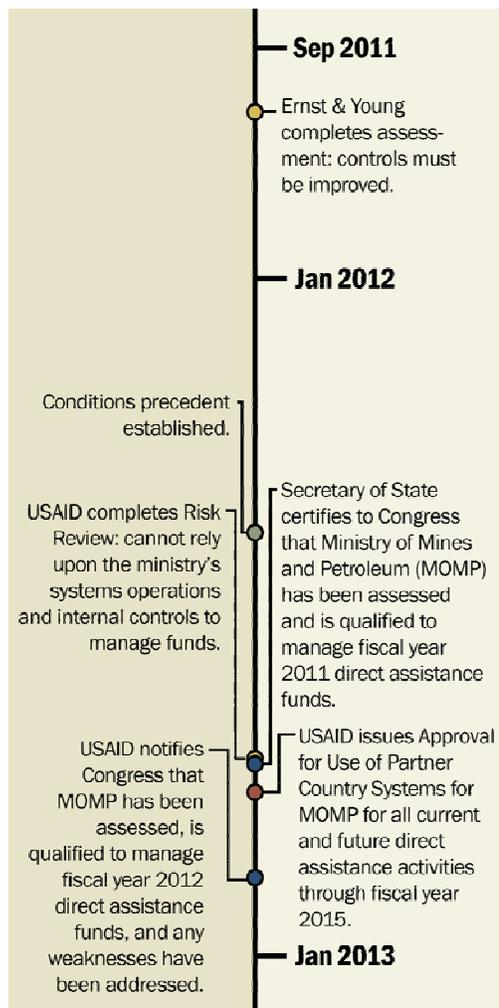
Risk Mitigation Measures	Met	Unclear	Not Met
Develop clear terms of reference for the leadership and evaluation committee for the land leases.			○
Distribute copies of the terms of reference to each member of the leadership and evaluation committee.		○	
Transfer all assistance funding into an escrow bank account	○		
De-emphasize Internal Audit on the payment process.			○
Develop risk base audit approach in the annual audit program			○
Develop a standard audit program and a checklist to serve as a guide for all audit engagements.			○
Submit interim risk based audit reports to USAID			○
Develop a ministry wide information Communication Technology system policy to include disaster recovery plan.			○
Develop unique user ID and password for all users of the information systems			○
Define and restrict systems access to staff according to their roles and functions.			○
Purchase licensed software for the Ministries IT systems			○
Develop a policy for accounting for revenue.			○
Prepare monthly reconciliations on revenue accounts.			○
Prepare monthly receivable aging analysis report			○
Review and approve monthly receivable aging report.			○
tag all fixed assets with an identification number.			○
Update fixed assets register on regular basis to reflect: date of purchase, asset type, location , serial number, tagged number.			○
Develop and document a formal succession plan for staff and projects.			○
Establish a training committee to review and plan staff training needs.			○
Develop training plan for each member of staff			○

Develop a policy for recruitment			<input type="radio"/>
Verify that adequate reference checks have been made on every prospective employee and properly documented			<input type="radio"/>
Conduct annual ethics training for all employees			<input type="radio"/>
Develop annual work objectives for all employees			<input type="radio"/>
Document recruitment disclosure forms for senior management and HR staffs			<input type="radio"/>
Document time and attendance for all employees.			<input type="radio"/>
Link employees pay benefits to the time and attendance register and reconcile regularly			<input type="radio"/>
Conduct compliance audit			<input type="radio"/>
Develop written policies and procedures for the procurement processes			<input type="radio"/>
Request OAA's involvement in all critical procurements.			<input type="radio"/>
Obtain signed conflict of interest from personnel who are involved in the procurement processes			<input type="radio"/>
Develop a plan to introduce procurement reforms.			<input type="radio"/>
Develop written policies and procedures for monitoring and evaluation and disseminate notices to all staff		<input type="radio"/>	
Back-up information technology systems regularly on and off site.			<input type="radio"/>
Audit all USAID projects annually.			<input type="radio"/>
Conduct periodic audits on revenue accounts			<input type="radio"/>
Conduct periodic inventor of fixed assets, possibly every six months.			<input type="radio"/>
Submit regular project reports to USAID		<input type="radio"/>	
Update if applicable, employee security checks periodically			<input type="radio"/>
Update employees code of conduct regularly			<input type="radio"/>
Send monitoring and evaluation reports to the M&E directorate at the head office and copies to the provincial offices			<input type="radio"/>
Submit copies of M&E reports to USAID.	<input type="radio"/>		

Source: SIGAR analysis of USAID risk reviews and implementation letters.

APPENDIX IX - MINISTRY OF MINES AND PETROLEUM OVERVIEW

Figure 9 - Assessment and Certification Timeline of MOMP



Source: SIGAR analysis of USAID public financial management assessments, risk reviews, approval of use of partner country systems, and congressional contact.

The Ministry of Mines and Petroleum (MOMP) promotes the development of market-based mineral and hydrocarbon sectors, and encourages and protects private capital investments into these enterprises, as stated in the Afghanistan Constitution and the Afghan National Development Strategy. Table 10 provides an overview of the U.S. Agency for International Development's (USAID) direct assistance programs and funding for MOMP, as of August 2013.

Table 12 - USAID's Direct Assistance Programs and Funding for MOMP, as of August 2013

Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursement (millions \$)
Sheberghan Gas Development Program	active	90.0	30.0	0.0
Total Active		90.0	30.0	0.0
Mining Investment and Development for Afghanistan	planned	45.0	0.0	0.0
Total Planned		45.0	0.0	0.0

Source: USAID funding data, as of August 1, 2013.

Sheberghan Gas Development Program (Active)

The Sheberghan Gas Development Program seeks to rehabilitate two existing gas wells and drill two additional wells. The program also aims to construct a gas processing plant to allow for the gases extracted to be made suitable for use.

Mining Investment and Development for Afghanistan Program (Planned)

The Mining Investment and Development for Afghanistan program will attempt to reform mining policy and regulation in Afghanistan in order to encourage economic development. This program will also strengthen institutional capacity at MOMP with the overall goal of supporting mining development in the private sector.

Summary of Assessment Conclusions and Results

Public Financial Management Assessment (Ernst & Young)

- MOMP should form an independent monitoring committee.
- MOMP should develop terms of reference for committees involved in the procurement process.
- MOMP should fill key positions that exist in the organization.

Ernst & Young's Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

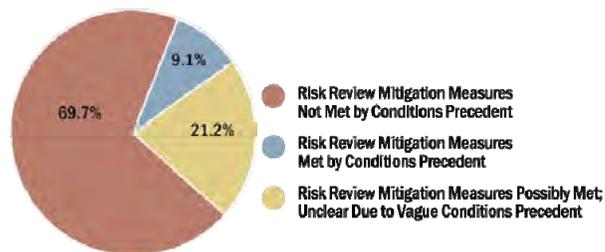
Risk Review (USAID)

- MOMP's financial management/accounting system is not adequate to properly manage and account for donors' funds.
- MOMP does not have the financial management capacity to manage proposed activities.
- MOMP's internal controls are not adequate to manage donors' funds.
- MOMP's procurement management units do not have sufficient systems and management capacity to implement activities and manage donors' funds.
- The internal control environment is not adequate to mitigate the risk of corruption and it is unclear if MOMP has the will to combat corruption.
- Lack of accountability of public officials, financial data susceptible to manipulation, lack of standards to prevent undue preferential treatment such as nepotism and cronyism, and the likelihood for kickbacks and collusion.
- Management attitude has a pervasive affect on the culture and attitude of the entity. This attitude affects the integrity and ethical values of the entity...Accordingly the risks identified at that level will be difficult to mitigate.

USAID's Conclusion: The U.S. government cannot rely on MOMP's systems operation and internal controls to manage donors' funds.

Summary of Conditions Precedent for MOMP Programs

Sheberghan Gas Development Program: USAID/Afghanistan only included 3 of the 33 mitigation measures listed in its risk review as pre-award conditions precedent in the program implementation letter. Seven additional mitigation measures could have been met in the conditions precedent, but the conditions precedent are too vague, and could allow for the mitigation measure to not be fully implemented.



Mining Investment and Development for Afghanistan program:

This is a planned program; no conditions precedent currently exist.

Summary of Suggested Mitigation Measures USAID Identified for MOMP

The following table lists the risks USAID identified in its risk review of MOMP and identifies whether each risk was included in the program implementation letter as a condition precedent, an ongoing condition, or not included in the implementation letter at all.

Table 13 - USAID's Stage 2 Suggested Risk Mitigation Measures for MOMP

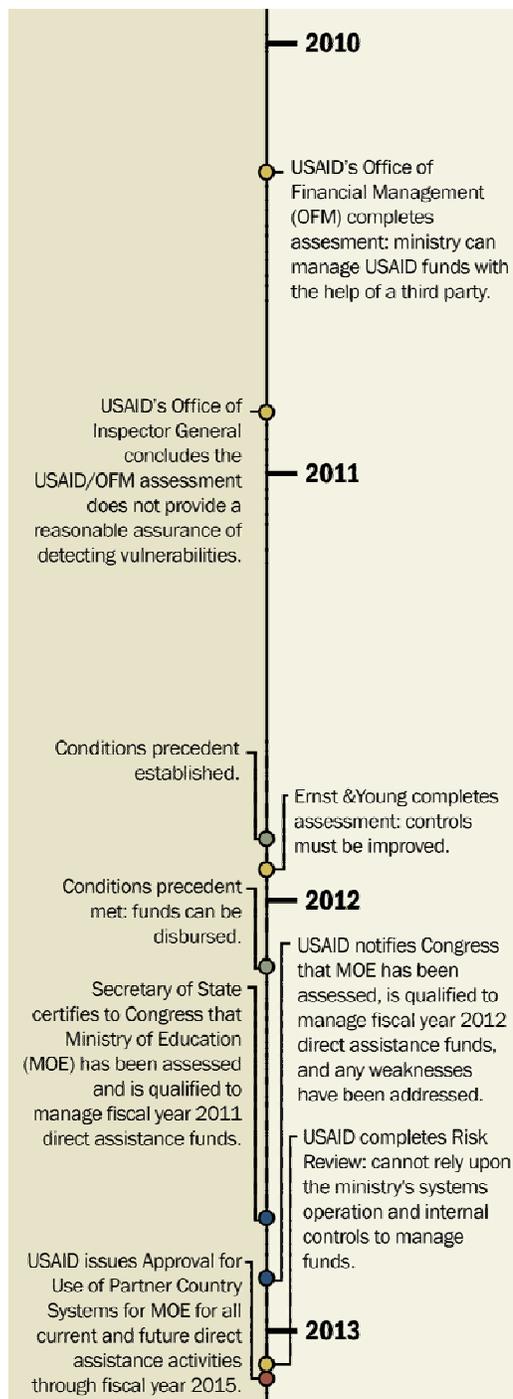
Risk Mitigation Measures	Met	Unclear	Not Met
Transfer all assistance funding in escrow bank accounts	●		
Substantial involvement of USAID's staff in the implementation and/or hiring third party monitor			●
Hold employees accountable to the fullest extent of the law if violated		●	
Conduct audits to prevent fraud, waste and abuse			●
Conduct Ethics trainings as well		●	
Proper segregation of duties amount accounting staff		●	
Rotations of assignments within the staff to ensure all staff know and understand different levels of responsibility			●
Request the installation of computerized financial system with built-in controls	●		
Encourage data storage and validation for all USAID funded activities to ensure accountability and reliability of information		●	
Back up information on a daily basis			●
Evaluating revenue generation systems within the ministry to make sure all revenues are recognized			●
Conduct employee validation surveys of payroll to ensure all employees are properly accounted for			●
Conducting market price analysis/surveys to ensure proper prices are being paid for goods and services		●	
Request OAA's involvement in all critical procurement in all third party monitor decisions			●
Obtain signed conflict of interest forms from senior staff		●	
Conduct fraud awareness trainings and briefings to employees		●	
Maintain accurate asset registers within the ministry		●	
Institute more stringent accountability standards and policies to hold individuals accountable		●	
Set individual benchmarks before any funds are disbursed for goods and services			●
Conduct pre-selection of vendors to ensure acceptable quality standards are maintained		●	
Acquire USAID approval on major procurement of goods and services		●	
Conduct physical inspections of goods at delivery to verify quality			●
USAID audits all projects annually		●	

Conduct periodic surprise investigations of suspicious activities			●
Conduct yearly audits of financial transactions			●
Conduct monitoring and evaluations of all USAID-funded activities	●		
Conduct audits of the on-budget programs annually			●
Conducting regular audits of all assets on the balance sheet			●
Conduct yearly payroll audits			●
Conducting surprise inspections and evaluations of petty cash practices within the ministry for proper accountability		●	
Perform yearly audits			●
Conduct regular audits of cash and property to insure proper accountability			●
Conduct regular audits and physical inspections of all assets		●	

Source: SIGAR analysis of USAID risk reviews and implementation letters.

APPENDIX X - MINISTRY OF EDUCATION OVERVIEW

Figure 10 - Assessment and Certification Timeline of MOE



Source: SIGAR analysis of USAID public financial management assessments, risk reviews, approval of use of partner country systems, and congressional contact.

The Ministry of Education (MOE) is responsible for the provision of primary and secondary education in Afghanistan. The ministry formulates education policy and curriculum, as well as promoting teacher development while continuously monitoring and evaluating education. Table 11 provides an overview of the U.S. Agency for International Development's (USAID) direct assistance programs and funding for MOE, as of August 2013.

Table 14 - USAID's Direct Assistance Programs and Funding for MOE, as of August 2013

Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursement (millions \$)
Basic Education and Literacy and Vocational Education and Training, textbook printing	active	26.7	20.0	11.8
Total Active		26.7	20.0	11.8
Basic Education and Literacy and Vocational Education and Training	planned	158.5	0.0	0.0
Afghanistan Workforce Development Program	planned	47.6	0.0	0.0
Total Planned		206.1	0.0	0.0

Source: USAID funding data, as of August 1, 2013.

Basic Education, and Literacy and Technical-Vocational Education and Training

The Basic Education, Literacy, and Technical-Vocational Education and Training program seeks to improve education and vocational-training access for women and other marginalized populations. The program will strengthen MOE's ability to measure student learning outcomes, provide in-service and pre-service training to teachers and administrators, print additional textbooks, and improve the employability of youth by providing literacy and critical skills development.

Afghanistan Workforce Development Program (Planned)

The Afghanistan Workforce Development Program's objective is to increase employment for Afghans by improving workers' skills and linking these

students to credit and business opportunities. The program is expected to provide training or job placement for 25,000 workers, one quarter of them women. It will also improve the training and skills of vocational trainers and enhance technical, vocational, and business management courses. This program aims to establish linkages between training providers and employers.

Summary of Assessment Conclusions and Results

Public Financial Management Assessment (Ernst & Young)

- MOE's Internal Audit Department should be adequately resourced with permanent staff having required professional qualification.
- MOE should form a policy of using only licensed software.
- MOE should make the independent monitoring and evaluation department fully functional.

Ernst & Young's Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

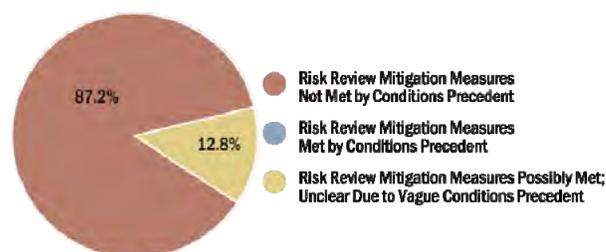
Risk Review (USAID)

- MOE's financial management and accounting system is not adequate to properly manage and account for donors' funds.
- MOE does not have the financial management capacity to manage proposed activities.
- MOE's internal controls are not adequate to manage donors' funding.
- MOE's procurement management units do not have sufficient systems and management capacity to implement activities and manage donors' funds.
- MOE did not fully comply with the Afghan government's procurement laws and regulations.
- MOE's internal control environment is not adequate to mitigate risk of fraud, waste, and abuse, as several key controls are not implemented and it is unclear if the ministry has the capacity to combat corruption effectively.
- MOE does not "have the capacity to encourage and enforce code of government ethics, and/or to discourage potential corrupt acts."

USAID's Conclusion: The U.S. government cannot rely on MOE's systems of operations and internal controls to manage donors' funds.

Summary of Conditions Precedent for MOE Programs

Basic Education, and Literacy and Technical-Vocational Education and Training: USAID/Afghanistan may have included five of the 39 mitigating measures identified in its risk review as conditions precedent in the program implementation letter, but the conditions precedent are too vague, and could allow for the mitigation measure to not be fully implemented.



Afghanistan Workforce Development Program: This is a planned program; no conditions precedent currently exist.

Summary of Suggested Mitigation Measures USAID Identified for MOE

The following table lists the risks USAID identified in its risk review of MOE and identifies whether each risk was included in the program implementation letter as a conditions precedent, an ongoing condition, or not included in the implementation letter at all.

Table 15 - USAID's Stage 2 Suggested Risk Mitigation Measures for MOE

Risk Mitigation Measures	Met	Unclear	Not Met
Develop policy and procedures or mechanisms which require the Ministry to monitor its strategic plan and compare the actual results to strategic plan			<input type="radio"/>
Set terms of reference to for leadership committee			<input type="radio"/>
Submit quarterly reports to the senior management of the ministry to compare actual results to planned activities			<input type="radio"/>
Clearly defined policies and procedures need to be implemented to ensure effective internal control			<input type="radio"/>
Document the control procedures implemented to enable the department to monitor their control activities and provide clear reports for reporting purposes			<input type="radio"/>
Establish an audit committee with oversight responsibility over the internal audit department			<input type="radio"/>
Clearly define key performance indicators to assess the internal audit departments effectiveness			<input type="radio"/>
Conduct risk based audits on various divisions with the ministry			<input type="radio"/>
Monitor and follow - up on the implementation of prior year recommendations given by auditors in their assessment report			<input type="radio"/>
Establish a formal legal department and allocate appropriate qualified staff to the division			<input type="radio"/>
Document the roles and responsibilities of the legal advisor and legal department. Include responsibilities such as a thorough review of ministerial procurement of goods and services			<input type="radio"/>
Review of all contracts entered into with the ministry to safeguard the MoE against any potential legal risk		<input type="radio"/>	
Clearly define system access and implement controls to restrict access to key functions			<input type="radio"/>
Segregate the management and maintenance of all the systems from the system users and transfer to the information technology division			<input type="radio"/>
Use bank accounts for the collection of revenues			<input type="radio"/>
Implement policies and procedures to limit the amount of cash being utilized by the ministry			<input type="radio"/>
Implement proper reconciliation mechanisms to controls cash operations			<input type="radio"/>
Provide budget program and expenditure tracking (BPET) system input access to the provincial level to remain consistent with information in the Afghan Financial Management System (AFMIS)			<input type="radio"/>
Reconcile the BPET system with the data available in AFMIS system on monthly basis			<input type="radio"/>

Develop a proper procedure for numbering and recording of all M-3 forms in order to ensure the completeness of record and to prevent duplicate payments		<input type="radio"/>	
Request signed statement from management certifying that USAID funds will not be used for supporting nepotism and cronyism		<input type="radio"/>	
Prepare formal agreements between the Ministry and its employees which must be signed and kept in the employee files			<input type="radio"/>
Update employees code of conduct and distribute it to all staff			<input type="radio"/>
Conduct ethics training for all employees			<input type="radio"/>
Ensure newly hired staff signs the job description and deliver the copy of all policies, procedure and Job description to the new employee			<input type="radio"/>
Develop annual work objectives for all employees and conduct performance evaluations on all employees on an annual basis			<input type="radio"/>
Conduct training for all staff for necessary skills development and productivity enhancement			<input type="radio"/>
Develop written policies and procedures for the procurement process	<input type="radio"/>		
Request OAA's involvement in all critical procurements	<input type="radio"/>		
Obtain signed conflict of interest from personnel who are involved in the procurement processes			<input type="radio"/>
Develop a plan to introduce procurement reforms		<input type="radio"/>	
Develop procedures for all procurements including procurements below AFS 500,000	<input type="radio"/>		<input type="radio"/>
Develop written approval thresholds for clear identification for approval authority and disseminate these thresholds to all procurement personnel			<input type="radio"/>
Develop formal procedures to handle procurement related disputes			<input type="radio"/>
Develop written policies and procedures for monitoring and evaluation			<input type="radio"/>
Audit all USAID on -budget projects annually			<input type="radio"/>
Submit interim risk based audit reports to USAID			<input type="radio"/>
Disseminate submission of monitoring and evaluation reports to senior ministerial officials for approval and corrective actions		<input type="radio"/>	
Submit quarterly monitoring and evaluation reports to USAID		<input type="radio"/>	

Source: SIGAR analysis of USAID risk reviews and implementation letters.

APPENDIX XI - MINISTRY OF COMMUNICATION AND INFORMATION TECHNOLOGY OVERVIEW

Figure 11 - Assessment and Certification Timeline of MOCIT



Source: SIGAR analysis of USAID public financial management assessments, risk reviews, approval of use of partner country systems, and congressional contact.

The Ministry of Communication and Information Technology's (MOCIT) mandate is to provide communication, information technology, and postal services to citizens of Afghanistan. MOCIT is attempting to bring telecom and information technology access to rural areas, increase high speed internet, extend fiber optic networks, and upgrade other communications and information technology infrastructure. Additionally, MOCIT is implementing E-Afghanistan, a program attempting to promote access to information technology and communications systems for Afghan citizens and to introduce e-governance within public institutions. Table 12 provides an overview of the U.S. Agency for International Development's (USAID) direct assistance programs and funding for MOCIT, as of August 2013.

Table 16 - USAID's Direct Assistance Programs and Funding for MOCIT, as of August 2013

Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursement (millions \$)
District Communication Network	completed	14.2	14.2	14.2
District Communication Network, Policy Capacity Initiative	completed	1.0	1.0	1.0
Total Completed		15.2	15.2	15.2
E-Government Resource Center	planned	3.9	0.0	0.0
Total Planned		3.9	0.0	0.0

Source: USAID funding data, as of August 1, 2013.

E-Government Resource Center (Planned)

The objective of the E-Government Resource Center is to introduce an information technology platform that can improve government operations, increase the transparency and accountability of government transactions, and promote efficiencies in the provision of government services. The program will serve as the source for all of the Afghan government's expertise and guidance for the deployment of E-government programs in other ministries and agencies. The program will focus on capacity building, especially in areas such as procurement of technical assistance, information technology platform and policy development, awareness raising campaigns, and training of Afghan officials.

Summary of Assessment Conclusions and Results

Public Financial Management Assessment (KPMG)

- MOCIT should undertake capacity building measures by providing training for staff in the Finance department.
- MOCIT should enhance the capacity of the internal audit department by hiring staff having the requisite skill set and defining internal audit procedures which are in line with best practices.
- MOCIT specific processes should be defined after carrying out detailed internal control risk assessment in order to mitigate risk of control weaknesses.
- Monitoring and evaluation policies and procedures should be developed and implemented.

KPMG's Conclusion: MOCIT is a high risk entity. Weaknesses identified in the report must be addressed as pre-award disbursement conditions.

Risk Review (USAID)

- MOCIT's financial management and accounting system is not adequate to properly manage and account for donors' funds.
- MOCIT's internal controls are not adequate to manage donors' funds.
- MOCIT's procurement management units do not have sufficient systems and management capacity to implement activities and manage donors' funds.
- MOCIT did not fully comply with Afghan government procurement laws and regulations.
- MOCIT's internal control environment is not adequate to ensure effective and efficient operations and compliance with applicable laws and regulations, safeguard assets against theft and unauthorized use, nor mitigate the risk of corruption.

USAID's Conclusion: The U.S. government cannot rely on MOCIT systems operation and internal controls to manage donors' funds.

Summary of Conditions Precedent for MOCIT Programs

E-Government Resource Center: This is a planned program; no conditions precedent currently exist.

Summary of Suggested Mitigation Measures USAID Identified for MOCIT

The following table lists the risks USAID identified in its risk review of MOCIT. Due to the District Communication Network program being funded as a host country contract there are no conditions precedent to compare the suggested mitigation measures to.

Table 17 - USAID's Stage 2 Suggested Risk Mitigation Measures for MOCIT

Risk Mitigation Measures
Develop clear terms of reference of the leadership committees.
Distribute copies of the terms of reference to each member of the leadership committee.
Document leadership committee meeting minutes
Hire external legal advisor
Involve the legal department in all procurement contracts and agreements
Establish an Audit Committee with an oversight responsibility for the Internal Audit Department
Develop an internal Audit manual

Provide training for personnel at the internal audit department and document those trainings

Develop a plan for Internal Audit to perform risk based audits at HQ and hubs

Develop a MOCIT specific finance manual to address key policies and procedures including checking for funds availability prior to incurring expenditures.

Develop a policy on budget formulation process

Establish an internal budget committee

Define the basis of budget amounts and document the basis

Budget committee approve and sign the budget and document meeting minutes

Include provincial offices in the budgetary formulation process

Compare actual results with budget and investigate variances

Budget Committee meets quarterly to review variance report

Develop and approve a fixed asset management policy

Tag all fixed assets with an identification number

Update fixed assets register on regular basis to reflect: date of purchase, asset type, location, serial number, tagged number.

Provide USAID a list of all fixed or long term depreciable assets funded with USAID funds

Develop an internal cash management policy

Establish a reporting line for the cashier

Develop a petty cash register to record all cash transactions

Conduct surprise cash count and document the result

Develop an internal management policy for staff advances

Develop a register to record staff advances

Perform advance ageing analysis for tracking overdue advances

Develop a plan to automate attendance system at HQ and at the hubs

Document time and attendance for all employees

Link employees pay benefits to the time and attendance register and reconcile regularly and use banking system for all salary payments

Involve finance department in payroll reconciliation

Conduct compliance audit

Perform and document reference checks of all new hires

Obtain signed conflict of interest forms from all staff

Conduct annual ethics training for staff

Prepare job descriptions for all key positions

Develop written policies and procedures for the procurement processes

Request OAA's involvement in all critical procurements

Obtain signed conflict of interest from personnel who are involved in the procurement process

Document procurement committee meeting

Develop a plan to introduce procurement reforms

Involve the legal department in all procurement contracts

Develop a procurement specific database allowing monitoring and analysis of procurement data

Create a monitoring and evaluation department with clearly defined roles and responsibilities

Develop written policies and procedures for monitoring and evaluation

Perform annual audit of all USAID projects

Convene regular audit committee meetings and document meeting minutes

Conduct annual financial and programmatic audits on all USAID projects

Conduct annual risk assessments and develop specific internal procedures with specific responsibilities

Conduct periodic inventory of fixed assets, possibly every six months

Conduct periodic inventory of all fixed or long term depreciable assets purchased with USAID funds and send the inventory confirmation to USAID

Conduct regular performance audit to include asset verification

During financial audit, have auditors verify cash management process

Send monitoring and evaluation reports to the M&E department at the head office and copies to the provincial offices

Submit copies of M&E reports to USAID

Develop clear terms of reference of the leadership committees.

Distribute copies of the terms of reference to each member of the leadership committee.

Document leadership committee meeting minutes

Hire external legal advisor

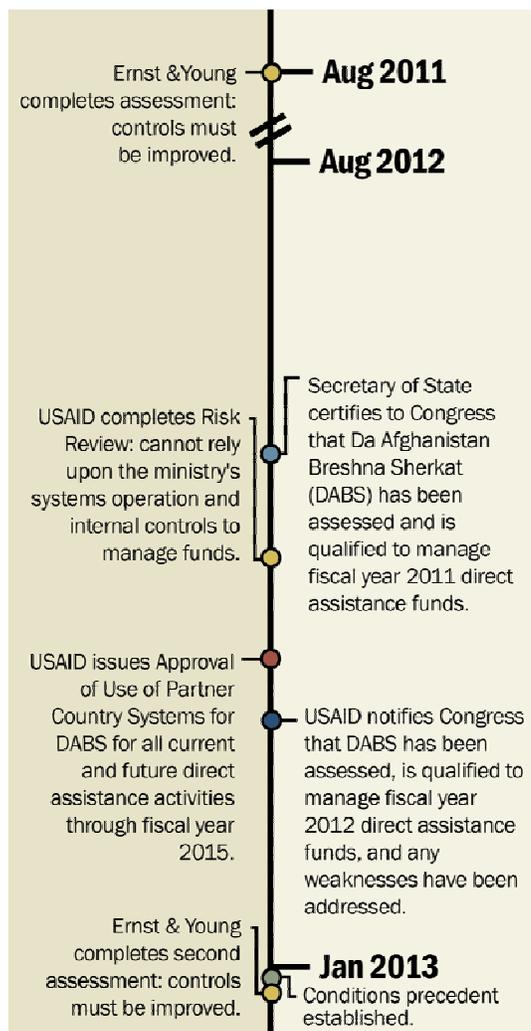
Involve the legal department in all procurement contracts and agreements

Establish an Audit Committee with an oversight responsibility for the Internal Audit Department

Source: SIGAR analysis of USAID risk reviews and implementation letters.

APPENDIX XII - DA AFGHANISTAN BRESHNA SHERKAT OVERVIEW

Figure 12 - Assessment and Certification Timeline of DABS



Source: SIGAR analysis of USAID public financial management assessments, risk reviews, approval of use of partner country systems, and congressional contact.

Da Afghanistan Breshna Sherkat (DABS) is the national power utility company of Afghanistan, operating and managing domestic power generation as well as power importation, transmission and distribution. DABS is owned by shareholders with shares held by the Ministry of Finance, Ministry of Energy and Water, the Ministry of Economy, and the Ministry of Urban Planning and Development. Table 13 provides an overview of the U.S. Agency for International Development's (USAID) direct assistance programs and funding for DABS, as of August 2013.

Table 18 - USAID's Direct Assistance Programs and Funding for DABS, as of August 2013

Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursement (millions \$)
Power Transmission Expansion and Connectivity	active	342.0	263.3	0.0
Kajaki Dam	active	75.0	75.0	0.0
Total Active		417.0	338.3	0.0

Source: USAID funding data, as of August 1, 2013.

Power Transmission Expansion and Connectivity Program (Active)

The Power Transmission Expansion and Connectivity program will commercialize the distribution of electricity in Kabul and key load centers throughout the country. The program will also assist DABS in managing and operating the electric system and provide key equipment for the load centers. With USAID assistance, DABS will also procure a contractor to assist DABS in managing and operating the Southern Electric Power System.

Kajaki Dam (Active)

In the 1950s, American engineers built the Kajaki Dam on the Helmand River as an electrical and irrigation project. The plans called for three turbines to be installed to generate power but progress ceased when the Soviet Union invaded Afghanistan in 1979 and only two turbines have been installed. USAID now plans to provide funds to DABS directly for the third turbine installation.

Summary of Assessment Conclusions and Results

Public Financial Management Assessment (Ernst & Young)

- DABS should bring all of their customers onto a computerized billing system.
- DABS should design a procedure to record all assets transferred between departments.
- DABS should design procedures for conducting a cash count on a daily basis.
- DABS management should introduce a standard format to obtain the monthly expenditure reports from the hubs.

Ernst & Young's Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

Risk Review (USAID)

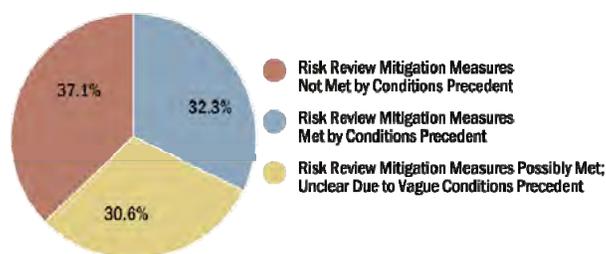
- DABS financial management and accounting system is not adequate to properly manage and account for donors' funds. DABS has been struggling to implement strong financial management controls, and off-balance sheet financing remains a high risk.
- DABS's internal controls are not fully adequate to manage donors' funds as most of the internal controls weaknesses identified in the initial assessment remain unaddressed.
- DABS internal control environment is not fully adequate to mitigate risk of corruption. However, the considerable measures management has taken to address most of the governance weaknesses identified in the initial assessment demonstrate to a certain degree the will to address concerns that could lead to corrupt acts.

USAID's Conclusion: USAID cannot rely on DABS systems operation and internal controls to manage donors' funds.

Summary of Conditions Precedent for DABS Programs

Power Transmission and Connectivity Program: The implementation letter for the program included as conditions precedent 20 of the 62 mitigation measures that the mission identified in its risk review. An additional 19 mitigation measures may be accounted for in the conditions precedent, but the conditions precedent are too vague, and could allow for the mitigation measure to not be fully implemented.

Kajaki Dam: The Kajaki Dam project uses the same conditions precedent as the Power Transmission Expansion and Connectivity Program.



Summary of Suggested Mitigation Measures USAID Identified for DABS

The following table lists the risks USAID identified in its risk review of DABS and identifies whether each risk was included in the program implementation letters as a condition precedent, an ongoing condition, or not included in the implementation letters at all.

Table 19 - USAID's Stage 2 Suggested Risk Mitigation Measures for DABS

Risk Mitigation Measures	Met	Unclear	Not Met
Approve and circulate the five years strategic plan to key management personnel	○		
Prepare annual budgets using the strategic plan	○		
Compare annual budget to actual results			○
Prioritize financial management , accounting and internal control issues on agenda items at BOD meetings	○		
Transfer all assistance funding into an escrow bank account	○		
Implement a capacity building program for financial management and other newly hired key staff	○		
Develop a plan for Internal Audit to perform risk base audit at HQ and hubs	○		
Finalize all outstanding financial statement (2008 to date)	○		
Close all open audit recommendations since 2008	○		
Introduce general ledger preparation into the accounting processes			○
Prepare trial balance for all the sub offices			○
Submit quarterly consolidated financial statements to USAID	○		
Automate the accounting system for HQ and the hubs	○		
Train Financial management staff on the use of the new accounting software		○	
Prepare financial statement in accordance with International Financial Reporting Standards (IFRS) or Generally Accepted Accounting Principles (GAAP)	○		
Back up information technology systems regularly on and off site	○		
Tag all fixed assets with an identification number.	○		
Update fixed assets register on regular basis to reflect: date of purchase, asset type, location, serial number, tagged number.	○		
Define the process for inter departmental transfer of assets			○
Have an approved fixed assets (capitalization) policy	○		
Implement a computerized billing system in all the hubs	○		
Reconcile voltage consumption to receivable account	○		

Categorize customers according to consumption pattern	<input type="radio"/>		
Perform surprise cash count by senior management			<input type="radio"/>
Stamp all invoices received with "received stamp" and all payment vouchers with "paid" stamp			<input type="radio"/>
Obtain monthly expenditures from all the hubs, using the monthly expenditure standard form.	<input type="radio"/>		
Extend the automated attendance system to the hubs	<input type="radio"/>		
Document time and attendance for all employees	<input type="radio"/>		
Link employees pay benefits to the time and attendance register and reconcile regularly	<input type="radio"/>		
Conduct compliance audit			<input type="radio"/>
Obtain signed conflict of interest forms from all staff	<input type="radio"/>		
Conduct annual ethics training for staff	<input type="radio"/>		
Prepare job descriptions for all key positions	<input type="radio"/>		
Perform reference checks of all new hires		<input type="radio"/>	
Develop template for exit interviews		<input type="radio"/>	
Perform analysis on the reasons of employee outflow and make recommendations to the Senior management Group (SMG) and Board of Directors		<input type="radio"/>	
Develop a mechanism to pre-qualify vendors for routine purchases	<input type="radio"/>		
Obtain signed conflict of interest from personnel who are involved in the procurement processes	<input type="radio"/>		
Develop a plan to introduce procurement reforms	<input type="radio"/>		
Request OAA's involvement in all critical procurements			<input type="radio"/>
Involve the legal department in all procurement contracts	<input type="radio"/>		
Establish a separate M&E department from the Internal Audit			<input type="radio"/>
Monitoring personnel at the hubs and provincial level report the director of M&E at HQ	<input type="radio"/>		
Audit all USAID projects annually	<input type="radio"/>		
Conduct periodic inventory of fixed assets, possibly every six months	<input type="radio"/>		
Provide Signed Statement to USAID that funds provided will not be used to pay fines or liabilities associated with Da Afghanistan Breshna Mousasa and Power Construction Entity merger.	<input type="radio"/>		
Provide copies of audited financial statements to USAID for the years 2010, 2011, and 2012	<input type="radio"/>		

Develop a chart of accounts that clearly accounts for USAID funds.	<input type="radio"/>		
USAID to conduct periodic financial on DABS with DABS' internal audit department and train department of risk-based audit.	<input type="radio"/>		
Conduct comprehensive and nationwide survey on all electricity users and develop and roster		<input type="radio"/>	
Develop a billing system based on that roster	<input type="radio"/>		
During financial audit have auditors verify the meter readers data		<input type="radio"/>	
Develop revenue projections and compare projections to actual receipts and analyze differences	<input type="radio"/>		
Submit annual audited financial statements to USAID	<input type="radio"/>		
Develop a fixed asset management policy	<input type="radio"/>		
Provide USAID a list of all fixed or long term depreciable assets funded with USAID funds	<input type="radio"/>		
Conduct periodic inventory of all fixed or long-term depreciable assets purchased with USAID funds and send the inventory confirmation to USAID	<input type="radio"/>		
Conduct regular performance audit to include asset verification	<input type="radio"/>		
Complete and approve Business Continuity and Disaster Recovery Plan.	<input type="radio"/>		
Convene regular audit committee meetings and document meeting minutes			<input type="radio"/>
Implement Basic Internal controls in the financial management system.	<input type="radio"/>		
Submit copies of M&E reports to USAID.	<input type="radio"/>		

Source: SIGAR analysis of USAID risk reviews and implementation letters.

APPENDIX XIII - MINISTRY OF FINANCE OVERVIEW

Figure 13 - Assessment and Certification Timeline of MOF



Source: SIGAR analysis of USAID public financial management assessments, risk reviews, approval of use of partner country systems, and congressional contact.

The Ministry of Finance (MOF) is responsible for the management and execution of the Afghan government budget, the collection of taxes, the organization and control of public expenditure, payments to the government, and the management of customs. Table 14 provides an overview of the U.S. Agency for International Development's (USAID) direct assistance programs and funding for MOF, as of August 2013.

Table 20 - USAID's Direct Assistance Programs and Funding for MOF, as of August 2013

Program	Status	Total Estimated Commitments (millions \$)	Total Obligations (millions \$)	Total Disbursement (millions \$)
Salary Support Program	completed	2.0	1.7	1.7
Total Completed		2.0	1.7	1.7
Civil Service Technical Assistance Program	active	36.3	36.3	28.8
Total Active		36.3	36.3	28.8

Source: USAID funding data, as of August 1, 2013.

Civil Service Technical Assistance Program (Active)

The goal of the Civil Service Technical Assistance Program is to recruit, hire, place, and support technical advisors throughout government institutions. These advisors do not replace civil servants, but assist their Afghan counterparts in building institutional capacity.

Summary of Assessment Conclusions and Results

Public Financial Management Assessment (Ernst & Young)

- MOF should tag all fixed assets with unique fixed asset identification numbers.
- MOF should draft a standard set of legal terms and conditions and every contract above a certain threshold should be formally vetted by the legal advisory.
- MOF should implement a debt strategy.
- MOF should prepare a separate follow up by the internal audit team.

Ernst & Young’s Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

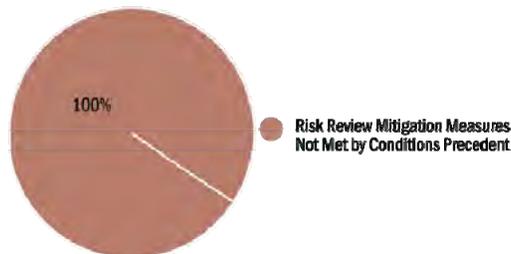
Risk Review (USAID)

- MOF’s current policies, procedures and internal controls framework are generally sufficient to adequately safeguard and account for donors’ funds. However, there are material control weaknesses that can have adverse impact on the MOF’s capacity in regards to managing donors’ funds.
- MOF has adequately designed controls to comply in all material respects, with applicable laws and regulations and no material exception thereto has been observed.
- MOF financial management and accounting system is adequate to properly manage and account for donors’ funds, except for the conditions detailed, to enhance its financial management and accounting system.
- MOF procurement management units have sufficient systems and management capacity, except for some weaknesses as detailed below.

USAID’s Conclusion: USAID cannot fully rely on MOF systems operation and internal controls to manage donors’ funds.

Summary of Conditions Precedent for MOF Programs

Civil Service Technical Assistance Program: Of the 46 mitigation measures identified in USAID/Afghanistan’s risk review, the mission did not list any as conditions precedent in the program implementation letter.



Summary of Suggested Risk Mitigation Measures USAID Identified for MOF

The following table lists the risks USAID identified in its risk review of MOF and identifies whether each risk was included in the program implementation letter as a condition precedent, an ongoing condition, or not included in the implementation letter at all.

Table 21 - USAID’s Stage 2 Suggested Risk Mitigation Measures for MOF

Risk Mitigation Measures	Met	Unclear	Not Met
Define and document terms of reference for its Board Management Committee that specify their scope of work, roles and responsibilities.			○
Devise standard audit program and a checklist to serve as a guide for all audit engagements and training of IAED staff on such standardized checklists.			○
The high risk issues requiring immediate attention should be covered in separate follow up audits			○

The follow up report should be discussed in the Audit Committee meeting and appropriate actions should be taken accordingly.			<input type="radio"/>
Include risk base audit in the annual audit program.			<input type="radio"/>
Develop a policy which requires the Ministry periodically review actual performance against its strategic plan, document same and be presented to the Strategic Committee			<input type="radio"/>
A clear and robust Business Continuity and Disaster Recovery plan should be developed and backup information on a regular basis			<input type="radio"/>
Only licensed software should be used for the IT systems at the Ministry.			<input type="radio"/>
Assess the sustainability of the capacity of departments and consider ways in which knowledge and skill could be passed on to Afghan staff			<input type="radio"/>
Internal control written procedures should be comprehensively documented and communicated across the organization, management should monitor the understanding of those procedures by operational employees			<input type="radio"/>
Petty cash should be counted and reconciled by the designated personnel (who is independent of custodian) with petty cash register on at least a weekly basis.			<input type="radio"/>
Use impress system of cash in hand			<input type="radio"/>
Monthly reconciliation should be made between current and last month payroll.			<input type="radio"/>
All fixed assets should be tagged with unique fixed asset identification number and the existence be verified during yearly audits			<input type="radio"/>
Fixed assets register should be updated on regular basis to reflect: date of purchase, asset type, location, serial number, tagged number, respective user ect/			<input type="radio"/>
Conduct periodic inventory of fixed assets, possibly every six months and the results should be presented to the Steering Committee			<input type="radio"/>
Reconcile inventory record with financial record.			<input type="radio"/>
Mof should establish a committee to closely monitor the execution of its budget and development programs and provide feedbacks to management on regular basis			<input type="radio"/>
Develop a plan to automate attendance system at the provincial revenue and custom offices which should then be used by the Finance Directorate to process the payroll of staff to ensure accuracy.			<input type="radio"/>
All the documents involved in the recruitment process should be filed at a single location in the employee permanent files.			<input type="radio"/>
A senior person in the Record Keeping section should review the employee permanent file after it has been prepared by Record Keeping Officer for ensuring that all required documents have been filed.			<input type="radio"/>

The job description of the employee should be signed off by the respective employee as well as the Head of Directorate, as an evidence of concurrence with the job responsibilities and should be documented in the employees' personal files			<input type="radio"/>
On a quarterly basis a comparison should be prepared between the planned and actual trainings, in order to identify the progress.			<input type="radio"/>
HR Directorate should develop a format for the exit interview and conduct discussion with the staff and document the reasons on the exit interview form			<input type="radio"/>
The form should be signed off by the employee and the HR Director and maintained in the employee file.			<input type="radio"/>
A formal process for reference checks should be put in place			<input type="radio"/>
The reference checks should be maintained in the permanent file of the employee.			<input type="radio"/>
A standard set of legal terms and conditions should be drafted and every contract above certain defined threshold should be formally vetted by the legal advisory.			<input type="radio"/>
A standard checklist should be developed for documents to be maintained in the file.			<input type="radio"/>
Should set a frequency at which it should generate the monitoring reports using the MIS. Monitoring reports should be reviewed by the Procurement Director and the variances should also be documented.			<input type="radio"/>
A threshold may be determined (such as +/- 10%), and if there is any variance above the threshold, the reasons should be documented and investigated in detail			<input type="radio"/>
Procurement Directorate should enter the list of registered bidders in PMIS.			<input type="radio"/>
The vendors list should be periodically evaluated for their performance and updated accordingly.			<input type="radio"/>
The strategic plan should be updated on an annual basis to incorporate the impact of the dynamic economic environment.			<input type="radio"/>
The reporting line of OIU should be to the Minister directly to minimize any conflict of interest of segregation of duties.			<input type="radio"/>
The focal points reporting to the PIU should be independent of the directorate and/or mustofiat.			<input type="radio"/>
A training plan should be established and be linked with the annual staff appraisals.			<input type="radio"/>
A system based technical monitoring system should be implemented by PIU.			<input type="radio"/>
The technical monitoring system should be interlinked with AFMIS to generate reports which link financial and physical progress of the projects.			<input type="radio"/>
Independent third parties surveys should be carried out to ascertain the effectiveness / efficiency of services provided by the line ministries and reported to the Ministry of Finance			<input type="radio"/>

Since the information is readily available with the Ministry of Finance, the information can be disclosed			<input type="radio"/>
Arrangements be made to incorporate contingent liabilities in budget planning process			<input type="radio"/>
Vendor analysis should be undertaken to assess the volume of contracts granted to particular vendors.			<input type="radio"/>
The system / IT platform be enabled so as to keep a record of the assets acquired and the same be integrated with the AFMIS the treasury's main financial and accounting system			<input type="radio"/>
A formal liquidity contingency plan should be drawn up.			<input type="radio"/>
The debt strategy should be augmented to incorporate these aspects.			<input type="radio"/>

Source: SIGAR analysis of USAID risk reviews and implementation letters.

APPENDIX XIV - OVERVIEWS OF MINISTRIES WITH PUBLIC FINANCIAL MANAGEMENT ASSESSMENTS, BUT NO USAID RISK REVIEWS

Ministry of Rural Rehabilitation and Development

The Ministry of Rural Rehabilitation and Development (MRRD) was established to ensure the social, political, and economic well-being of rural Afghanistan. The ministry assists with the provision of services and local governance in rural areas. The ministry emphasizes promoting alternatives to poppy development and assisting the poor and vulnerable.

Public Financial Management Assessment (KPMG)

- The ministry has an absence of coordination mechanisms.
- The ministry has capacity constraints emanating from human resource quality.
- The ministry faces issues in financial and treasury management functions.
- The ministry's management has shown a lack of management responsiveness towards audit recommendations.

Overall Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions. The ministry is a high-risk for future funding.

Afghanistan Independent Human Rights Commission

The Afghanistan Independent Human Rights Commission (AIHRC) was established to protect and promote human rights in Afghanistan. The Commission also investigates reports of human rights violations in the country.

Public Financial Management Assessment (KPMG)

- AIHRC's control environment's was assessed as high risk and capacity gaps pose major risks which must be addressed before the first disbursement.
- AIHRC's internal audit department is not functioning and according to the management auditors have not conducted any audits.
- AIHRC's procurement policy is not in compliance with best practices as required under Afghan procurement law and USAID regulations.

Overall Conclusion: Capacity gaps pose some manageable risks and certain strengthening measures must be completed before the first disbursement.

Independent Administrative Reform and Civil Service Commission

The Independent Administrative Reform and Civil Service Commission (IARCSC) was established to create a system of civil servants to help bolster the Afghan government. The civil servants serve all ministries and enhance the capabilities and effectiveness of the Afghan government.

Public Financial Management Assessment (Ernst & Young)

- IARCSC must improve its corporate governance structure.
- IARCSC must improve its financial management, budgeting and accounting systems.
- IARCSC must monitor its procurement and purchasing system.

Overall Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

Ministry of Public Works

The Ministry of Public Works (MOPW) is responsible for road maintenance, repair, and construction, and for the construction of railroad tracks across the country. The only roads that MOPW is not responsible for are rural roads, which are overseen by the Ministry of Rural Reconstruction and Development.

Public Financial Management Assessment (Ernst & Young)

- MOPW needs to strengthen its internal audit department.
- MOPW should enhance its budgeting capacity.
- MOPW should strengthen the monitoring and evaluation process.
- MOPW should develop formal procedures for the procurement process.

Overall Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

Ministry of Information and Culture

The Ministry of Information and Culture (MOIC) is responsible for managing tourism and culture, media, national radio and television, and youth affairs in Afghanistan. The ministry promotes local cultures and skills, broadcasts national media through a variety of means, including newspaper, radio, television, promotes tourism to promote economic development, and encourages youths to become successful in various fields.

Public Financial Management Assessment (Ernst & Young)

- MOIC should establish a monitoring and evaluation department.
- MOIC should establish a contract management unit.
- MOIC should reconsider its organization structure in respect to finance, policy and planning, and procurement.
- MOIC revenue collection needs to be strengthened.
- MOIC fixed assets should be recorded and verified.

Overall Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

Ministry of Economy

The Ministry of Economy's goal is to increase economic and social development and establish economic policies for Afghanistan. The ministry attempts to provide balanced economic development through the encouragement of private sector development with a focus on improving income per capita, domestic production, employment levels, and price sustainability.

Public Financial Management Assessment (Ernst & Young)

- The ministry should strengthen its sectoral directorates.
- The ministry should clearly document the mechanism for maintaining backup and subsequent retrieval of documents.
- The ministry should develop a fixed asset register.
- The ministry should develop an automated financial management and accounting system.

Overall Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions.

Ministry of Higher Education

The Ministry of Higher Education's mission is to expand and develop Afghanistan's institutions for higher education through training of teachers, establishing curriculum and special education programs, providing in-service training, and promoting further education for university faculty.

Public Financial Management Assessment (Ernst & Young)

- The ministry should form a management and leadership committee.
- The ministry should develop a plan for maintaining back up and subsequent retrieval of critical documents.
- The ministry should develop an automated financial management and accounting system.
- The ministry should develop a fixed asset register.

Overall Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions. Overall risk level as a result of the assessment is considered to be high.

Ministry of Transport and Civil Aviation

The Ministry of Transport and Civil Aviation designs, regulates, and manages air and ground transportation while operating airports and the national airline. In addition, the ministry operates numerous other enterprises connected to the transport business.

Public Financial Management Assessment (KPMG)

- The ministry should address capacity gaps in the control environment.
- The ministry should establish an independent internal audit function.
- The ministry should develop detailed monitoring and evaluation policies and procedures.

Overall Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions. The ministry is a high-risk for future funding.

Ministry of Energy and Water

The Ministry of Energy and Water manages all water and energy resources in Afghanistan. The ministry creates energy and water development policies, manages resources, designs and implements laws and regulations, conducts studies, and provides technical support to other ministries when needed.

Public Financial Management Assessment (KPMG)

- The ministry's revenue budget is not duly supported by detailed analysis and valid assumptions.
- The ministry's cashier is solely responsible for petty cash and cash books are not maintained.
- The ministry's reconciliation of inventory records with financial records are not maintained.

Overall Conclusion: Material weaknesses identified in the report must be addressed as pre-award disbursement conditions. The ministry is a high-risk for future funding.



UNCLASSIFIED

November 2, 2012

ACTION MEMORANDUM FOR THE ADMINISTRATOR

THROUGH: AA/OAPA – J. Alexander Thier

SUBJECT: Request to Waive Compliance with Automated Directives System (ADS) Chapter 220 Public Financial Management Risk Assessment Framework (PFMRAF) Procedures for All Appropriated Funds made Available to USAID/Afghanistan through Fiscal Year 2013

Recommendation

That you waive compliance with ADS Chapter 220 procedures in accordance with ADS section 220.3.2.2 in order to avoid impairment of U.S. Government Foreign Assistance Objectives.

The requested waiver will cover all funds appropriated and made available to USAID/Afghanistan through and including FY 2013 appropriations. This waiver will allow the Agency to meet the commitments made by the United States Government (USG) to the Government of the Islamic Republic of Afghanistan (GIROA). As described below, this waiver will avoid impairment of USG foreign assistance and foreign policy objectives in Afghanistan. These objectives – in the case involving commitments of direct assistance to GIROA – were announced by the USG in January 2010 and reaffirmed by Secretary of State Clinton and you in July 2010 at the Kabul Conference.

Approve _____

Disapprove _____

NOV 20 12

Background

USAID's development policy ultimately must support long-term, sustained progress and make assistance unnecessary in the long term by partnering with countries to use their internal systems, build their capacity, strengthen core institutions, maximize the impact of assistance they receive, and provide for their people. USAID's assistance is most effective when it can work through partner country public financial management (PFM) systems rather than around them, to ensure that the aid received reinforces the accountability of a government to its people.

Since 2002, the U.S. Government assistance strategy for Afghanistan has been to work with international partners in a civilian-military effort to combat terrorism and re-establish security and stability within the country. In January 2010 at the London Conference on Afghanistan, the USG announced a public strategic foreign-assistance decision, reaffirmed by Secretary of State Clinton and you at the July 2010 Kabul Conference, which committed the U.S.

Government to provide at least 50 percent of U.S. Government assistance directly to GIRoA, to be channeled through GIRoA's core budget systems within two years (2012). During the July 2010 Kabul Conference, the international donors endorsed the Public Financial Management (PFM) Roadmap. The PFM Roadmap is the implementation plan for the National Priority Program Number One. The first action under the PFM Roadmap was to assess a total of 14 line ministries under a single harmonized donor evaluation. An international donor group that included the U.S. Embassy and USAID representatives agreed that the PFM Roadmap assessment should proceed. The World Bank offered to provide support to the Ministry of Finance (MoF) Budget Department and to prepare the Terms of Reference to contract with an independent consulting firm to lead the PFM assessments.

GIRoA and the World Bank contracted with a British Certified Public Accounting firm to conduct 14 individual Ministerial assessments to be completed within two GIRoA fiscal years. In June 2011, the first draft assessment report on one of the 14 ministries was received. USAID obtained an initial copy of the draft assessment report from the U.S. Treasury representative assigned to the MoF. Upon review of the draft document, the USAID Mission determined that the assessment did not provide the level of review USAID would require to make risk-determination evaluations that could lead to direct Government to Government (G2G) assistance agreements, sufficient to meet the USG's standards of fiduciary safeguards. Specifically, the GIRoA/World Bank contracted assessments did not include testing of entity level Public Financial Management (PFM) systems in order to validate overall systems operations and internal controls, and identify performance risks.

USAID immediately opened a series of dialogues with GIRoA about the need for a more in-depth systematic review of the line Ministries required by USAID. During this same timeframe, a turnover of key players involved in the contract team performing the assessments, delayed the GIRoA-World Bank assessment engagements. By the end of June 2011, USAID convinced GIRoA of the benefits of conducting a second series of more-stringent assessments of each line Ministry. USAID negotiated with GIRoA and arrived at a new scope of work for these assessments, which USAID unilaterally contracted for, beginning in July 2011.

In August 2011, the Agency issued a new draft policy – ADS Chapter 220 – pertaining to the use of reliable partner country systems for direct G2G assistance. That policy chapter was substantially updated in late March 2012 and continues to undergo modifications – the latest in July 2012, where risk assessment questionnaire guidelines were modified. This ADS chapter with its latest modifications now requires a multi-stage approach in the process leading to a decision of whether USAID should consider use of a partner country's systems to implement direct assistance programs.

The first step in the ADS 220 process for assessing the viability of a partner country's systems to manage G2G assistance is an Enhanced Democracy, Human Rights, and Governance (DRG) Review and the Stage 1 PFMRAF Rapid Appraisal. The DRG macro-level assessment is designed to determine whether a G2G investment could empower a government at the expense of its people. The DRG review is a Washington-led Mission assessment. The Stage I Rapid Appraisal focuses on public financial-management systems and includes an analysis of democratic accountability systems, with an emphasis on oversight and governance relating to

public financial management (including the DRG Review). Stage 1 is intended to be a high-level overview of partner country systems and governance structures. It is intended to provide the Mission a high-level snapshot of fiduciary risks associated with use of the partner country PFM systems and helps inform the decision as to whether the Mission should move forward and undertake a more rigorous, formal Stage 2 PFMRAF Risk Assessment. As noted above, USAID/Afghanistan has been engaged in direct G2G assistance to GIRoA for several years. The Mission did not undertake the Stage 1 DRG assessment or PFMRAF Rapid Appraisal because the guidance did not exist at the time the Mission started G2G assistance to GIRoA.

The second step in the ADS 220 process is the PFMRAF Stage 2 Risk Assessment. Current Agency policy set forth in ADS 220 requires that upon conclusion of the macro-level assessment (DRG review and PFMRAF Stage 1), risk tolerance is evaluated jointly between the Mission, the Regional Bureau, the DCHA Bureau, and the global partner country systems risk management team (GPCSRMT) within the office of the CFO. If the joint determination by the Mission and Washington results in a determination the risk tolerance is acceptable at the macro level, then the Mission could consider whether to proceed with further assessment regarding the risks appurtenant to direct bilateral G2G assistance to the Partner Country Government. Upon a decision to do so, the USAID Mission would then proceed with the PFMRAF Stage 2 Risk Assessment, an entity-level assessment of the individual Ministry to identify implementation risks. This would enable the Mission to develop a risk mitigation strategy tailored to individual G2G activities and specific, identified risk factors with a particular Ministry.

While USAID/Afghanistan has not fulfilled every step in the ADS 220 process because the Mission never underwent the macro-level assessment, doing so at this time would undermine the U.S. Government's foreign assistance and foreign policy objectives and is also unnecessary. Given the history of G2G assistance in Afghanistan, this situation is understandable. Macro-level assessments are to guide the decision process about whether G2G assistance should be considered as a bilateral assistance objective. In Afghanistan, that decision was made several years ago at the highest levels of the U.S. Government. The USG's foreign policy decision in January 2010, which was reaffirmed by Secretary Clinton and you at the Kabul conference in July 2010, strongly reiterated the U.S. commitment to direct G2G assistance to GIRoA. This commitment was not made subject to review of macro-level risk in Afghanistan. Essentially, the foreign policy decision to engage in G2G assistance in Afghanistan has replaced the first step under ADS 220 outlined above – the DRG Review and Stage 1 PFMRAF Rapid Appraisal. At this point, it would be counter-productive and potentially inconsistent with articulated foreign policy and foreign assistance objectives of the U.S. Government for the Mission to go through this process with the current GIRoA administration.

ADS 220 also requires a DRG Review, which is applied during the course of the Stage 1 PFMRAF Rapid Appraisal to determine whether G2G programming would empower a government at the expense of its people. Because guidelines for the DRG portion of the assessment are still under development, it is not possible to conduct a full review without undue delay and thus impairment of U.S. foreign policy and foreign assistance objectives. However, USAID will ensure transparency and accountability for any funds or other resources provided to the GIRoA. USAID will also ensure that the assessment and other requirements of Section 7031 of the FY 12 Foreign Operations Appropriations Act are fully met and documented.

More importantly, the Mission has complied with the spirit and purpose of that guidance. The Mission has exercised appropriate due diligence in the entity level assessments undertaken of each line Ministry and parastatal organization and is appropriately identifying risks and designing specific risk mitigation strategies into each entity's G2G assistance agreement. The Mission has worked closely with the the CFO and believes these Mission-initiated entity level assessments are in substantial compliance with the Stage 2 Risk Assessment guidance as promulgated currently under ADS Chapter 220. By "substantial compliance" the Mission means that the PFM systems of each entity have been tested to validate overall systems operations and internal controls, and as a result performance risks have been identified enabling the development of risk-mitigation measures for inclusion into each G2G assistance agreement. As a result, conducting a Stage 2 Assessment at this point would be duplicative and wasteful, using U.S. Government funds needlessly and intruding upon the GIRoA entities already assessed for no additional value.

In addition to having substantially fulfilled Stage 2 of the PFMRAF, all assistance provided directly to GIRoA will comply with all applicable legal requirements.

The U.S. Government assistance strategy for Afghanistan is entering a transitional phase expected to continue until the end of calendar year 2014, when military operations will be sequentially curtailed, and the Afghan government will become responsible for ensuring stability and security in the country. The U.S. Government has made significant commitments for planned activities during this transition phase. These G2G activities through 2014 are planned at an estimated obligation level of approximately \$ 2.4 billion dollars, using FY 2011, FY 2012, and FY 2013 appropriated funds.

In light of the high-level U.S. political commitments made to GIRoA regarding direct G2G assistance, formal, mechanical compliance with ADS 220 assessment requirements, particularly the DRG review and PFMRAF Stage 1 Rapid Appraisal and the Stage 2 Assessment, is unnecessary and runs the risk of doing substantial harm to U.S. Government foreign-assistance objectives in Afghanistan. Robust assessments of the current Afghan political and governance situation, performed on the same terms as assessments done in other countries where USAID works, could cause the U.S. Government not to fulfill the existing promises of assistance to GIRoA made by the President, the Secretary of State and you. Even with a waiver of ADS 220 policy, the Mission is and will continue to be in compliance with all applicable laws.

This waiver will apply to all funds appropriated and made available to USAID/Afghanistan through and including FY 2013 appropriations.

Resource Implications

Per ADS 220.3.2.2, waivers of the procedures for commitments in excess of \$50 million must be initiated by the cognizant Assistant Administrator, cleared by the CFO and the GC, and approved by the Administrator.

APPENDIX XVI - COMMENTS FROM THE U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT AND SIGAR'S RESPONSE



MEMORANDUM

January 23, 2014

TO: Mr. John F. Sopko
Special Inspector General for
Afghanistan Reconstruction (SIGAR)

FROM: Donald L. "Larry" Sampler (s)
Assistant to the Administrator for
Afghanistan and Pakistan

SUBJECT: USAID Response to SIGAR Audit Report, "Afghan
Ministry Assessments:" (SIGAR 14-X Audit Report)

Executive Summary

Direct assistance is an important part of USAID's bilateral assistance program in Afghanistan in support of U.S. national security objectives. Oversight of these programs is critical and we welcome SIGAR's continuing examination of these efforts. While there is no way to eliminate risk completely or guarantee a result in undertaking development programming in Afghanistan, USAID, in the field and in Washington, is acutely conscious of the trust that has been placed with us to safeguard taxpayer funds while implementing development programs in support of the national interest. We are always looking at ways to refine and adopt improvements to our systems and look forward to continuing to work with SIGAR In that regard.

This SIGAR audit report on direct assistance to Afghanistan looks closely at a series of risk assessments and internal risk reviews funded and conducted by USAID to examine the internal processes of specific Afghan Ministries in advance of any direct assistance. This was done to ensure appropriate risk mitigation measures are in place and that USG funds are safeguarded, consistent with USAID procedures and Congressional requirements.

SIGAR's audit did not identify waste, fraud or abuse in USAID's direct assistance program. While the audit report examines and calls attention to the risks USAID identified in the Ministries that could potentially impact direct assistance programming in Afghanistan, it fails to acknowledge the full range of risk mitigation measures USAID subsequently employed. On the first page of

See SIGAR
Comment 1.

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the draft report, SIGAR explicitly states, “We did not examine the implementation of USAID-funded direct assistance programs, assess the effectiveness of USAID’s methods for safeguarding U.S. direct assistance funds, or determine whether fraud and misuse of funds existed with these programs.”

We therefore do not believe the report has any basis to conclude that USAID has failed to fully implement measures designed to mitigate the risks that we ourselves identified. We look forward to working closely with SIGAR in the future, should they choose to examine the actual implementation of these programs.

See SIGAR
Comment 2.

The Department of State and USAID have complied fully with the spirit and the letter of the law in providing Congress extensive information on the risks and risk mitigation measures for direct assistance in Afghanistan. In addition to the formal certifications and notifications required by law, USAID and the State Department provide Congress information through a variety of means, including testimony, briefings, written responses to questions, and additional Congressional notifications of intent to obligate appropriated funding. We are prepared to appropriately respond to any further requests from Congress with information on these programs.

See SIGAR
Comment 3.

We appreciate SIGAR’s review of the Department of State’s Fiscal Year 2011 certification and USAID’s FY2012 Congressional Notification with respect to direct assistance and will use SIGAR’s analysis to improve future submissions. The FY 2011 government assistance certification was submitted to Congress by the Department of State in September 2012 with an accompanying Memorandum of Justification that stated USAID had completed Public Financial Management Risk Assessments (risk assessments) of the Ministry of Finance and Ministry of Higher Education. This information was repeated in USAID’s FY2012 country Congressional Notification, which was transmitted in November 2012. In response to concerns raised by SIGAR about when the two assessments were finalized, USAID is reviewing the circumstances surrounding the receipt and completion of the assessments. We have confirmed that the risk assessments for the Ministry of Finance and Ministry of Higher Education that USAID made available to congressional staff, upon request, were the final versions of the assessments. USAID had in place at the time an overall process, that was accurately described in submissions to Congress, to identify deficiencies at all potential ministry partners and put in place strong risk mitigation measures prior to the disbursement of any FY 2011 on-budget funding.

We note that the memorandum of justification that accompanied the Fiscal Year 2011 certification said explicitly that the certification was not the end of our oversight process: “For each activity implemented through a direct government-to-government mechanism, USAID will develop, through project implementation letters ... specific terms and conditions applicable to each activity...” This clearly indicated that USAID was continuing to work with the ministries to develop further plans to implement the findings of the risk assessments.

We appreciate SIGAR’s acknowledgement of the extensive effort made by USAID to ensure that our assistance to the Afghan government is implemented with rigorous oversight and accountability to mitigate the risks USAID identified in its assessments of Afghan ministries. In particular we note that SIGAR highlights “positive developments” in our work, including the risk mitigation plan developed for Da Afghanistan Breshna Sherkat (DABS) that identifies specific mitigation measures to be employed to confront each weakness. USAID has already completed similar risk mitigation plans for individual ministries with which we have direct assistance programs.

See SIGAR
Comment 4.

Protection of Sensitive Information

Continued U.S. development engagement is critical to Afghanistan’s stability and to protecting the vital interests of our own country. Improving governance, building infrastructure, creating economic opportunity, and enhancing the health and education of the people of Afghanistan are essential to solidifying our military gains and advancing our political and diplomatic goals for the country and the region.

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5.

USAID has learned from its experience in Afghanistan and in similar countries around the world and has applied best practices to design and implement on-budget and off-budget programs to mitigate risk. A key first step is understanding the precise capacity of government partners in order to protect U.S. funding from waste and abuse.

In this context, the United States requires close cooperation from government partners in providing very sensitive information to us about the capacity and deficiencies at potential recipient ministries in order to protect USG funds and ultimately improve ministry capacity. This information is truly sensitive and could be exploited in Afghanistan’s highly political environment. USAID and the State Department have previously notified SIGAR that certain information provided in connection with this audit, including the risk assessments and

internal risk reviews, is Sensitive But Unclassified (SBU¹) and therefore not appropriate for public distribution. In addition, USAID notes that the audit report's appendices 1-15 and other portions of the report directly quote information taken from SBU documents that is not appropriate for public distribution.

These risk assessments and internal risk reviews were generated for the internal use of the US Government and the entities that are the subject of the assessments. Demonstrating their openness and willingness to strengthen ministerial management controls, parts of the Afghan government provided unprecedented access for the independent auditors to complete the risk assessments based on understandings that the results of the risk assessments would not be made public. Unfortunately, public release of these materials will likely result in reduced cooperation from the Afghan Government and could undermine our ability to conduct proper oversight of direct assistance programs in the future. USAID and State Department at various levels have requested on numerous occasions that SIGAR not make this sensitive material available to the public, and we again request that SIGAR not make public sensitive information that could damage our bilateral relationships with the Government of the Islamic Republic of Afghanistan.

The conclusions of the USAID internal risk review for each Ministry are not in dispute and their specific details are not relevant to the findings of this audit, which focuses on the process by which the assessments were conducted. The fact that this audit did not examine the effectiveness of the risk mitigation measures put in place by USAID argues further for removal of specific details quoted from internal risk reviews on Pages 8-9 of the draft report as well as in the appendices. We are ready to work with SIGAR to identify again the specific text which we consider most damaging if released.

See SIGAR Comment 6.

Draft Audit Recommendations

The Department of State and USAID agree with the substance of the three recommendations and are already complying with them. Therefore we recommend that all three be closed.

Recommendation 1: The USAID Administrator require compliance with all parts of Automated Directive Systems (ADS) 220 -except for the Stage 1 macro-level review - for the use of all direct assistance funds for fiscal year 2014 and beyond.

¹ Sensitive But Unclassified (SBU) is a designation equivalent to For Official Use Only (FOUO), which is used by the military and other agencies for information that warrants a degree of protection and administrative control and meets legal or regulatory criteria for exemption from public disclosure.

USAID Comments: USAID agrees with this recommendation, and in fact, USAID already complies with ADS 220 stage 2 requirements. For future years funding, USAID intends to continue to comply with the requirements of ADS 220, with the exception of completion of the Stage 1 assessment, as recommended by SIGAR, and therefore requests closure of this recommendation.

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Comment
7.

Recommendation 2: USAID/Afghanistan fully inform Congress of the status of ministry assessments USAID or its contractors have completed, the mitigating measures Afghan ministries have implemented, and the level of risk to U.S. funds.

USAID Comments: USAID has provided extensive information to Congress about direct assistance and regularly responds to Congressional requests for information regarding USAID's direct assistance in Afghanistan, including risks and risk mitigation measures. In early 2014, through the regular notification procedures of the Appropriations Committees, USAID will be providing updated information on its direct assistance program, and is ready at any time to provide Congress with access to additional information. As USAID is regularly updating Congress and providing extensive information on direct assistance in Afghanistan, we request this recommendation be closed.

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Comment
8.

Recommendation 3: USAID/Afghanistan develop a plan, similar to the one created for Da Afghanistan Breshna Sherkat (DABS), for each Afghan ministry that has a completed USAID risk review that defines how each of the risks identified are being or will be mitigated, and suspend direct assistance disbursement to these ministries until these plans are completed.

USAID Comments: USAID agrees with this recommendation. USAID has identified the risk mitigation plan developed for DABS as a best practice and has already prepared similar plans for the six ministries receiving USAID direct assistance. While USAID prepared a narrative risk report as part of each internal risk review, the DABS risk mitigation plan highlighted by SIGAR presents this same information in a matrix format, which provides a useful and more visual way to detail the condition/weakness, potential risk and action to address the condition/weakness. To simplify this going forward, a matrix will be included in addition to the narrative. USAID, therefore, requests closure of this recommendation.

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Comment
9.

USAID's Direct Assistance in Afghanistan

A major component of the USG's approach to development assistance in Afghanistan involves supporting the Afghan government, as developmentally appropriate, so it can take increasing ownership for development and sustain the gains made over the past decade. Using local systems has been a goal of the current and previous administrations, as announced at the Paris Declaration and in Busan. It is Agency policy to build host country capacity through measured and responsible use of partner country systems that acknowledges existing vulnerabilities, employs appropriate risk mitigation approaches during implementation, and provides for capacity building measures that correct vulnerabilities both prior to and throughout implementation. USAID employs a cautious and methodical approach to the design, implementation and management of direct assistance provided to the Afghan government.

Before USAID contemplates direct assistance to any Afghan government ministry or entity, it undertakes an extensive risk assessment, known as a Public Financial Management Risk Assessment (PFMRA), to determine whether the ministry or entity has the systems and controls necessary to effectively manage US government funds. To date, 13 risk assessments have been performed by independent international public accounting firms that have been approved by USAID's Office of Inspector General. These assessments, which SIGAR summarized in its report, were performed in accordance with agency policy. After completion of the risk assessment for each ministry, USAID also performed its own internal risk review. While USAID has conducted 13 risk assessments, it is moving forward with providing direct assistance to only seven of the assessed ministries.

Once a risk assessment is complete, the Mission responds to the deficiencies identified by working with the ministry to develop a risk mitigation plan to address deficiencies, some immediately and others over time. USAID uses a multi-tier risk mitigation plan and employs various techniques to address vulnerabilities identified. Each risk mitigation plan contains five standard risk mitigation measures:

1. Separate project bank accounts with specific authorization of use with USAID monitoring and audit rights.
2. Robust concurrent audit requirements with quarterly and annual reporting to identify and address issues on an ongoing basis.
3. Substantial involvement for those projects with significant procurement actions: Review/approval of solicitations, contracts, invoices prior to disbursements.
4. Incorporation of condition precedents and/or ongoing covenants based on the results of the risk assessments and the nature of the activities included in the direct assistance programs. This is followed by a comprehensive review to determine if the identified condition precedents have been met

and ongoing covenants are being addressed. The use of the implementation letter and related annex to document and reinforce terms of agreements.

5. For reimbursement type mechanisms, monitoring, review of programmatic and financial reports along with supporting documentation prior to payment of vouchers.

The risk mitigation plan begins with the selection of a repayment mechanism suited to the capacity of a given ministry, such as using a cost reimbursement agreement. The process continues with identification of “conditions precedent” (CPs) (which are actions required to be completed prior to any disbursement of funds), includes ongoing controls and risk mitigation measures during implementation of a project, and is generally supported by concurrent technical assistance to address vulnerabilities over the long term. The line ministry never touches the money.

The Mission Director, as principal officer in country for USAID, has the authority to sign the Approval of Use of Partner Country Systems (AUPCS), as outlined in ADS 220.2a-b. No “Global team” or Washington approval, as mentioned in the SIGAR report, is required for the AUPCS. The ADS 220 waiver in no way affected the detailed financial review process, and so the insinuation in the audit report that funds are “at risk” due to lack of a Washington review is not supported by the facts.

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USAID then enters into project level agreements with each ministry receiving direct assistance. Most of USAID’s project level agreements with ministries contain conditions precedent. USAID staff verifies at the outset whether a CP has been accomplished and no disbursements through government systems can occur until after all CPs are satisfied. And, again, no funds are disbursed to line ministry systems.

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Depending upon the nature of the project, USAID then selects a “reimbursement mechanism” for determining when funds may be disbursed to a ministry: either (a) reimbursement of actual costs already incurred or (b) reimbursement after achievement of specific milestones. Under either method, no funding is disbursed until USAID formally verifies and documents that goods and services have been received, milestones have been achieved, and costs can be reimbursed. After verification, funds are disbursed into the project bank account at the Central Bank. As a result of these disbursement procedures, as of December 2013, while approximately \$1.06 billion has been committed for direct assistance, \$745 million has been obligated and approximately \$270

million has actually been disbursed.² Some activities envisioned at the time of the SIGAR field work to be performed as direct assistance will now be implemented by other means, therefore while the audit notes a commitment amount of \$1.6 billion, the current amount as noted above is \$1.06 billion.

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In addition to the safeguards put into place related to our disbursement procedures, USAID also exercises direct oversight when substantial procurements are involved by reviewing and approving solicitations and contracts between the Afghan government and its third party contractors, as well as observing the procurement technical review panels. USAID also provides extensive off-budget technical assistance to ministries receiving direct assistance. At the Ministry of Public Health and Ministry of Education has established a third party program management unit within these Ministries, which reviews and verifies all aspects of their programs as well as provides technical assistance to the Ministry. USAID tailors the work with each ministry to suit the specific development needs and to provide the appropriate risk mitigation measures for each project.

While USAID acknowledges that the majority of the weaknesses identified in the risk assessments were rated as high or critical, the risk assessments were conducted at the institutional level and thus did not take into account whether particular weaknesses applied at the project level. Risks identified as “High” or “Critical” at the macro level of the ministry may not be relevant at the project level, especially given our extensive project-level mitigation measures. For example, direct assistance to DABS relies heavily on third party technical assistance and substantial USAID ongoing monitoring oversight, which mitigates vulnerabilities. USAID is substantially involved in DABS’ procurement process through reviews and approvals of solicitations, validation of signed contracts, and third-party verification of contract progress as part of the invoice review and disbursement process.

In the report, SIGAR makes reference to 104 major risks. USAID believes it is important to make the distinction between the (i) actual vulnerability that was identified during the risk assessment and (ii) the potential of an adverse event occurring if the vulnerability is not addressed. For example, if the potential risk cited in a risk assessment relates to the “misappropriation of cash arising from the payment of salaries in cash,” as part of the risk mitigation plan for this ministry USAID will identify actions that the ministry must take to prevent this potential event from occurring. Mitigation measures could include paying all salaries through the official banking system, conducting annual payroll audits,

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² (1) In the case of direct assistance, “Committed” means the total estimated amount which USAID expects to fund for the project. “Obligated” means the amount USAID has set aside for disbursements. “Disbursed” means the amount USAID has transferred into the project account at the Central Bank.

and reconciling and monitoring payroll each month. The Mission’s Office of Financial Management, Government to Government (G2G) team performs ongoing monitoring and follow-up reviews to ensure implementation of the risk mitigation plan while simultaneously building the capacity of the ministries.

So USAID addresses risks in a variety of ways. The audit report focuses on conditions precedent as if they are the only available risk mitigation measure, incorrectly assuming that vulnerabilities can only be addressed in advance by using a single corresponding condition precedent at the program level for each condition or weakness. In practice, using conditions precedent is only one of a variety of ways that the Mission mitigates risk. Therefore, the charts included in Figure 3 of the audit report provide an inaccurate representation of the potential risks involved in the actual implementation of the programs because they focus on conditions precedent as the sole means of risk mitigation. It is imperative that the entire suite of interventions, consisting of multiple levels of mitigation techniques, is considered in evaluating overall risk to U.S. funds.

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As highlighted in SIGAR’s report, the risk mitigation plan for DABS, “is a positive development,” acknowledging that USAID has identified the weaknesses related to the DABS activity and how each of the weaknesses will be mitigated. Further, as noted in the SIGAR alert letter issued on December 31, 2013, mitigation measures applied to the DABS project to install power lines, SIGAR noted “these additional oversight provisions are reasonable.” While USAID prepared a narrative risk report as part of each of its internal risk reviews, the DABS risk mitigation plan highlighted by SIGAR presents this same information in a matrix format, which provides a useful and more visual way to articulate the condition/weakness, potential risk and relevant actions to address the condition/weakness. USAID has already developed similar risk mitigation plans for each of the six ministries to which it provides direct assistance.

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There is no way to completely eliminate risk, but we have gone to great lengths to design, implement, and refine over time a risk mitigation system that we believe provides robust protection for U.S. taxpayer funds. In one activity, for example, with the Independent Directorate for Local Government (IDLG), a USAID Inspector General-approved firm audited the program at our request and the audit identified anomalies that led us to suspend the program. USAID is in the process of verifying questioned costs from the audit.

SIGAR’s draft audit report, as noted above, presents an incomplete picture of the direct assistance program by calling-out the risks that USAID itself has identified through our ministry risk assessments, while neglecting to fully recognize USAID’s risk mitigation measures. The audit also fails to

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acknowledge how USAID controls the flow of funds from accounts we control through until disbursed directly to the implementing partners.

Communication with Congress

The Department of State and USAID have complied with statutory requirements prior to U.S. assistance funds being made available for direct government assistance in Afghanistan. In meeting those requirements, the Department of State and USAID have consulted closely with the committees of jurisdiction, providing extensive information on the risks and risk mitigation measures for direct assistance in Afghanistan. Furthermore, we appreciate the value of Congressional oversight of U.S. assistance programming in Afghanistan and support SIGAR's role in the oversight process.

State and USAID make every effort to be thorough in the Certification and Congressional Notification (CN) processes with the common understanding between the State Department and USAID and their committees of jurisdiction that the submission of these formal documents to Congress is the beginning of a consultative process with Congress. The Fiscal Year 11 and Fiscal Year 12 country CNs for Afghanistan provided a top-line summary of a variety of programs and much more detailed discussions take place once the CN is submitted. Even at a summary level, the Fiscal Year 11 country CN #7 ran to 37 pages of text and the Fiscal Year 12 country CN #10 was 42 pages.

In subsequent discussions with and briefings for congressional committees of jurisdiction on the country CNs, it is not unusual for different committees to have different areas of focus and therefore to request disparate additional information on programs during separate briefings that we offer to each committee. Staff on these Congressional committees were active participants in reviewing these formal documents and asking follow-up questions at these briefings. Questions that State and USAID briefers were unable to answer or answer fully at these briefings were taken back and addressed in follow up briefings or written responses to the respective committees or staff who posed the questions. In addition, on many occasions, congressional staff follow-up with written questions following briefings.

It is also common for committees to place holds on funding that has been notified for Afghanistan, pending the provision of additional information requested from the Administration. Accordingly, the submission of CNs for Afghanistan to Congress is the beginning of a lengthy process that can take weeks or months to reach a point where all information sought by the committees has been provided and all of the notified funding can be obligated by USAID. Directly related to the Fiscal Year 2011 Afghanistan country CN

(dated November 21, 2011) and the FY12 Afghanistan country CN (dated November 15, 2012) combined, we provided at least sixteen briefings for Congressional staff, and in addition to the numerous questions answered during the briefings, the Administration answered approximately 45 follow-up questions from Congressional staff, totaling 32 pages of questions and answers.

We note that the memorandum of justification that accompanied the Fiscal Year 2011 Certification said explicitly that the certification was not the end of our oversight process: “For each activity implemented through a direct government-to-government mechanism, USAID will develop, through project implementation letters ... specific terms and conditions applicable to each activity...”

With regard to other specific findings in the draft audit report:

- “USAID has only provided redacted copies of the Ernst & Young and KPMG public financial management assessment reports to some congressional staff.”
 - This is incorrect. When USAID provided copies of the assessments (with limited redactions) to Congressional staff, as requested, it also offered access to un-redacted copies of the assessments. USAID has briefed numerous committee staff on direct assistance, as to risks and risk mitigation measures, both in the course of CN briefings and in other settings. This procedure has been utilized in an effective manner to keep Congress informed on other programs as well.
- “Additionally, USAID officials told us they have not provided Congress with copies of their internal risk reviews of Afghan ministries’ ability to manage donors’ direct assistance funds.”
 - Congress has been provided extensive information about direct assistance in Afghanistan and has not requested access to these internal risk reviews. USAID is prepared and ready to appropriately respond to any requests from Congress for additional information on our Afghanistan direct assistance program.
- “While USAID informed Congress that the Ministry of Finance was considered qualified ‘with the necessary risk mitigation strategy in place,’ USAID did not fully disclose in the 2012 notification that it had identified 46 risks within the ministry.”
 - The CN also did not list all of the specific mitigation measures USAID took to mitigate identified risks for individual ministries, for the simple reason that State and USAID anticipated providing that

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level of detail in briefings or written responses to questions posed by the committee staff once they had reviewed the CN.

- “USAID’s notification also did not disclose that the majority of measures intended to mitigate these risks had not been implemented at the time of the notification, even though the 2012 limitation on direct assistance states that funds may be made available for direct assistance to an Afghan government ministry only if ‘any identified vulnerabilities or weaknesses of such agency or ministry have been addressed.’”
 - The Fiscal Year 2012 appropriations law stipulates that funds may be made available for direct Government-to-Government assistance only if any identified vulnerabilities and weaknesses have been addressed. The notification by itself does not make available any funds to any program. Funds are only made available as part of the implementation of a program.
 - Also, as noted above, the memorandum of justification that accompanied the Fiscal year 2011 certification made clear that there were a number of additional measures USAID would develop to ensure effective oversight of any USG funds made available under these programs.

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Comment
21.

ADS 220 Waiver

USAID has complied with the financial requirements set out in Agency policies in ADS 220 for direct assistance. Per the extensive documentation provided to SIGAR, USAID demonstrated it substantially complied with Agency policies on partner country systems in ADS 220.

USAID has made very clear it is still adhering to the core elements of the policy, with the sole exception of elements of Stage I, which is a macro-level, preliminary assessment that was for all intents and purposes already accomplished in Afghanistan. Particularly, USAID substantially complies with ADS 220 in the areas related to financial oversight. That USAID did not perform the macro-level Stage I review, including the “enhanced democracy, human rights, and governance review” would not have changed the decision to move to the Stage II assessments since the decision was made and communicated to Congress, the Afghan Government and the International Community.

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22.

The ADS 220 waiver was granted not only on foreign policy grounds, but also because, to quote the 2012 waiver, “USAID/Afghanistan has been engaged in direct G2G assistance to GIRoA for several years” (p. 3) and, “[m]ore

importantly, the Mission has complied with the spirit and purpose of the guidance” (p. 4). The ADS 220 waiver in place for Afghanistan only applies to appropriated funds made available to the Mission through Fiscal Year 2013, not Fiscal Year 2015 as stated in the audit report. As is made clear in the waiver memo for ADS 220, USAID is committed to fulfilling Agency requirements to the fullest extent possible. The risk assessments performed for USAID and summarized in this report are but one illustration of USAID’s efforts to comply with Agency regulations. The statement that funds are “at risk” because of the waiver ignores the extensive documentation that SIGAR used to make this report that was done in accordance with Agency guidance. Furthermore, the implication that USAID does not require ministries to implement mitigation measures is inconsistent with the extensive documentation provided to SIGAR demonstrating how USAID itself mitigates the risks we identified.

See SIGAR
Comment
23.

Finally, as this audit does not examine the implementation of USAID direct assistance programs, we do not believe this report has any basis on which to question whether the identified vulnerabilities have been addressed prior to funds being made available.

See SIGAR
Comment
24.

SIGAR's Response to USAID's Comments

COMMENT ONE: We disagree, as it was never the intention of our audit to identify fraud, waste, or abuse at the program level. As we explained to USAID from the beginning of this audit, our objectives were to: (1) assess the extent to which Ernst & Young and KPMG adhered to USAID contract requirements when conducting the ministry assessments; (2) describe assessment findings and conclusions about the ability of the Afghan ministries to manage U.S. funds and analyze how USAID has used, or plans to use, the assessments to inform its direct assistance to the Afghan government; and, (3) examine the U.S. Department of State's certification and USAID's notification provided to Congress, pursuant to congressional requirements for providing direct assistance to the Afghan government. In our report, we provide several examples of steps USAID has taken or plans to take to ensure that the seven ministries with a USAID risk review use the funds for their intended purposes. These include establishing conditions precedent and ongoing conditions, developing monitoring and evaluation plans, and using on-budget monitors to evaluate these programs. We also provide more general examples of steps USAID might take to ensure that direct assistance funds are used appropriately, such as building ministry capability through off-budget programs USAID directly funds and manages, providing funds on a reimbursable basis, and establishing separate bank accounts to be used solely for specific programs. SIGAR, as noted in this report, is currently conducting an audit of these additional measures that USAID and other U.S. agencies may take to safeguard on-budget funds from waste, fraud, and abuse.

COMMENT TWO: As detailed in this report, USAID did not implement the vast majority of risk mitigation measures that it and its contractors identified in the ministry assessments and the risk reviews as necessary to address the significant weaknesses within the ministries. Specifically, USAID only required the seven ministries with a USAID risk review—or less than 8 percent—of the recommended risk mitigation measures prior to receiving direct assistance funds. That is a sound basis for our conclusion and is irrelevant to the actual implementation of direct assistance programs or whether any fraud or misuse of funds has occurred. We note, however, that while this audit did not seek to uncover instances of fraud or misuse of funds, SIGAR does have an ongoing criminal investigation into alleged corruption at the Ministry of Public Health. One aspect of this investigation is focused on the ministry's Grants and Contracts Management Unit, which USAID has stated it established, in large part, to safeguard direct assistance funds.

While we stand by our conclusions, in the interest of clarity, we have modified some of the language in our report to emphasize that USAID's failure to mitigate risks relates to those measures designed to fix problems within the ministries—rather than external measures intended to protect U.S. government funds from misuse once the decision has been made to award them.

COMMENT THREE: We state clearly in our report that USAID has complied with the statutory requirement to inform Congress. However, we maintain that some of the information in the 2011 certification and 2012 notification was inaccurate, or at least, incomplete. For example, USAID did not disclose the full extent of the risks identified at each of the ministries or that over 90 percent of the mitigating measures identified in the risk reviews had not been implemented. Those are, in our view, serious omissions of fact.

COMMENT FOUR: The narrative reports that USAID/Afghanistan provided us during the course of our audit for these other ministries do not explicitly state what actions USAID is or will be taking to mitigate all of the identified risks. It is unclear if this statement is referring to those same narrative reports. If so, we note that they do not provide the same level of detail that is included in the risk mitigation matrix for Da Afghanistan Breshna Shekat. For that reason, we reiterate the importance of our third audit recommendation.

COMMENT FIVE: USAID has designated the ministry assessments and the internal risk reviews as Sensitive but Unclassified (SBU) and requested SIGAR to withhold this information and unspecified, but related portions of our audit report from public release because “release of these materials will likely result in reduced cooperation from the Afghan Government” and release “could damage our bilateral relationships with the Government of the Islamic Republic of Afghanistan.”

USAID asserts that the ministry assessments and internal risk reviews “were generated for the internal use of the US Government and the entities that are the subject of the assessments” (*i.e.*, the Afghan ministries). USAID also asserts that “parts of the Afghan government provided unprecedented access for the independent auditors to complete the risk assessments based on understandings that the results of the risk assessments would not be made public.”

Despite repeated requests from SIGAR, USAID has not provided any documentary evidence that it promised the Afghan government that this information would be withheld from the public. In any case, the fact that USAID specifically decided to designate the ministry assessments and the risk reviews as “unclassified” means that this information cannot be withheld from public release on the basis of that rationale.

The State Department’s Foreign Affairs Manual addresses this issue very clearly:

“Information obtained from or exchanged with a foreign government or international organization as to which public release would violate conditions of confidentiality or otherwise harm foreign relations *must be classified in order to be exempt from release under FOIA or other access laws. The SBU label cannot be used instead of classification to protect such information.*”⁸⁴

Notwithstanding the Foreign Affairs Manual, USAID’s comments define SBU as a designation for “information that warrants a degree of protection and administrative control and meets *legal or regulatory criteria for exemption from public disclosure*” (emphasis added). However, USAID has not articulated any basis in law or regulation that would require SIGAR to censor all or part of this report.

USAID’s mention of “legal or regulatory criteria for exemption from public disclosure” appears to be an oblique reference to the discretionary exemptions under the Freedom of Information Act, 5 U.S.C. § 552, (FOIA) that permit an agency to withhold certain information under narrowly defined circumstances. However, USAID has not explained how any part of SIGAR’s audit report might fall within any of those discretionary exemptions or explained why those exemptions should be asserted.

Moreover, there is a strong presumption in law and policy in favor of public disclosure. The main purpose of FOIA is to ensure public disclosure, not to prevent it. In addition, the SBU designation is a subcategory of “Controlled Unclassified Information” (CUI).⁸⁵ Executive Order No. 13,556 established “an open and uniform program” for managing CUI.⁸⁶ In describing the reasons for establishing this program, the order states that:

“[E]xecutive departments and agencies . . . employ ad hoc, agency-specific policies, procedures, and markings to safeguard and control this information This inefficient, confusing patchwork has resulted in inconsistent marking and safeguarding of documents, led to unclear or *unnecessarily restrictive* dissemination policies, and created impediments to authorized information sharing. *The fact that these agency-specific policies are often hidden from public view has only aggravated these issues.*”⁸⁷

⁸⁴ 12 FAM 543(f) (emphasis added). This provision applies to both USAID and the State Department. See 12 FAM 511.1(a).

⁸⁵ Presidential Memorandum for Heads of Executive Departments and Agencies Concerning Classified Information and Controlled Unclassified Information, 74 Fed. Reg. 26,277 (May 27, 2009).

⁸⁶ Exec. Order No. 13,556, 75 Fed. Reg. 68,675 (November 9, 2010).

⁸⁷ Exec. Order No. 13,556, 75 Fed. Reg. 68,675 (November 9, 2010). (emphasis added).

The Department of Justice and the National Archives and Records Administration have issued joint guidance implementing Executive Order No. 13,556, which states that “FOIA should not be cited as a safeguarding or dissemination control authority for [CUI].”⁸⁸ This is because “[t]he purpose of the FOIA is to open agency activities to the public.”⁸⁹ Similarly, the President has stated that departments and agencies should not “keep information confidential merely because public officials might be embarrassed by disclosure, because errors and failures might be revealed, or because of speculative or abstract fears.”⁹⁰

Therefore, in the absence of any basis in law or regulation articulated by USAID for withholding this information from public scrutiny, SIGAR will publish this audit report in full.

COMMENT SIX: USAID’s statement that the conclusions of the internal risk reviews and their specific details “are not relevant to the findings of this audit” is puzzling. As stated clearly throughout our report, our second audit objective was, in part, to “describe the assessment findings and conclusions about the ability of the Afghan ministries to manage U.S. funds.”

COMMENT SEVEN: We disagree with USAID’s assertion that it is already complying with this recommendation. As we noted in our report, USAID headquarters officials from the Global Partner Country Systems Risk Management Team told us they did not perform quality control reviews of the contracted public financial management assessments, USAID/Afghanistan’s risk reviews, or any risk mitigation strategies, as required by ADS 220. To date, USAID has not provided any evidence that these quality control reviews occurred.

COMMENT EIGHT: We disagree with USAID’s assertion that it is already complying with this recommendation. During our fieldwork, USAID officials based in Afghanistan told us they had not provided Congress with copies of or access to the Stage 2 risk reviews. Moreover, when we met with officials from USAID’s Office of Afghanistan and Pakistan Affairs, based in Washington, they appeared unaware of these reviews and told us they had not seen them.

Finally, as noted in our report, some of the information in the 2011 certification and 2012 notification was inaccurate, or at least, incomplete. For example, they did not disclose the full extent of the risks identified at each of the ministries or that over 90 percent of the mitigating measures identified in the risk reviews had not been implemented prior to disbursing funds.

COMMENT NINE: We have not yet obtained evidence that USAID has already prepared similar plans for the six ministries receiving USAID direct assistance. The narrative reports that USAID/Afghanistan provided us during the course of our audit do not explicitly state what actions USAID is currently, or will be taking in the near future, to mitigate all of the identified risks. If the plans referenced in this comment are new documents developed after our fieldwork, we request that USAID provide us copies of them so that we can assess them and determine whether closure of this recommendation is appropriate.

⁸⁸ Memorandum from John P. Fitzpatrick, Director, Controlled Unclassified Information Office, National Archives and Records Administration, and Melanie Ann Pustay, Director, Office of Information Policy, U.S. Department of Justice, to Senior Agency Officials for Executive Order No. 13556, “Controlled Unclassified Information” (November 22, 2011).

⁸⁹ Memorandum from John P. Fitzpatrick, Director, Controlled Unclassified Information Office, National Archives and Records Administration, and Melanie Ann Pustay, Director, Office of Information Policy, U.S. Department of Justice, to Senior Agency Officials for Executive Order No. 13556, “Controlled Unclassified Information” (November 22, 2011).

⁹⁰ Presidential Memorandum for Heads of Executive Departments and Agencies Concerning the Freedom of Information Act, 74 Fed. Reg. 4,683 (Jan. 21, 2009).

COMMENT TEN: The statement that “No ‘Global team’ or Washington approval, as mentioned in the SIGAR report, is required for the AUPCS” is incorrect. Automated Directive System (ADS) 220, as revised on March 26, 2012, states, “The Agency has established a set of conditions that would, if complied with, constitute formal approval for the use of a partner country [public financial management] system. These conditions are known collectively as the Accountability Framework and include...completion of due diligence on the partner country systems targeted for use by the [Partner Country Systems] Team, and review and quality control of the due diligence by the [Global Partner Country Systems Risk Management Team].”

COMMENT ELEVEN: The statement that “the ADS 220 waiver in no way affected the detailed financial review process” is also incorrect. As we note in our report, USAID officials from the Global Partner Country Systems Risk Management Team, based in Washington, told us they did not perform quality control reviews of the contracted public financial management assessments, USAID/Afghanistan’s risk reviews, or any risk mitigation strategies, as required by ADS 220.

COMMENT TWELVE: We acknowledge in our report that USAID created conditions precedent for direct assistance programs for the five ministries that would have been subject to ADS 220 requirements had the agency not waived them for Afghanistan. We also explain that USAID certified each of these ministries as having met the conditions precedent prior to disbursing funds. However, it is important to note, as detailed in our report, that USAID only set as conditions precedent 24—or less than 8 percent—of the risk mitigation measures identified in the risk reviews. Moreover, while prohibiting funds from being disbursed to line ministry systems is one measure to safeguard funds from misuse, it is an external measure that does not address the underlying weaknesses within the ministries.

COMMENT THIRTEEN: We have added language in our report to note that the amount of \$1.6 billion was current, as of August 2013, and we have also added a footnote to reflect USAID’s updated direct assistance commitment.

COMMENT FOURTEEN: Although we recognize the distinction between the risks, we believe it is important to mention all of the risks USAID identified within the ministries, especially those that could potentially be exploited, resulting in an adverse event of significance. This is especially true in a country like Afghanistan, which suffers from pervasive corruption.

COMMENT FIFTEEN: The purpose of figure 3 is to illustrate the percentage of mitigation measures that (1) were included as conditions precedent in the program implementation letters for the five ministries identified, (2) were not included as conditions precedent, and (3) might have been included as conditions precedent but the conditions precedent were vague. The analysis supporting the figure is accurate and methodologically sound. We acknowledge that USAID takes other steps to ensure that direct assistance funds provided to the Afghan government are used for their intended purposes and we detail many of those steps in our report. However, we have focused on conditions precedent and ongoing conditions because these are the only steps required to address risks within the ministries receiving direct assistance funds. Moreover, the additional measures that USAID uses to safeguard funds from misuse do not directly address the underlying problems within the ministries that limit their ability to manage donor funds.

COMMENT SIXTEEN: See comment 9.

COMMENT SEVENTEEN: See comment 1.

COMMENT EIGHTEEN: When we asked USAID/Afghanistan and USAID headquarters officials in August 2013 if they had shared copies of the Ernst & Young and KPMG public financial management assessments with the Congress, they told us they had only provided redacted copies to some congressional staff. Based on the new information provided in USAID's comments, we have deleted this sentence from the text of our final report.

COMMENT NINETEEN: We note that USAID did not disagree with our statement that the agency did not provide copies of its Stage 2 risk reviews to Congress. We also question whether congressional staff were aware of the existence of the Stage 2 risk reviews. Notably, officials in USAID's Office of Afghanistan and Pakistan Affairs, based in Washington, appeared unaware of these reviews when we asked about them in August 2013, and stated that they had not seen them.

COMMENT TWENTY: The significance of our point regarding the Ministry of Finance is that, while USAID informed Congress that the ministry was considered qualified "with the risk mitigating measures in place," it did not disclose that it had also identified 46 risks within the ministry and had not required the ministry to address most of these risks prior to giving the ministry direct assistance funds. We believe that is important information that, if shared, would have strengthened Congress's oversight of USAID's direct assistance program.

COMMENT TWENTY-ONE: We agree with these statements of fact; however, they do not contradict any of the information provided in our report.

COMMENT TWENTY-TWO: We acknowledge in our report that USAID substantially complied with ADS 220, except for Stage 1, despite the Administrator's waiver of its requirements; however, the agency has not fully complied with the remaining stages of ADS 220, specifically the requirement for the Global Partner Country Systems Risk Management Team to perform quality control reviews throughout the process.

COMMENT TWENTY-THREE: We state in our report that "the USAID Administrator waived all ADS 220 requirements for all agency funds made available to USAID/Afghanistan through fiscal year 2013 appropriations." Our understanding, based on interviews with USAID officials, is that the agency would not obligate or disburse funds appropriated in fiscal year 2013 until fiscal year 2015 at the earliest. We have updated the report to clarify this point. In addition, as noted in comment 1, we describe examples of actions USAID takes to ensure that direct assistance funds are used for their intended purposes. Finally, as clearly laid out in our report, we reviewed and analyzed a variety of USAID documentation to develop and support our findings.

COMMENT TWENTY-FOUR: See comment 2.

APPENDIX XVII - ACKNOWLEDGMENTS

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The mission of the Special Inspector General for Afghanistan Reconstruction (SIGAR) is to enhance oversight of programs for the reconstruction of Afghanistan by conducting independent and objective audits, inspections, and investigations on the use of taxpayer dollars and related funds. SIGAR works to provide accurate and balanced information, evaluations, analysis, and recommendations to help the U.S. Congress, U.S. agencies, and other decision-makers to make informed oversight, policy, and funding decisions to:

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