SIGAR

Special Inspector General for Afghanistan Reconstruction

SIGAR 15-61 Financial Audit

USAID's Increased Electoral Participation in Afghanistan Program: Audit of Costs Incurred by the Consortium for Elections and Political Process Strengthening

JUNE 2015

SIGAR 15-61-FA/IEPA

SIGAR

Special Inspector General for Afghanistan Reconstruction

WHAT THE AUDIT REVIEWED

On September 28, 2008, the U.S. Agency for International Development (USAID) signed a cooperative agreement, with an initial cost of $40 million, with the Consortium for Elections and Political Process Strengthening (CEPPS) to support the Increased Electoral Participation in Afghanistan program. The primary goals of the program were to (1) strengthen the ability of candidates and the electorates to articulate, organize, and compete in the upcoming elections, and (2) to increase public awareness and oversight of the electoral process. The program was expected to increase effective and informed participation in the 2009 and 2012 elections, as well as provide support to ensure transparency and broad-based participation in the electoral process.

SIGAR's financial audit, performed by Davis and Associates Certified Public Accountants, PLLC (Davis), reviewed $10,040,492 in expenditures charged to the agreement from October 1, 2012, to September 30, 2013. The objectives of the audit were to (1) identify and report on significant deficiencies or material weaknesses in CEPPS's internal controls related to the cooperative agreement; (2) identify and report on instances of material noncompliance with the terms of the cooperative agreement and applicable laws and regulations, including any potential fraud or abuse; (3) determine and report on whether CEPPS has taken corrective action on prior findings and recommendations; and (4) express an opinion on the fair presentation of CEPPS's Special Purpose Financial Statement. See Davis's report for the precise audit objectives.

In contracting with an independent audit firm and drawing from the results of the audit, SIGAR is required by auditing standards to review the audit work performed. Accordingly, we oversaw the audit and reviewed its results. Our review disclosed no instances where Davis did not comply, in all material respects, with U.S. generally accepted government auditing standards.

June 2015

USAID's Increased Electoral Participation in Afghanistan Program: Audit of Costs Incurred by the Consortium for Elections and Political Process Strengthening

SIGAR 15-61-FA

WHAT THE AUDIT FOUND

Davis and Associates Certified Public Accountants, PLLC (Davis) identified two material weaknesses and two significant deficiencies in the Consortium for Elections and Political Process Strengthening's (CEPPS) internal controls, and three instances of material noncompliance with the terms and conditions of the cooperative agreement. Specifically, CEPPS was not able to provide adequate support for a competitive procurement process for $894,126 in subcontracts. As a result, CEPPS could not prove that these costs were reasonable, and the U.S. government may not have received the most competitive price. In addition, CEPPS could not provide supporting documentation to comply with applicable terms and conditions of the cooperative agreement for certain expenses, such as travel, currency exchanges, or local tax payment obligations, which resulted $175,467 in ineligible costs.

As result of these internal control deficiencies and instances of noncompliance, Davis identified $1,070,576 in total questioned costs, consisting of $895,109 in unsupported costs—costs not supported with adequate documentation or that did not have required prior approval—and $175,467 in ineligible costs—costs prohibited by the agreement, applicable laws, or regulations.

Category	Ineligible	Unsupported	Total Questioned Costs
Personnel and Wages	$0	$983	$983
Travel	$31,272	$0	$31,272
Contractual	$0	$894,126	$894,126
Other Direct Costs	$144,195	$0	$144,195
Totals	**$175,467**	**$895,109**	**$1,070,576**

Davis obtained and reviewed prior audit reports and other assessments that could have a material impact on the Special Purpose Financial Statement. Davis identified two prior audit findings pertaining to an improper vetting process for contracts and a lack of proper controls over document retention. After reviewing and assessing documentation, Davis determined that CEPPS properly addressed the two audit findings, and no further action was required.

Davis issued a modified opinion on the Special Purpose Financial Statement due to a lack of adequate supporting documentation related to subcontracts, travel, and other direct costs, resulting in $1,070,576 in questioned costs.

WHAT SIGAR RECOMMENDS

Based on the results of the audit, SIGAR recommends that the USAID Agreement Officer:

1. **Determine the allowability of and recover, as appropriate, $1,070,576 in questioned costs identified in the report.**
2. **Advise CEPPS to address the report's four internal control findings.**
3. **Advise CEPPS to address the report's three noncompliance findings.**

June 1, 2015

The Honorable Alfonso E. Lenhardt
Acting Administrator
U.S. Agency for International Development

Mr. William Hammink
USAID Mission Director for Afghanistan

We contracted with Davis and Associates Certified Public Accountants, PLLC (Davis) to audit the costs incurred by the Consortium for Elections and Political Process Strengthening (CEPPS) under a U.S. Agency for International Development (USAID) cooperative agreement to support the Increased Electoral Participation in Afghanistan program.[1] Davis's audit covered $10,040,492 in expenditures charged to the cooperative agreement from October 1, 2012, through September 30, 2013. Our contract required that the audit be performed in accordance with generally accepted government auditing standards issued by the Comptroller General of the United States.

Based on the results of audit, SIGAR recommends that the USAID Agreement Officer:

1. **Determine the allowability of and recover, as appropriate, $1,070,576 in questioned costs identified in the report.**
2. **Advise CEPPS to address the report's four internal control findings.**
3. **Advise CEPPS to address the report's three noncompliance findings.**

The results of the Davis audit are detailed in the attached report. We reviewed Davis's report and related documentation. Our review, as differentiated from an audit in accordance with U.S. generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on CEPPS's Special Purpose Financial Statement. We also express no opinion on the effectiveness of CEPPS's internal control or compliance with the cooperative agreement, laws, and regulations. Davis is responsible for the attached auditor's report and the conclusions expressed in the report. However, our review disclosed no instances where Davis did not comply, in all material respects, with generally accepted government auditing standards issued by the Comptroller General of the United States.

We will be following up with USAID to obtain information on the corrective actions taken in response to our recommendations.

John F. Sopko
Special Inspector General
for Afghanistan Reconstruction

(F-045)

[1] USAID awarded cooperative agreement number 306-A-00-08-00529-00 to CEPPS to support the Increased Electoral Participation in Afghanistan program, which was intended to support broad citizen participation in the 2009 and 2012 elections.

DAVIS AND ASSOCIATES CERTIFIED PUBLIC ACCOUNTANTS, PLLC

FINANCIAL AUDIT

OF

COSTS INCURRED BY THE CONSORTIUM FOR ELECTIONS AND POLITICAL PROCESS STRENGTHENING UNDER THE COOPERATIVE AGREEMENT 306-A-00-08-00529-00 TO SUPPORT THE INCREASED ELECTORAL PARTICIPATION IN AFGHANISTAN PROGRAM FOR THE PERIOD OCTOBER 1, 2012, THROUGH SEPTEMBER 30, 2013

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April 30, 2015

TRANSMITTAL LETTER

To: Mr. Charles Botwright
Office of Special Inspector General for Afghanistan Reconstruction

From: Davis and Associates Certified Public Accountants, PLLC

Subject: Financial Audit of Costs Incurred by the Consortium for Elections and Political Process Strengthening (CEPPS) under the Cooperative Agreement 306-A-00-08-00529-00 to support the Increased Electoral Participation in Afghanistan program for the period October 1, 2012 to September 30, 2013

This letter transmits the final audit report of the subject effort. We issued a modified opinion on the fairness of the presentation of the Special Purpose Financial Statement. Our audit disclosed $1,070,576 of questioned costs that were required to be questioned in the Special Purpose Financial Statement. Our audit detected three instances of material non-compliance and four significant deficiencies in Internal Control; we consider two of these to be material weaknesses.

Davis & Associates

Davis and Associates Certified Public Accountants, PLLC

211 North Union Street

Suite 100

Alexandria, Virginia 22314

EXECUTIVE SUMMARY

Background

The U.S. Agency for International Development - (USAID/Afghanistan) signed a cooperative agreement on September 28, 2008 with the Consortium for Elections and Political Process Strengthening (CEPPS) to support the Increased Electoral Participation in Afghanistan program. The primary goals of the program were to strengthen the ability of political stakeholders to articulate, organize and compete in the upcoming elections and increase public awareness and oversight of the electoral process. The program was a component of USAID/Afghanistan's Strategic Objective 02 – A democratic government with broad citizen participation. The program was expected to include buy-in from relevant stakeholders and partners to increase effective and informed participation in the planned 2009/2012 elections as well as to provide support to ensure transparency and broad-based participation in the electoral process itself.

The Cooperative Agreement 306-A-00-08-00529-00, incorporated at an initial estimated cost of $40 million for the period of performance of September 28, 2008 through September 28, 2011, funded the Consortium for Elections and Political Process Strengthening. After 23 modifications, the project's period of performance was extended to September 30, 2013 and the total cost was increased to $91.5 million.

The costs incurred through September 30, 2012 were previously audited. Our audit covers the period of performance from October 1, 2012, to September 30, 2013, where CEPPS incurred costs totaling $10,040,492.

CEPPS is a legal joint venture of three separate organizations, the International Foundation for Electoral Systems (IFES), the International Republican Institute (IRI) and the National Democratic Institute (NDI). IFES, IRI and NDI are all private non-profit organizations. While CEPPS is the prime recipient of the cooperative agreements, it issues sub awards to each member of the joint venture who each maintain their own financial, personnel and HR policies and are individually responsible for implementing their respective components of the program.

Work Performed

Davis and Associates Certified Public Accountants, PLLC was engaged by the Office of Special Inspector General for Afghanistan Reconstruction (SIGAR) to conduct a financial audit of the CEPPS project.

Methodology - Procedures Performed

Below are the documents that were used for the performance of this audit:

- The Cooperative Agreement 306-A-00-08-00529-00 between the USAID/Afghanistan and CEPPS.
- Contracts and subcontracts with third parties.
- The written procedures approved by USAID/Afghanistan.
- USAID Office of Inspector General, *Guidelines for Financial Audits Contracted by Foreign Recipients (Guidelines)* dated February 2009.
- ADS Chapter 591 - *Financial Audits of USAID Contractors, Recipients, and Host Government Entities.*

- Mandatory Standard Provisions for U.S. Nongovernmental Grantees (USAID Automated Directives System, Chapter 303 Internal Mandatory References).
- All policies and procedures.

Our audit approach was significance and risk-based. Significance is the relative importance of a matter within the context it is being considered, including qualitative and quantitative factors.

Special Purpose Financial Statement

We examined CEPPS' Special Purpose Financial Statements by budgeted line item under the agreement, including the budgeted amounts by category and major items. We reviewed OMB Circular A-122 to ensure that all costs incurred in Afghanistan and the U.S. under the USAID-funded agreement were allocable, reasonable, properly supported, allowable and properly included by CEPPS in the Special Purpose Financial Statements by category and major item.

Internal Controls

Through inspection of documents, inquiry of personnel and observation of procedures, we obtained a sufficient understanding of CEPPS and its environment, including its internal control, to assess the risk of material misstatement of the books and records of CEPPS, whether due to error or fraud, and to design the nature, timing, and extent of further audit procedures.

Compliance with Laws and Regulations

We identified the significant provisions of laws and regulations to design relevant compliance-related procedures for the audit. We looked at those provisions (a) for which compliance could be objectively determined and (b) that had a direct and material effect on the Activity. Our audit included steps to allow us to detect all material instances of noncompliance, defined as instances that could have a direct and material effect on the Special Purpose Financial Statements.

Follow Up to Prior Audit Recommendations

We inquired of management as to whether or not any prior audit or compliance reviews had been performed with respect to the project under audit.

Objectives Defined by SIGAR

The following audit objectives were defined within the Performance Work Statement for Financial Audits of Costs Incurred by CEPPS funded by the U.S. Government for Reconstruction Activities in Afghanistan:

Audit Objective 1 – Special Purpose Financial Statement

Express an opinion on whether CEPPS' Special Purpose Financial Statement for the award presents fairly, in all material respects, revenues received, costs incurred, items directly procured by the U.S. Government and balance for the period audited in conformity with the terms of the award and generally accepted accounting principles or other comprehensive basis of accounting.

Audit Objective 2 - *Internal Controls*

Evaluate and obtain a sufficient understanding of the audited entity's internal control related to the award; assess control risk; and identify and report on significant deficiencies including material internal control weaknesses.

Audit Objective 3 – *Compliance*

Perform tests to determine whether the audited entity complied, in all material respects, with the award requirements and applicable laws and regulations; and identify and report on instances of material noncompliance with terms of the award and applicable laws and regulations, including potential fraud or abuse that may have occurred.

Audit Objective 4 – *Corrective Action on Prior Findings and Recommendations*

Determine and report on whether the audited entity has taken adequate corrective action to address findings and recommendations from previous engagements that could have a material effect on the special purpose financial statement.

Scope

In the performance of the audit, we applied audit procedures to IFES, IRI and NDI. In our discussion, when describing audit procedures utilized, we refer to CEPPS as they are the Auditee. However, these procedures were applied to all three entities.

We conducted our audit from October 22, 2014 through January 11, 2015. The audit covered Cooperative Agreement 306-A-00-08-00529-00. The Recipient was CEPPS. The period covered under this audit was October 1, 2012 through September 30, 2013. The total amount of unburdened direct costs for the period under audit was $10,040,492; we selected $3,996,484 of that population for substantive testing. Our testing of indirect costs was limited to applying the rates to verify the indirect costs using the negotiated indirect cost rate agreements (“NICRA”) or provisional rate, as applicable for the given fiscal year, as approved by USAID/Afghanistan.

Summary of Audit Results

Special Purpose Financial Statements

We issued a modified opinion on the fairness of the presentation of the Special Purpose Financial Statement. [See *Independent Auditor's Report on the Special Purpose Financial Statements*, Page 18]

We determined that there was an adequate accounting system in place to properly account for and classify costs incurred; however, CEPPS did not properly exclude some unallowable costs. Our audit disclosed $1,070,576 of costs that were required to be questioned in the Special Purpose Financial Statement. [See *Detailed Audit Findings*, Page 26]

Table 1 - *Summary of Findings and Questioned Costs*

Finding Number	Audit Areas	Matter	Questioned Costs Description	Total Amount Questioned
IFES 1	Non-Compliance	Competitive bid process not applied on selection of subcontractors	Unsupported	$894,126
IFES 2	Internal Control	Incorrect Exchange rates applied on conversion of US Dollars to local currency	Ineligible	$29,550
IRI 1	Non-Compliance	Local Tax Law Provision and Incurring Additional Costs in Tax Payments	Ineligible	$112,199
IRI 2	Internal Control	Salary withholding taxes not recorded in the accounting system	N/A	**$0**
IRI 3	Internal Control	Employee payment not support by adequate documentation	Unsupported	$983
NDI 1	Non-Compliance	Business Class Airfare purchased without acceptable justifications	Ineligible	$31,272
NDI 2	Internal Control	Incorrect allocation rate applied to certain field office costs	Ineligible	$2,446
			Total Questioned Costs	**$1,070,576**

Internal Controls

Our audit detected four significant deficiencies in Internal Control that we consider two of these to be material weaknesses. [See *Independent Auditor's Report on Internal Control*, Page 20]

Compliance with Laws and Regulations

Our audit detected three instances of material non-compliance that are required to be reported. [See *Independent Auditor's Report on Compliance*, Page 22]

Follow Up to Prior Audit Recommendations

Our audit determined that CEPPS had properly addressed two prior audit findings. [See *Status of Prior Audit Findings*, Page 24]

Management Response to Findings

We presented our findings to CEPPS and requested a management response. CEPPS provided written responses, which included additional documentation. We reviewed the written responses and examined the additional documentation.

The management comments are included in Appendix A; our responses to these comments are included in Appendix B.

Exhibit I
The Consortium for Elections and Political Process Strengthening
Consolidated Special Purpose Financial Statement
October 1, 2012 through September 30, 2013

			Questioned Costs				
		Actual for the Period		**Unsupported Costs**		**Ineligible Costs**	**Notes**
Revenue	$	11,708,228	$	-	$	-	3
Total Revenue	$	11,708,228	$	-	$	-	
Costs Incurred							
Personnel and Fringe	$	2,169,709	$	983	$	-	3,A
Travel	$	1,082,920	$	-	$	31,272	3,B
Equipment and Supplies	$	148,199	$	-	$	-	3
Contractual	$	4,489,986	$	894,126	$	-	3, F
Other Direct Costs	$	2,149,678	$	-	$	144,195	3,C,D,E
Indirect Costs	$	1,667,736	$	-	$	-	3
Total Program Amount	$	11,708,228	$	895,109	$	175,467	
Outstanding Fund Balance	$	-					4

(The accompanying notes to the Special Purpose Financial Statement are an integral part of this Statement prepared by CEPPS entities)

Exhibit II
The Consortium for Elections and Political Process Strengthening
Consolidating Special Purpose Financial Statement
October 1, 2012 through September 30, 2013

Revenue	Actual for the Period	Questioned Costs: Unsupported Costs	Questioned Costs: Ineligible Costs	Notes
IFES	$ 3,814,392	$ -	$ -	
IRI	3,609,119	-	-	
NDI	4,284,716	-	-	
Total Revenue	$ 11,708,228	$ -	$ -	
Personnel and Fringe Benefits				
IFES	$ 1,257,366	$ -	$ -	
IRI	282,159	983	-	A
NDI	630,184	-	-	
Travel				
IFES	130,476	-	-	
IRI	158,057	-	-	
NDI	794,387	-	31,272	B
Equipment and Supplies				
IFES	31,440	-	-	
IRI	20,887	-	-	
NDI	95,872	-	-	
Contractual				
IFES	822,665	894,126	-	F
IRI	2,398,076	-	-	
NDI	1,269,245	-	-	
Other Direct Costs				
IFES	938,472	-	29,550	D
IRI	472,116	-	112,199	C
NDI	739,090	-	2,446	E
Total Indirect Costs				
IFES	633,973	-	-	
IRI	277,825	-	-	
NDI	755,938	-	-	
Total Program Amount	$ 11,708,228	$ 895,109	$ 175,467	

(The accompanying notes to the Special Purpose Financial Statement are an integral part of this Statement prepared by CEPPS entities)

Notes to the Special Purpose Financial Statement [1]

Note 1 - Status and Operation

NDI

The National Democratic Institute for International Affairs (NDI) is a nonprofit, nonpartisan, nongovernmental organization that has supported democratic institutions and practices in every region of the world for more than three decades. Since its founding in 1983, NDI and its local partners have worked to establish and strengthen political and civic organizations, safeguard elections, and promote citizen participation, openness and accountability in government. NDI's headquarters is located in Washington, D. C.

IRI

The International Republican Institute (IRI) was formed in April 1983 in the District of Columbia as a nonprofit corporation. IRI headquarters is in District of Columbia located at 1225 Eye Street, NW. IRI is governed by its Board of Directors and is completely independent of the U.S. government. IRI advances freedom and democracy worldwide by developing political parties, civic institutions, open elections, good governance and the rule of law.

IFES

International Foundation for Electoral Systems (IFES) was established in 1987 as a non-profit corporation in District of Columbia. IFES supports the building of democratic societies around the world and provides technical assistance in the areas of election administration, civil society development, good governance and the rule of law. IFES maintains field offices in many countries where its programs are operated. IFES' Headquarters is at 1850 K Street, NW Fifth Floor, Washington, D.C. 20006.

[1] Prepared by CEPPS Management

Note 2 - Summary of Significant Accounting Policies

Basis of Presentation

The accompanying Special Purpose Financial Statement includes costs incurred by IFES, IRI and NDI under Cooperative Agreement 306-A-00-08-00529-00 ("The Agreement") to support Increased Electoral Participation in Afghanistan with the Consortium for Elections and Political Process Strengthening for the period October 1, 2012 to September 30, 2013. Because the Statement presents only a selected portion of the operations of IFES, IRI and NDI, it is not intended to and does not present the Balance Sheets, Statements of Net Income, or Cash Flows of IFES, IRI and NDI. The information in this Special Purpose Financial Statement is presented in accordance with the requirements specified by the Office of the Special Inspector General for Afghanistan Reconstruction and is specific to Cooperative Agreement 306-A-00-08-00529-00. Therefore, some amounts presented in this Special Purpose Financial Statement may differ from amounts presented in, or used in the preparation of IFES, IRI and NDI's Statements of Financial Position, Statements of Activities, or Statements of Cash Flows.

Basis of Accounting

NDI

The Special Purpose Financial Statement has been prepared on the accrual basis of accounting whereby expenses are recognized when incurred.

IRI

Grant revenue is recognized as qualified costs under the grant awards are incurred.

IFES

Revenues are recognized when earned. Payments from USAID are based on drawdowns from a Federal Letter of Credit.

Foreign Currency Conversion Method

The operational currencies in Afghanistan are the Afghani and U.S. Dollar. Presentation currency is the U.S. Dollar. Currency translations have been done on the following basis.

- U.S. Dollar Expenditures – recorded in U.S. Dollars.
- Afghani Expenditures – converted to U.S. Dollars using the monthly weighted average exchange rate of actual currency conversions during each period. The monthly weighted average exchange rates for the period under audit ranged from 51.72 to 56.18 Afghani to one U.S. Dollar.
- Average exchange rate for the period under audit:
    - U.S. Dollar = 53.78 Afghani

IRI Note: IRI did have local expenditures under the award. The majority of the local expenditures were paid with US Dollars; however, there were some expenditures paid in Afghani currency.

Note 3 – Major Cost Categories

Below are the major categories of costs expended under the cooperative agreement that are included within the budget lines on the Special Purpose Financial Statement.

Personnel and Benefits

NDI

Personnel includes salary costs charged as direct costs for U.S. Nationals (USNs) and Third Country Nationals (TCNs) for hours attributed directly to the Agreement. The proportional amount of fringe benefits based on actual salaries charged is also included in this category.

IRI

IRI maintains an electronic timesheet system in order to ensure compliance with the OMB 122 requirements and to enable IRI to accurately compensate and charge staff time. IRI charges personnel costs based on the actual time devoted to the program (level of effort) as evidenced by time sheets certified by employees and approved by his/her supervisor.

IRI's provisional fringe benefit rate is negotiated with IRI's cognizant federal agency, the U.S. Agency for International Development. The actual audited fringe benefit rate for FY13 is 47.17% of total salaries for U.S. staff.

IFES

Personnel costs include: Salaries and Direct Benefits for US Nationals and Third Country Nationals, as well as Wages and Benefits to Cooperating Country Nationals.

Fringe Benefits are benefits paid to or on behalf of IFES' employees and include health, dental, short and long-term disability, life insurance, federal holidays, sick and annual leave, and payroll taxes.

Travel

NDI

The Travel category includes all costs of travel to, from, and within Afghanistan for airfare, local transportation, meals and incidentals, lodging, and other related travel costs incurred directly for the Agreement purposes.

IRI

International airfare, per diem and incidental expenses such as the cost of visas, immunizations, shipping, surplus baggage, etc. for trips to and from Afghanistan for employees, international trainers and consultants were incurred. Costs also included ground transportation and in-country airfare for local staff, participants and those traveling throughout Afghanistan to conduct and monitor program activities and subcontractors.

IFES

Travel Costs include International and Domestic Airfare, Local Transportation, Per Diem, and other travel costs such as Visa Fees, Excess Baggage Costs, and SOS coverage.

Equipment and Supplies

NDI

Equipment and Supplies includes office supplies, computing devices, equipment rental, repairs and maintenance, as well as any other equipment necessary for sustainable operations in Afghanistan.

IRI

Office supplies, such as paper, folders and file organizers were purchased for the program, and include photocopying costs in Washington. The costs may also cover computers and accessories such as a monitor and docking station, keyboard, mouse, and Skype headphones.

IFES

This category includes Non-Capital Furniture and Equipment.

Contractual

NDI

The Contractual category includes all costs associated with national staff salaries and benefits, as well as contracts for activities such as security, printing and translation. This cost category also includes consultant fees for both international and locally hired experts.

IRI

Contractual services include audit, legal and security services necessary for the successful completion of the program. IRI also hired local Afghan nationals to fulfill duties in the field office under the supervision of the Resident Country Director and other expats based in Afghanistan. The cost of local staff also included pension provision, severance, medical allowance and education allowance. Other contractual obligations under this award included contracts local and international organizations to fulfill requirements for focus groups, media work and election and civic education activities per the scope of the program.

IFES

Contractual costs include the following major categories:

Commodities – items procured for the direct benefit of the host country agency being supported and may include equipment, the printing of ballots, bulk supplies, etc.

Sub-recipients – costs incurred by local partner organizations who were engaged to perform specific objectives under the program.

Consultants - individuals under contract to provide specific services related to a project or contract. Examples include IT consultants and voter education consultants.

Other Direct Costs

NDI

Other Direct Costs include allowances and housing for international staff, rent and utilities for field offices, telecommunications, sub-grantee expenses, workshop/conference expenses, as well as other direct costs necessary for the implementation of the Agreement.

IRI

Costs incurred include telephone and internet capabilities for the Washington and Kabul-based staffs, as well as costs associated with postage and delivery of materials to and from the Kabul office. Training costs, space and utilities costs for housing of expatriates and office space for IRI's Afghanistan operations and insurance required for the safety of IRI expat and local staffs were also incurred for this project.

Indirect Costs

NDI

Indirect Costs include general and administrative indirect costs allocated in accordance with the Negotiated Indirect Cost Rate Agreements (NICRA) for NDI and CEPPS.

IRI

Indirect costs for each project are calculated based on a fixed percentage rate negotiated with IRI's cognizant federal agency, the U.S. Agency for International Development, (22.28% for FY13), which is applied to modified total direct costs, consisting of all salaries and wages, fringe benefits, materials and supplies, contracted services, occupancy, travel, and subgrants and subcontracts up to the first $25,000 (regardless of the period covered by the subgrant or subcontract). Equipment of more than $5,000 per unit, donated services, in-kind contributions, and that portion of each subgrant and subcontract in excess of $25,000 will be excluded from the base.

CEPPS Indirect Costs – Effective with the NICRA dated October 1, 2009, CEPPS' current provisional indirect cost rate is 0.51% of total direct costs applied to all CEPPS Associate Awards. Total direct costs are defined as total costs incurred by the CEPPS Partners, including each partner's indirect costs based on each partner's approved indirect cost rates. The CEPPS NICRA rate is negotiated with CEPPS' cognizant federal audit agency, the United States Agency for International Development (USAID).

Indirect Costs include general and administrative indirect costs allocated in accordance with the Negotiated Indirect Cost Rate Agreements (NICRA) for NDI and CEPPS.

Note 4 – Reconciliation

The fund balance represents the difference between costs incurred, including applicable indirect cost burdens and cooperative agreement funding.

Revenue – period under audit	$	11,708,228
Costs – period under audit	$	11,708,228
Variance	$	-
Total Agreement Funding	$	91,510,215
Billed through September 30, 2013	$	88,881,587
Remaining Unbilled Cost	$	-
Funds Available	$	2,628,628

Note 5 – Subsequent Events

The actual costs incurred for October 1, 2012 to September 30, 2013 in the accompanying special purpose financial statements reflects NDI expenses under the cooperative agreement for the fiscal year ending September 30, 2013, as reported on the Schedule of Expenses for Federal Awards in the finalized A-133 audit report for the same period.

Subsequent to the period covered in the audit of the accompanying special purpose financial statements, NDI reported an additional $27,380 of costs under this cooperative agreement, inclusive of the allocation of $152 for CEPPS provisional indirect. The costs reported by NDI were primarily close-out costs incurred within the 90-day close-out period of October 1 to December 31, 2013. CEPPS had notified USAID in advance of NDI incurring the costs.

Notes to the Questioned Costs Presented on the Special Purpose Financial Statement[2]

Note A – Personnel and Fringe Benefits – Unsupported Costs

Unsupported costs are those costs for which sufficient supporting documentation is not available.

Finding IRI 3 – Education and Health Allowance – questioned $983. IRI did not properly verify the salary rate in the payroll sheet with the rates established in the employee's contract for this particular employee. [*Please refer to detailed Finding IRI 3 on page 35*]

Note B – Travel – Ineligible Costs

Ineligible costs are explicitly questioned because they are unreasonable; prohibited by the audited agreement or applicable laws and regulations; or not award related.

Finding NDI 1 – First and Business Class Airfares – questioned $31,272. NDI believed their justification for the traveler's need to work immediately upon arrival is in accordance with NDI travel policy and the use of anything other than economy class airfare is allowable. [*Please refer to detailed Finding NDI 1 on page 36*]

Note C – Other Direct Costs – Ineligible Costs

Ineligible costs are explicitly questioned because they are unreasonable; prohibited by the audited agreement or applicable laws and regulations; or not award related.

Finding IRI 1 – Withholding Tax Payment – questioned $112,199. The taxes were not withheld from payments to its local vendors and local employees. IRI believed they were obliged to make the tax payments to settle an outstanding amount owed to the Afghan government. [*Please refer to detailed Finding IRI 1 on page 31*]

Note D – Other Direct Costs – Ineligible Costs

Ineligible costs are explicitly questioned because they are unreasonable; prohibited by the audited agreement or applicable laws and regulations; or not award related.

Finding IFES 2 – Currency Exchange Rate – questioned $29,550. IFES did not use the appropriate exchange rates when converting amounts to US Dollars. [*Please refer to detailed Finding IFES 2 on page 28*]

Note E – Other Direct Costs – Ineligible Costs

Ineligible costs are explicitly questioned because they are unreasonable; prohibited by the audited agreement or applicable laws and regulations; or not award related.

Finding NDI 2 – Admin Cost-Sharing Rates – questioned $2,446. NDI did not perform proper review of these vouchers to ensure the correct rates and amounts are charged to the project. [*Please refer to detailed Finding NDI 2 on page 38*]

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[2] Prepared by Auditor

Note F – Contractual Costs – Unsupported Costs

Unsupported costs are those costs for which sufficient supporting documentation is not available.

Finding IFES 1 – Competitive Bid Process – questioned $894,126. The failure to comply with policies pertaining to opening goods and services to open and free competition is the result of a lack of knowledge by project staff of the applicable policies. Subcontracts were awarded based upon a misunderstanding of the proper justification for sole source procurements. [*Please refer to detailed Finding IFES 1 on page 26*]

Independent Auditor's Report on the Special Purpose Financial Statement

To the President, Consortium for Elections and Political Process Strengthening
1934 Old Gallows Rd., Suite 500
Vienna, VA 22182

Report on the Financial Statements

We have audited, the Special Purpose Financial Statement of the Consortium for Elections and Political Process Strengthening ("CEPPS") to support the Increased Electoral Participation in Afghanistan program under Cooperative Agreement 306-A-00-08-00529-00 for the period October 1, 2012 through September 30, 2013, hereinafter referred to as the financial statements. Our responsibility is to express an opinion on these financial statements based on our audit.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of the Special Purpose Financial Statement in accordance with U.S. Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Special Purpose Financial Statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Special Purpose Financial Statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Basis for Qualified Opinion

The results of our tests disclosed the following material questioned costs as detailed in the Special Purpose Financial Statement: (1) $175,467 in costs that are explicitly questioned because they are not program related, unreasonable, or prohibited by the terms of the agreement; and (2) $895,109 in costs that are not supported with adequate documentation or did not have required prior approvals or authorizations.

Qualified Opinion

In our opinion, except for the effects of the questioned costs discussed in the basis for qualified opinion paragraph, the Special Purpose Financial Statement referred to above presents fairly, in all material respects, program revenues, costs incurred and reimbursed by the U.S. Agency for International Development for the period October 1, 2012 through September 30, 2013 in accordance with the terms of the agreement or in conformity with the basis of accounting described in Notes to the Special Purpose Financial Statement, Page 10.

Other Reports Required by Government Auditing Standards

In accordance with U.S. Government Auditing Standards, we have also issued our reports, dated January 10, 2015, on our consideration of CEPPS' internal control over financial reporting and our tests of its compliance with certain provisions of laws and regulations. Those reports are an integral part of an audit performed in accordance with U.S. Government Auditing Standards and should be read in conjunction with this Independent's Auditor's Report in considering the results of our audit.

Restriction on Use

This report is intended for the information of CEPPS, the U.S. Agency for International Development and SIGAR. Financial information in this report may be privileged. The restrictions of 18 USC 1905 should be considered before any information is released to the public.

Davis & Associates

Alexandria, Virginia
January 10, 2015

Independent Auditor's Report on Internal Control

To the President, Consortium for Elections and Political Process Strengthening
1934 Old Gallows Rd., Suite 500
Vienna, VA 22182

We have audited, the Special Purpose Financial Statement of the Consortium for Elections and Political Process Strengthening ("CEPPS") and related notes to the Statement, to support the Increased Electoral Participation in Afghanistan program under Cooperative Agreement 306-A-00-08-00529-00 for the period October 1, 2012 through September 30, 2013, hereinafter referred to as the financial statements, and have issued our report, dated January 10, 2015.

Management Responsibility

Management is responsible for establishing and maintaining internal control. Estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies and procedures. The objectives of internal control are to provide management with reasonable, but not absolute, assurance that the assets are safeguarded against loss from unauthorized use or disposition; transactions are executed in accordance with management's authorization and in accordance with the terms of the agreement; and transactions are recorded properly to permit the preparation of the financial statements in conformity with the basis of accounting described in Note 1.

Auditor Responsibility

We conducted our audit in accordance with U.S. *Government Auditing Standards* issued by the Comptroller General of the United States. In planning and performing our audit, we considered the entity's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we do not express an opinion on the effectiveness of the entity's internal control. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected and projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

Internal Control over Financial Reporting

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses, and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

We consider the following deficiencies in the entity's internal control to be material weaknesses:

- IFES used the same exchange rate for the entire year. As a result, all of the expenditures that were made in the local currency were over billed when converted back to U.S. dollars. Over the course of the year, the actual exchange rate differed from the exchange rate used by as much as 15.2% (57.6343 vs. 50.00). The average rate over the year of 54.17305 represents an 8.3461% variance from the 50.00 that was consistently used. [Please refer to detailed Finding IFES 2 on page 28]
- IRI did not record salary withholding tax in its accounting system and relied on one individual employee to maintain separate records which may open the process to the possibility of fraud and misuse of funds collected from withholding taxes. [Please refer to detailed Finding IRI 2 on page 33]

We consider the following deficiencies in the entity's internal control to be significant deficiencies:

- IRI did not properly review and verify supporting document for payroll costs resulting in unsupported costs billed to the project. [Please refer to detailed finding IRI 3 on page 35]
- NDI did not accurately calculate and properly verify the allocation rates applied to field office costs resulted in overbilling to the project. [Please refer to detailed finding NDI 2 on page 38]

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control, and not to provide an opinion on the effectiveness of the entity's internal control. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

Restriction on Use

This report is intended for the information of CEPPS, the U.S. Agency for International Development and SIGAR. Financial information in this report may be privileged. The restrictions of 18 USC 1905 should be considered before any information is released to the public.

Davis & Associates

Alexandria, Virginia
January 10, 2015

Independent Auditor's Report on Compliance

To the President, Consortium for Elections and Political Process Strengthening
1934 Old Gallows Rd., Suite 500
Vienna, VA 22182

We have audited, the Special Purpose Financial Statement of the Consortium for Elections and Political Process Strengthening ("CEPPS") and related notes to the Statement, to support the Increased Electoral Participation in Afghanistan program under Cooperative Agreement 306-A-00-08-00529-00 for the period October 1, 2012 through September 30, 2013, hereinafter the financial statements, and have issued our report dated, January 10, 2015

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its USAID-funded program.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the USAID-funded program based on our audit of the types of compliance requirements referred to above. We conducted our audit in accordance with U.S. *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Schedule of Costs Incurred in Afghanistan and the U.S. is free of material misstatement resulting from violations of agreement terms and laws and regulations that have a direct and material effect on the determination of the Schedule of Costs Incurred in Afghanistan and the U.S. amounts.

Compliance and Other Matters

Compliance with agreement terms and laws and regulations applicable to CEPPS is the responsibility of CEPPS' management. As part of obtaining reasonable assurance about whether the Schedule of Costs Incurred is free of material misstatement, we performed tests of CEPPS' compliance with certain provisions of agreement terms and laws and regulations. However, our objective was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

Material instances of noncompliance are failures to follow requirements or violations of agreement terms and laws and regulations that cause us to conclude that the aggregation of misstatements resulting from those failures or violations is material to the Special Purpose Financial Statement.

In performing our testing, we considered whether the information obtained during our testing indicated the possibility of fraud or abuse. Evidence of possible fraud or abuse was not indicated by our testing. The results of our tests disclosed three instances of noncompliance that are required to be reported here under Government Auditing Standards and which are described in Findings IFES 1, IRI 1 and NDI 1 on pages 26, 31 and 36, respectively.

CEPPS' responses to the findings identified in our report are attached as Appendix A to this report. We did not audit these responses and, accordingly, we express no opinion on them.

This report is intended for the information of CEPPS, the U.S. Agency for International Development, and the Special Inspector General for Afghanistan Reconstruction, and is not intended to be and should not be used by anyone other than these specified parties. Financial information in this report may be privileged. The restrictions of 18 U.S.C. 1905 should be considered before any information is released to the public. However, subject to applicable laws, this report may be released to Congress and to the public by SIGAR in order to provide information about programs and operations funded with amounts appropriated or otherwise made available for the reconstruction of Afghanistan.

Davis & Associates

Alexandria, Virginia
January 10, 2015

Finding Number: 2013-01
Improper Vetting Procedures (Material Non-Compliance)

Prior Finding

"NDI and IFES did not have a written policy to enforce the vetting procedures prior to FY 2011 and FY 2012, respectively. In addition, NDI and IFES's new policy did not include the vetting of previous contracts that had already been awarded."

Current Status

We performed certain audit procedures on the CEPPS' response to these findings to determine if they had put the proper remediation procedures in place. We examined the following information:

1. USAID OIG Audit Report Number F-306-14-008-N, dated March 27, 2014 which included the Management Response
2. Written policies and procedures
3. Selected Subcontract Files

We examined the audit report to determine the findings that were required to be addressed. We reviewed both CEPPS's management response as well as the Auditor's further comments for items to be addressed. We reviewed the written policies and procedures regarding vetting and review subcontractor files and determined that the Auditee had properly addressed the finding and no further action is required.

Finding Number: 2013-02
Lack of Proper Supporting Documentation (Deficiency and Questioned Cost)

Prior Finding

"High Turnover and inadequate controls over document retention at the partner organization's headquarters resulted in documentation being misplaced or incomplete."

Current Status

We performed certain audit procedures on the CEPPS' response to these findings to determine if they had put the proper remediation procedures in place. We examined the following information:

1. USAID OIG Audit Report Number F-306-14-008-N, dated March 27, 2014, which included the Management Response
2. Written policies and procedures
3. Selected Subcontract Files

Given the prior findings we set the sample size for testing at 46% of total costs incurred under the audit period. We selected a statistically significant sample to allow us to determine if the Auditee had successfully mitigated this finding – this sample size was selected to provide us with reasonable assurance. While we did question some costs, we found that the Auditee had substantially mitigated this finding and no further action is required.

Finding Number: **IFES 1**

Audit Area: **Material Non-Compliance - Competitive Bid Process**

Condition:

We observed several instances where goods and services were subcontracted for a total dollar amount over $5,000 but were not accompanied with adequate supporting documentation showing the solicitation of three or more formal bids, cost and price analysis or prior approval and justification for sole source selection. The following subcontractors performed services and provided goods in excess of $5,000 for the period under audit without being exposed to a competitive bid process:

GW Consulting – Security Services ($890,806 paid in FY13)
The services of GW were subcontracted under the CEPPS project based on the fact that IFES was using the same service from them on a different project that they were performing simultaneously in Afghanistan.

IT Support Contractor - ($3,320 Sampled, Greater than $5,000 paid in FY13)
An Internal Selection Memo was drafted by IFES explaining that there was a pre-existing relationship between the subcontractor and IFES. The memo also explained that the subcontractor is known to be qualified; however, the qualifications are not unique.

Criteria:

Title 22, Part 226 of the Code of Federal Regulations

§226.43 – Competition

"All procurement transactions shall be conducted in a manner to provide, to the maximum extent practical, open and free competition."

§ 226.45 Cost and price analysis.

"Some form of cost or price analysis shall be made and documented in the procurement files in connection with every procurement action. Price analysis may be accomplished in various ways, including the comparison of price quotations submitted, market prices and similar indicia, together with discounts. Cost analysis is the review and evaluation of each element of cost to determine reasonableness, allocability and allowability."

§ 226.46 Procurement records.

"Procurement records and files for purchases in excess of the small purchase threshold shall include the following at a minimum: (a) Basis for contractor selection, (b) Justification for lack of competition when competitive bids or offers are not obtained, and (c) Basis for award cost or price."

According to the *IFES Field Office Policies and Procedures Manual*, goods and services provided in excess of $5,000 require the solicitation of three or more formal written bids. A Sole Source Justification may be used in very restricted circumstances such as the following:

Unicity*, i.e. the item is only available from one single supplier, like for parts maintenance; or*

Immediacy*, i.e. delays resulting from competitive solicitation are not acceptable; or*

Emergency*, i.e. delays resulting from other methods of solicitation are not bearable; or*

Legitimacy*, i.e. specific contexts (geographic, contractual, political, legal, military, security,*

etc.) may allow such a non-competition of sources; or

Inadequacy*, all sources are qualified as inadequate (compatibility, compliance, price, quality,*

service, support, etc.); or

Exigency*, i.e. any other specific reason dictating the choice of a given provider.*

Questioned Costs

$894,126

Cause

The failure to comply with U. S. regulation and IFES's own policies pertaining to opening goods and services to open and free competition is the result of a lack of knowledge by project staff of the applicable policies. Subcontracts were awarded based upon a misunderstanding of the proper justification for sole source procurements.

Effect

Failure to open subcontracts over the $5,000 threshold to open and free competition can result in the Government not receiving the most competitive price for certain goods and services. It also opens the process to the opportunity of fraud. We questioned $894,126 as a result.

Recommendation

We recommend that IFES should provide training to its personnel and update its procedures for conducting open and free competition, as applicable, and in accordance with federal regulations. We also recommend that procedures should address sole source justification and require prior approval from funding agency. We also recommend that IFES should refund to USAID the $894,126 in unallowable security and IT costs.

Finding Number: **IFES 2**

Audit Area: **Material Weakness in Internal Control and Ineligible Costs - Currency Exchange Rates**

Condition

Upon review of the supporting documentation for the costs that were sampled, it became apparent that the same exchange rate was used for the entire fiscal year 2013 – 50.00 AFN/USD. However, after reviewing the historical rates for the entire period (Oct. 1, 2012 through September 30, 2013), the exchange rate was never lower than 51.3386, and was as high as 57.6343. The average rate for the fiscal year was 54.17305. We asked whether or not IFES documented how they determined the exchange rate, or if there was any guidance available for the field offices in determining exchange rates, but IFES was unable to provide us with a policy, written or otherwise, addressing the issue of currency conversion.

Exchange rates in Afghanistan fluctuate throughout the course of a year. It is important to use the relevant exchange rates for a given time period when converting amounts in Afghani back to the U.S. Dollar for accounting and reimbursement purposes. IFES used the same rate for the entire year. As a result, all of the expenditures that were made in the local currency were over billed when converted back to U.S. dollars. Over the course of the year, the actual exchange rate differed from the exchange rate used by as much as 15.2% (57.6343 vs. 50.00). The average rate over the year of 54.17305 represents an 8.3461% variance from the 50.00 that was consistently used.

Criteria

22 CFR 228.40, ***Local procurement***, states that:

“Local procurement in the cooperating country involves the use of appropriated funds to finance the procurement of goods and services supplied by local businesses, dealers or producers, with payment normally being in the currency of the cooperating country.”

USAID ADS Chapter 303 Section M15 states:

“Upon arrival in the cooperating country, and from time to time as appropriate, the recipient's chief of party must consult with the Mission Director who must provide, in writing, the procedure the recipient and its employees must follow in the conversion of United States dollars to local currency. This may include, but is not limited to, the conversion of currency through the cognizant United States Disbursing Officer or Mission Controller, as appropriate.”

Because local procurement is taking place using the local currency, amounts must be converted to U.S. Dollars for billing and reimbursement purposes. In order to ensure that the proper exchange rates are being utilized when converting amounts for transactions, there should be procedures in place within the organization to identify the exchange rates regularly to account for variations in the price of the Afghani relative to the U.S. Dollar.

Questioned Costs

We questioned $29,550 in direct costs.

We requested a breakdown of all costs incurred by IFES over the period that were incurred in the local currency. Using the provided information by IFES, we applied the average exchange rate for the relevant month, as reported by the Afghan Central Bank, to each amount in the document provided by IFES. The results for each month are as follows:

Month	Average Exchange Rate	Amount in AFN	Amount Initially Reported in USD	Estimated Revised Amount in USD	Estimated Amount Over Billed
October '12	51.99	640,640	$ 12,812.80	$ 12,322.37	$ 490.43
November '12	52.82	1,476,098	$ 29,521.96	$ 27,945.82	$ 1,576.14
December '12	51.33	1,126,156	$ 22,523.12	$ 21,939.53	$ 583.59
January '13	52.02	1,711,595	$ 34,231.90	$ 32,902.63	$ 1,329.27
February '13	51.75	1,792,506	$ 35,850.12	$ 34,637.80	$ 1,212.32
March '13	52.37	1,727,611	$ 34,552.22	$ 32,988.56	$ 1,563.66
April '13	53.89	1,543,917	$ 30,878.34	$ 28,649.42	$ 2,228.92
May '13	55.01	2,017,448	$ 40,348.96	$ 36,674.20	$ 3,674.76
June '13	55.59	3,481,657	$ 69,633.14	$ 62,630.99	$ 7,002.15
July '13	56.47	3,100,768	$ 62,015.36	$ 54,910.01	$ 7,105.35
August '13	55.80	917,042	$ 18,340.84	$ 16,434.44	$ 1,906.40
September '13	56.35	389,420	$ 7,788.40	$ 6,910.74	$ 877.66
Total		19,924,858	**$ 398,497.16**	**$ 368,946.51**	**$ 29,550.65**

Cause

IFES failed to consult with USAID or provide its field office with guidance on calculating exchange rates regularly to account for the fluctuations in the local currency, resulting in a material weakness. Because IFES did not have policies or procedures in place to determine relevant exchange rates were being used for reimbursement and billing purposes, it applied a single rate throughout the period under audit.

Effect

Not adjusting the exchange rates used in the field office accounting system result in inaccurate costs billed to the U.S. Government.

Recommendations

We recommend IFES implement uniform procedures across the organization to regularly calculate exchange rates for conversions from foreign currencies, and ensure that the exchange rates utilized are actual, accurate and relevant to the period. Further, we recommend that IFES maintains documentation supporting the exchange rates used when currency is exchanged. Finally, we recommend IFES reimburse to USAID the $29,550 that was an estimate of the overbilling or calculate the amount owed based on the daily exchange rate.

Finding Number: **IRI 1**

Audit Area: **Material Non-Compliance with Local Tax Law Provision and Incurring Additional Costs in Tax Payments**

Condition

IRI did not deduct and withhold certain withholding taxes from payments made to its local contractors between March 2009 and March 2012. After receiving a notification from the Afghanistan Ministry of Finance in 2011, IRI contracted a private consultant (Satchu & Zhouand) to determine the amount of withholding taxes that should have been remitted to the Afghan government. The consultant provided an initial estimate of $85,564, including penalties and a revised estimate of $76,521 (3,979,121 in local Afghan currency) on October 22, 2012 that excludes the penalties that IRI says were waived by the Afghan government. On November 18, 2012, IRI deposited nine separate payments for each period of taxes that should have been withheld and remitted to the Afghan government totaling $76,521 and billed the tax payments as costs to the project, which were reimbursed by USAID.

In addition, upon review of IRI's security subcontractors invoices (Pilgrims Group Limited), we found that Pilgrims billed IRI for 2% BRT (Business Receipt Tax) imposed by the Afghan government on the subcontractor gross receipts. In addition to the amount billed for security costs, IRI paid an additional $23,661 for the 2% tax, instead of withholding the 2% required tax from payments to its contractors. We questioned an amount of $18,004 (2% tax paid during our audit period) as additional costs to the project and consider it unallowable.

Criteria

According to the Strategic Objective Grant Agreement (SOAG) signed on September 19, 2005 between the United States of America and the Islamic Republic of Afghanistan, Annex 1, Section B. 4. Taxation:

(*b) Except as provided otherwise in this provision, the General Exemption in subsection (a) applies to, but is not limited to (1) any activity, contract, grant or other implementing agreement financed by USAID under this Agreement; (2) any transaction or supplies, equipment, materials, property or other goods (hereinafter collectively "goods") under (1) above; (3) any contractor, grantee, or other organization carrying out activities financed by USAID under this Agreement; (4) any employee of such organizations; and (5) any individual contractor or grantee carrying out activities financed by USAID under this Agreement.*

Questioned Costs

We questioned a total amount of $112,199 including associated indirect costs calculated as follows.

1. $94,094 ($76,521 in direct costs plus $17,049 for 22.28% IRI Overhead costs totaling to $93,570 plus $524 for additional 0.56% for CEPPS indirect costs).
2. $18,105 ($18,004 in direct costs plus 0.56% CEPPS indirect costs. No IRI Overhead applied for this amount).

Cause

An internal assessment conducted by a consultant on behalf of IRI determined that IRI did not withhold taxes on its payments to local contractors. After receiving the consultant's assessment, IRI remitted to the Afghan government the funds it should have withheld from IRI's payments to local contractors. IRI then billed this amount to USAID. USAID is exempt from paying taxes on its contracts. Therefore, USAID had no duty to cover the cost of the taxes that IRI may have been obligated to withhold from its subcontractors. By billing the amount of the tax payment to USAID, IRI was claiming an unallowable cost.

Effect

IRI did not fully comply with the local tax law and because IRI did not accurately apply Afghan tax law provisions, USAID was invoiced for $112,199 in tax amount as additional costs that were unallowable.

Recommendation

IRI should refund to USAID the amount of $112,199 questioned as unallowable costs. We also recommend that IRI follow local tax law provisions and improve its field office procedure manual related to contractor withholding taxes to ensure full compliance with the local tax law. IRI should also ensure that its subcontractors have a tax exemption, otherwise, withhold the applicable tax from their payments

Finding Number: **IRI 2**

Audit Area: **Material Weakness in Internal Control - Salary Withholding Taxes**

Condition

In reviewing IRI processes for recording salary withholding taxes, we found that IRI did not record the salary withholding tax for its local national employees in its main financial records such as the payroll sheets and in the accounting software. Instead, the salary withholding tax payments were tracked on a separate spreadsheet by an individual local employee of IRI (Office Manager) who then calculates the withholding tax amount for each employee and deposits those amounts to the Afghan Ministry of Finance, Revenue Department, obtaining a stamped bank deposit form from that department as proof of payment of the taxes.

Criteria

IRI Field Accounting Policy and Procedures, V. QUICKEN PROCEDURES:

Quicken is the accounting system used by IRI field offices for the purpose of financial record keeping and reporting.... Field accountants will enter all transactions in Quicken and submit Quicken files to HQs accounting not later than three business days after the end of the reporting month.

Article 58 of the Afghan Tax Law states that "All natural or legal profit and no- profit persons, ministries, state enterprises, municipalities and other State departments employing two or more employees in any month of a year shall be required to withhold taxes as provided in Article 4 of this Law from payment of salaries and wages and pay the amount withheld to the Government account."

Article 61.1 of the Afghan Income Tax Manual requires "The employer and employee have certain reporting obligations with respect to wage withholding that have to be complied with.

> *a) Every year, the employer must prepare an Annual Salary and Tax Statement for each employee subject to wage withholding. At any time that an employee ceases employment, the employer should provide the Annual Salary and Tax Statement at the time of cessation of employment.*
>
> *b) In addition, the employer must prepare an Annual Summary Report of Taxes Withheld and Wage and Tax Statement Transmittal Form. The purpose of this form is to provide the Ministry of Finance with a summary of all of the amounts that the employer has withheld from all of its employees during the year."*

Questioned Costs

None

Cause

IRI believed that only the employees are responsible for filing their taxes. Therefore, IRI did not properly establish control over documenting, recording and reporting of these taxes despite being aware of the local tax law requirements.

Effect

Relying on one individual employee rather than recording the withholding tax in the accounting system will open the process to the possibility of fraud and misuse of funds collected from withholding taxes. Also, IRI cannot ensure that taxes are recorded and reported accurately because there are no internal controls established to verify the amounts.

Recommendation

IRI should improve its procedures manuals to ensure proper internal controls over the process of collecting and depositing employee taxes are in place.

Finding Number: **IRI 3**

Audit Area: **Significant Deficiency in Internal Control - Employee payments Unsupported Costs**

Condition

Upon review of IRI local national employees' payroll, we found that a local national employee was paid $1,275 in salary for the month of January 2013 rather than $1,175 established as monthly salary in her employment contract for the period November 1, 2012 to June 30, 2013. In response to our request for information and supporting documents, IRI explained that the extra $100 per month paid to this employee was for education allowance ($550) and health allowance ($650). However, the employment contract states that such allowances will be reimbursed at actual costs incurred and supported by written receipts, which were not provided to us. Therefore, we question the additional cost in the amount of $800 ($100 per month for the period of employment contract) as unsupported and unallowable.

Criteria

Employee contract: *Payment of education and health allowances will be given as reimbursement based on supporting documents.*

IRI Field Office Accounting Policies and Procedures, III Allowable Costs*: "As a general rule, in order to be allowable all costs must be reasonable, necessary for the project implementation, and adequately documented."*

Questioned Costs

$983 ($800 in direct costs plus $178 for 22.28% IRI indirect costs totaling $978 plus $5for 0.56% CEPPS indirect costs)

Cause

IRI did not properly verify the employee payments in the payroll sheet with the supporting documents for this particular employee.

Effect

USAID paid $983 in costs that were unallowable under the agreement terms.

Recommendation

IRI should refund to USAID the amount of $983 questioned as unallowable costs. We also recommend that IRI ensure no other unsupported costs related to all IRI employees are billed to USAID.

Finding Number: **NDI 1**

Audit Area: **Material Non-Compliance -Purchase of Business Class Airfares – Unallowable Costs**

Condition

NDI incurred costs in the purchase of business class airfares for its employees traveling between the United States and Afghanistan. NDI used the same dual justification for purchase of all four Business class airfares, which was noted in the travel authorization forms stating that the travel exceeded 14 hours and the "*Need to immediately commence working upon arrival*". In one instance, a first class airfare was purchased from Washington to Denver.

Although NDI travel policy allows use of Business class airfare for various reasons including "*an imperative to operate on the ground immediately upon arrival or a short duration of say*." The same travel policy also states "*Use of this exception precludes the traveler from using a rest stop en route as well as a rest period upon arrival at the duty site.*" However, all travelers were provided with hotel accommodations in Dubai where their travel schedule required overnight stay.

In addition, when authorizing these trips, NDI made a costs comparison between these business class airfares and the highest coach fares, which resulted in relatively closer amounts, but OMB A-122 states "*Airfare costs in excess of* customary standard commercial airfare (coach or equivalent)… or *the lowest commercial discount airfare are unallowable"* without proper justifications.

We questioned the costs in excess of average lowest coach/economy class airfare because we did not find the documented justifications to meet OMB A-122 requirements for cost reasonableness and travel costs exceptions listed under the criteria below.

Audit Sample #	Voucher #	Booking Date	Travel Dates	Travel Route	Cost Incurred	Questioned Cost	Auditor Notes
31	200146549	8/8/2013	8/22/2013 to 9/1/2013	Washington - Dubai - Kabul - Dubai - Washington – Denver	$10,074.30	$7,754.30	Other economy class round trip tickets for routes between Washington DC and Kabul were purchased around the same period at costs between $1,966 and $2,320. Therefore, we question the amount in excess of $2,320.
	200146549	8/8/2013	8/18/2013 to 8/29/2013	Dubai - Kabul - Dubai - Washington	$7,352.24	$5,032.24	
	200146549	8/14/2013	9/20/2013 to 9/27/2013	Dubai - Kabul - Dubai - Washington	$9,843.90	$7,523.90	
	200146549	8/16/2013	9/12/2013 to 9/27/2013	New Jersey- Delhi -Kabul - Dubai - Washington	$7,292.79	$4,972.79	
	Total				**$34,563.23**	**$25,283.23**	**Plus $5,988.77 for OH and CEPPS level Indirect cost applications.

Criteria

OMB A-122, Attachment B, 51 – Travel Costs

c. Commercial air travel.

(1) Airfare costs in excess of the customary standard commercial airfare (coach or equivalent), Federal Government contract airfare (where authorized and available), or the lowest commercial discount airfare are unallowable except when such accommodations would: (a) require circuitous routing; (b) require travel during unreasonable hours; (c) excessively prolong travel; (d) result in additional costs that would offset the transportation savings; or (e) offer accommodations not reasonably adequate for the traveler's medical needs. The non-profit organization must justify and document these conditions on a case-by-case basis in order for the use of first-class airfare to be allowable in such cases.

(2) Unless a pattern of avoidance is detected, the Federal Government will generally not question a non-profit organization's determinations that customary standard airfare or other discount airfare is unavailable for specific trips if the non-profit organization can demonstrate either of the following: (a) that such airfare was not available in the specific case; or (b) that it is the non-profit organization's overall practice to make routine use of such airfare.

Questioned Costs

$31,272 ($25,283 in direct costs plus $5,815 for 23% NDI indirect costs totaling $31,098 plus $174 for 0.56% CEPPS indirect costs)

Cause

NDI believed their justification for the traveler's need to work immediately upon arrival in conjunction with the fact that the flight was in excess of 14 hours is in accordance with NDI travel policy and the use of business class airfare is allowable.

Effect

NDI did not properly follow the travel guidance, and therefore, USAID was billed $31,272 in unallowable costs.

Recommendation

We recommend that NDI refund to USAID $31,272 in unallowable costs. We also recommend that NDI consistently comply with federal regulations related to travel policy and purchase of business class airfares.

Finding Number: **NDI 2**

Audit Area: **Significant Deficiency in Internal Control - Shared Costs Over-Charged to Election Project – Unallowable Costs**

Condition

NDI charged its field office costs related to administrative personnel and operating costs based on an allocation schedule where all shared costs are charged to different beneficiary projects based on certain percentages. The election project was charged at different rates between 20% and 36% of all shared costs as fair share during our audit period. Although the rates for shared costs were applied consistently throughout the audit period, we noted certain instances where an incorrect allocation rate was used. As a result of using incorrect and higher allocation rates, the election project was overcharged in the amount of $1,977. We questioned this amount because this is the difference between the amounts that have been charged and the amount that should have been charged if the correct allocation rates were used.

Audit Sample #	Cost Description	Actual Amount Charged	Correct Amount	Questioned Cost Amount	Auditor Notes
23	Bamyan office rent for September 2013	$ 744	$ 600	$ 144	24.8% of Bamyan office rent charged to the Election project instead of 20% approved allocation rate for September 2013, resulting in a potential overcharge of $144 (4.8% of $3,000)
37	Transportation costs for June 2013	$11,854	$ 10,572	$ 1,282	37% charged instead of 33% approved rate for February - August 2013 resulting in potential overcharge of $1,281 (4% of $30,801+$1,236)
58	Vehicle leases for October 2012	$19,836	$ 19,285	$ 551	Cost charged to Election at 36% versus 35% allocated for October 2012 invoice in the total amount of $55,100 which result in potential overcharge of $551 (1% of $55,100)
	Total	**$32,434**	**$30,457**	**$1,977**	****Plus $469 for application of G&A and CEPPS-level Indirect Cost rates**

Criteria

Based on NDI internal memos for Afghanistan field costs allocation schedules, the following rates were approved for the CEPPS Election. *20% for September 2013, 33% for June 2013, and 35% for October 2012.*

Questioned Costs

$2,446 ($1,977 in direct costs plus $455 for 23% NDI indirect costs totaling to $2,432 plus $14 for 0.56% CEPPS indirect costs)

Cause

NDI did not perform proper review of these vouchers to ensure the correct rates and amounts are charged to the Election project.

Effect

Because the allocation rates were not applied correctly, USAID's CEPPS Election project was overbilled by $2,446.

Recommendation

We recommend that NDI properly review its vouchers with cost allocations to ensure the correct rates and amounts are charged to each project in the future. We also recommend that NDI refund USAID's CEPPS Election project for $2,446 overbilled.

Finding Number: IFES 1
Audit Areas: Material Non-Compliance - Competitive Bid Process

Management Response

Competitive Bid Process – GW Consulting Security Services ("GW")

The draft report concludes that IFES failed to comply with U.S. law and its own policies based on its misunderstanding of proper justification for sole source procurements. This conclusion is premised on the assumption that "the services of GW were subcontracted under the CEPPS project based on the fact that IFES was using the same service from them on a different project that they were performing in Afghanistan." The draft report recommends that IFES should update its procurement procedures, provide additional training, and refund to USAID the unallowable security costs.

IFES disagrees with the conclusion and rationale set forth in the draft report with respect to this finding, and maintains that IFES' decision to retain GW was (1) based on a number of factors and cost data that resulted in significant savings to the Government and are consistent with IFES's procurement policies and applicable regulations, and (2) the sole source justification and use of GW was presented to and accepted by USAID.

The rationale for IFES' decision to engage GW and the significant resultant cost savings (discussed below) were considered internally and presented to and accepted by USAID initially when the budget was modified and reprogramed for the first year of the CEPPS project (February 2009 to September 2009), and again when the CEPPS Agreement was formally modified for the period July 1, 2009 – September 29, 2011. The cost savings and sole source justifications associated with GW were subsequently incorporated by reference into the CEPPS Agreement pursuant to Modification 4, which deleted the "Program Description" section of the CEPPS Agreement in its entirety and replaced it with the revised proposal submitted by CEPPS on September 10, 2009.

In its proposal to USAID for an increased security budget under CEPPS, IFES indicated that GW was selected by IFES as the security provider for STEP based on a competitive process under a Request for Proposal in which seven bidders submitted an expression of interest. GW was selected during the competitive process, as they offered the best technical proposal and most reasonable cost for the provision of the services. Since there was considerable overlap in the scope, location and timing of the security services needed for the STEP and CEPPS programs, IFES had in its possession recent cost and performance information for comparable services from a number of qualified security providers upon which it could analyze and evaluate the costs proposed by GW for the services under the CEPPS program. At the time CEPPS security agreement commenced (March 23, *2009), less than five months had elapsed since the STEP competitive bidding process had concluded (November 2008). The IFES procurement policies provide an exception from full bid solicitation where, as here, a similar bidding process has been conducted within one year.*

In addition to the recent cost data and qualifications available to IFES from the STEP procurement, IFES also considered the potential and material cost savings that could arise from the use of GW on both the STEP and CEPPS projects based on shared and allocated basic security infrastructure. These costs savings were of heightened importance in light of the budgetary constraints imposed by USAID on the initial security budget for the CEPPS project and the deteriorating security situation in Afghanistan at that time. These material cost savings could only be realized if IFES selected GW since GW was the only firm that had the basic security infrastructure in place for the STEP project (on the most favorable terms based on a competitive procurement concluded less than five months prior to the commencement of the CEPPS project) and, consequently, the only firm capable of realizing the proposed cost reducing synergies. Hence, the concepts of unicity (as to GW) and inadequacy (as to other qualified security providers), and exigency (the security and safety of IFES personnel) were all present and considered by IFES in the selection of GW for the CEPPS project.

The following specific sole source justifications and cost reduction considerations were presented by IFES to USAID in the revised Program Description that was accepted by USAID and incorporated by reference into the CEPPS Agreement as part of Modification 4:

- *Hire full complement of local national (LN) guards, to staff both of its facilities (office and guest house). The guards will be trained by GW.*
- *To promote efficiency in the use of USAID's resources, CEPPS IFES will collaborate with the USAID-funded IFES STEP Afghanistan project to share the services of a full-time expatriate Project Security Manager, who will be responsible for overseeing the overall security for the IFES STEP and CEPPS projects. The Security Project Manager would officially be hired by IFES STEP and approximately 20% of his/her salary would be paid from CEPPS Afghanistan security funds.*
- *Likewise, IFES CEPPS will be responsible for approximately 30% of the salary for a Watchkeeper (LN), who will be responsible for tracking the movement of IFES vehicles and staff. IFES CEPPS will also contribute 10% of the subscription cost for the GW Operations room, which will be the monitoring and communications facilities to ensure that all IFES staff whereabouts are known at all times. The operations room will be staffed by the Watchkeeper.*
- *Hire LN armed Guard Commanders for each of its facilities.*
- *Hire LN armed Senior Guard Supervisor that will be responsible for overseeing and managing the guard commanders and guards.*
- *Hire LN armed escorts to accompany international staff when traveling in and around Kabul.*
- *Provide its current drivers with a driving course recommended by GW.*
- *Provide tracking devices for international staff and consultants.*
- *Provide tracking devices for each vehicle.*
- *Pay 10% of the Quick Reaction Force (QRF) subscription rate. The remaining cost of the QRF will be paid by IFES STEP.*

As to the recommendations set forth in the draft report, IFES reviews and updates its procurement policies and procedures on a regular basis. This includes the provision or supplementation of training as needed. Finally, IFES maintains that the security costs at issue are not "unallowable" insofar as they are not expressly unallowable under any applicable law, regulation or agreement, they are allowable under applicable law, and they were accepted as allowable by USAID.

Competitive Bid Process – IT Support Contractor

The draft report indicates that an Internal Selection Memo was drafted by IFES explaining that there was a pre-existing relationship between the subcontractor and IFES and that the subcontractor was known to be qualified. The draft report concludes that the qualifications of the subcontractor are not unique. As a result, the draft report concludes that IFES failed to comply with U.S. law and its own policies based on its misunderstanding of proper justification for sole source procurements. The draft report recommends that IFES should update its procurement procedures, provide additional training, and refund to USAID the unallowable costs.

IFES's disagrees with the conclusion and rationale set forth in the draft report with respect to this finding, and maintains that the decision to retain the IT support contractor was consistent with IFES's procurement policies and applicable regulations and resulted in cost savings to the Government.

The selection memorandum indicates the consultant was to be paid hourly at the rate of $20/hour to provide assistance on an as needed basis from anywhere between 2 and 20 hours per month for total compensation not to exceed $6300/year. The contract was being revised to convert the consultant's arrangement from a flat monthly fee of $600/month to the hourly arrangement because IFES felt this would result in cost savings based on IFES' historic use of the services. Although the ceiling was set at $6,300, based on a maximum anticipated use of 20 hours per month, the contract was anticipated to pay no more than $4,800 during the course of the year.

The consultant had worked with IFES for over two years and was known to possess the qualifications necessary to perform the work. The consultant was also familiar with IFES' systems and IT needs, whereas any other consultant would have required time (and added cost) to become familiar with the systems and user needs. For such a small contract for such a critical function as IFES' IT system, this consultant was uniquely qualified not based solely on skill set, but rather based on the consultant's known ability to perform the work, familiarity with the system, and a willingness to perform the work on an as needed basis for an uncertain level of compensation.

Finally, as with the security costs, the IT service costs at issue are not "unallowable" insofar as they are not expressly unallowable under any applicable law, regulation or agreement, they are allowable under applicable law, and they were not "determined unallowable" by USAID under applicable regulations.

Finding Number: **IFES 2**
Audit Areas: **Material Weakness in Internal Control and Ineligible Costs - Currency Exchange Rates**

Management Response

Across the organization, IFES uses the weighted average rate at which it converts US dollars into local currency to record transactions paid for in local currency. In addition, field offices are asked to exchange currencies at institutions that provide receipts or other forms of documentation of the transactions. The Afghanistan CEPPS office did not follow this practice during the fiscal year in question.

IFES accepts the finding and will implement the auditor's recommendations going forward.

Finding Number: **IRI 1**

Audit Area: **Material Non-Compliance with Local Tax Law Provision and Incurring Additional Costs in Tax Payments**

Management Response

Full compliance with applicable local laws is important to IRI and, accordingly, IRI implements robust policies and procedures to assist our field offices and staff with such compliance. In the context of this draft Finding, however, it must be recognized that, in many jurisdictions where IRI supports USAID's development of democracies and political systems, it is not uncommon to face difficulties in deciphering the exact applicability of local tax laws, especially where the U.S. Government and political organizations of the local jurisdiction provide inconsistent views. As a result, recipients of foreign assistance funds often look to the U.S. Government to provide guidance on navigating these issues.

The 2009 Afghanistan tax law is an example of this type of situation. See SIGAR Audit 13-8, Taxes: Afghan Government Has Levied Nearly a Billion Dollars in Business Taxes on Contractors Supporting U.S. Government Efforts in Afghanistan (May 2013) (available at http://www.sigar.mil/pdf/audits/2013-05-14-audit-13-8.pdf) ("SIGAR Report on Afghan Taxes"). "Finding Number IRI 1" addresses two separate tax-related issues based on this law, each of which is discussed below.

1. Tax Assessment by Afghanistan's Ministry of Finance

The first issue relates to IRI's payment of certain withholding taxes to the Afghan government. Here, the Draft Audit Report states that because IRI did not withhold certain taxes from its payments to local employees and vendors, IRI believed it was obliged to satisfy these outstanding taxes and did so using federal assistance funds. On the basis of this finding, the Draft Audit Report recommends that IRI refund to USAID $94,094 (including indirect costs as described above), follow local tax law provisions, and improve its field office procedures manual relating to contractor withholding taxes to ensure full compliance with local tax laws.

IRI disagrees with this draft Finding and the proposed Recommendation because IRI properly charged these taxes to the Cooperative Agreement.

After Afghanistan passed a new tax law in 2009, there was widespread confusion surrounding the application of Afghanistan taxes, including inconsistent directions from the U.S. Government and confusion among USAID implementers regarding their tax liabilities. USAID's implementers had previously been operating under tax exempt status pursuant to the Strategic Objective Grant Agreement ("SOAG") dated September 2005 between

USAID and Afghanistan, providing that U.S. foreign "assistance . . . is free from any taxes imposed under laws in effect in [Afghanistan]." As a result, it was unclear whether IRI was required to withhold certain taxes from payments made to local employees and local vendors, and to remit, on their behalf, those withheld amounts as taxes payable to the Afghanistan government.

In 2011, IRI received an initial notification of unremitted taxes from the Afghanistan Ministry of Finance ("MOF") and learned that Afghan authorities believed the 2009 tax law superseded the SOAG. IRI quickly sought guidance from USAID in Kabul on IRI's tax obligations. On November 30, 2011, IRI was told by its USAID Agreement Officer Representative that it was "undoubtedly tax exempt." Nonetheless, the inquiries from the MOF continued, and, as a result, IRI continued to press USAID for any further guidance in responding to the MOF. It was not until February 2012, after increasingly urgent requests from IRI and other implementers, that USAID distributed general guidance to its implementers on registering as a tax exempt organization under the new 2009 law. In April 2012, when IRI sought clarification regarding how this tax exempt status applied to specific tax liabilities, USAID directed IRI to seek advice from legal counsel. Meanwhile, IRI received repeated and increasingly threatening inquiries from the MOF about IRI's tax liabilities. When the MOF in Kabul threatened court action in response to IRI's alleged failure to pay taxes, IRI took the threat very seriously. As it turned out, IRI's concerns were not unfounded. The SIGAR report addressing tax collection efforts by the MOF reported that, as a result of alleged outstanding taxes, the MOF "restricted some contractors' freedom of movement" and also took actions that "resulted in arrests and arrest warrants for contractor personnel." See SIGAR Report on Afghan Taxes at 9.

RI followed USAID's direction, and after a competitive bidding process, retained in June 2012 a Kabul-based law firm, Satchu and Zhouand, to determine IRI's obligations and the amount of local taxes owed to the Afghan government within the new legal framework. Concurrently, IRI pursued tax exempt status from the MOF with USAID support. IRI received its letter of tax exemption in August 2012. The MOF, however, contended that IRI continued to have tax obligations under the 2009 law for certain categories of withholding taxes. In September 2012, IRI's local legal counsel calculated the alleged outstanding tax payments for the previous years, identifying $76,521.00 in uncollected withholding taxes from customary Ramadan bonuses paid to employees, rental agreements for certain field offices, and local contractors.

Although IRI and the various employees, landlords, and vendors jointly shared the obligation to pay these back taxes, IRI determined that it would be very difficult to retroactively impose and seek to collect these withholding taxes from these entities and individuals for various reasons. Among other reasons, such efforts could detract from IRI's efforts in fulfilling the objectives of the Cooperative Agreement, and impose on IRI substantial *administrative costs and burdens of pursuing numerous collection actions (often for small individual amounts) with minimal anticipated benefit due to the widespread confusion about the 2009 Afghan tax law. IRI also sought to avoid any reason for Afghanistan authorities to initiate legal actions against it.*

In addition, USAID was fully aware of IRI's plans to charge the payment of these taxes to the Cooperative Agreement. On September 24, 2012, IRI met with USAID officials to discuss IRI's proposed plan for addressing the assessment of unpaid taxes. At this meeting, IRI informed USAID of its intention to pay the taxes owed to the Afghan government using program funds, and USAID did not object. Indeed, USAID raised no concerns during that meeting, and simply requested a written summary from IRI that local USAID staff could forward to their contracting office. IRI complied and sent an email on September 27, 2012 to USAID that confirmed our prior discussion, namely that these taxes were incurred during IRI's performance of the Cooperative Agreement and that they would be applied to this agreement. IRI followed up with USAID by email on October 18, 2012, again confirming its intention to charge the payment of these Afghan taxes to the Cooperative Agreement.

On November 18, 2012, IRI completed payment of the $76,521.00 owed to Afghan tax authorities and billed the costs to the Cooperative Agreement, which had been in effect since 2009. On November 28, 2012, IRI informed USAID of this payment. The next day, USAID's Agreement Officer Representative acknowledged receipt of IRI's message and stated that he was "happy to hear that IRI has successfully put this issue behind them." Importantly, IRI did not charge any late fees to the Cooperative Agreement; IRI paid late fees, associated with these back taxes, from IRI private funds.

USAID thus accepted IRI's treatment of the back taxes, including charging these tax payments as costs associated with performing the Cooperative Agreement. Because USAID originally advised IRI that it did not need to collect these taxes and then acquiesced in IRI's plans to pay those back taxes, there is no basis for Davis to recommend reimbursement. See, e.g., Lockheed Martin Western Devel. Labs., 02-1 B.C.A. ¶ 31803 (2002) ("It is well established that where the Government has consistently accepted and allowed a cost in the past, the Government may not retroactively disallow the cost."); District of Columbia Eligibility for Local Public Works Grant Funds, B-118638, 1979 WL 11877 (Oct. 29, 1979) (recognizing that grantee is entitled to rely on federal agency's interpretation of relevant terms, despite Government's later reversal).

Given USAID's initial statements, the overall confusion arising from the 2009 Afghan tax law, and the consent by local USAID officials to IRI's treatment of these payments, IRI properly charged these taxes to the Cooperative Agreement.

2. Afghanistan's Business Receipt Tax

The second part of "Finding Number IRI 1" relates to IRI's payment of a local business tax to its security risk manager, who in turn, would transmit the funds to the MOF. Here, the Draft Audit Report stated that IRI relied on its subcontractor to pay the business tax due to the Afghan government and failed to withhold these taxes. On the basis of this finding, the Draft Audit Report recommends that IRI refund to USAID $18,105 (including indirect costs as described above), follow local tax law provisions, improve its field office procedures manual relating to contractor withholding taxes to ensure full compliance with local tax laws, and ensure that IRI's subcontractors secure a tax exemption (or, otherwise withhold the applicable taxes from contractor payments).

IRI does not agree with this draft Finding and the proposed Recommendation because IRI properly charged the business tax payments to the Cooperative Agreement.

The context of IRI's payment of these taxes to its security risk manager is important. IRI began paying them after it had been receiving increasingly threatening inquiries from the MOF about the unpaid back taxes described in Section 1 above. At the operative time, IRI had received advice that it was obligated to withhold a 2% Business Receipt Tax ("BRT") from the amount paid, under its subcontract, to its risk management consultant firm, Pilgrims Group Limited ("Pilgrims"), a U.K. company. The Draft Audit Report asserts (at 34) that IRI was "well aware of the local tax law requirements," but this statement is not consistent with the documents made available during this audit nor consistent with the confusion surrounding Afghanistan's tax laws at the time. As with the contractor withholding tax issue addressed above, the applicability of Afghanistan's various tax laws were far from clear. Nor did USAID provide consistent guidance to its implementers on those tax issues. In fact, in 2013, SIGAR itself concluded that U.S. and MOF officials disagreed as to the tax-exempt status of foreign subcontractors and that this disagreement generated confusion. See SIGAR Report on Afghan Taxes at 7. In any event, based on advice from local legal counsel—the same Kabul-based law firm, Satchu and Zhouand, that advised on the back taxes—IRI understood that its arrangement with Pilgrims was in compliance with local tax laws. IRI's legal counsel explained that "contracts, for which payment is transmitted directly from US to an international bank account (. . . UK for Pilgrims . . .), would not fall under IRI's obligation to withhold. However, it would fall under the contractor's obligation for payment." Thus, in order to comply with local tax law (as IRI understood it at the time), IRI and Pilgrims added a 2% BRT line item to Pilgrims' invoices starting in June 2012, which IRI paid. In addition, IRI worked with Pilgrims to confirm the tax exempt status of the subcontract.

IRI understood that Pilgrims would remit the BRT amount, currently held in escrow, to the Afghan government as part of its FY2013 tax filing. IRI understands from Pilgrims that Pilgrims is currently undergoing an audit by *the Afghan government for FY2013 and, as a result, Pilgrims' FY2013 taxes have not yet been finalized, including a determination of whether the BRT is owed to the Afghan government. IRI has already requested that Pilgrims return to IRI any BRT funds that it is not obligated to pay the Afghan government as a result of Pilgrim's audit by the Afghan government. IRI, in turn, will provide any reimbursed funds to USAID.*

As with the back taxes, IRI was fully transparent with USAID regarding its subcontract with Pilgrims. In May 2012, IRI shared its draft Pilgrims subcontract with USAID and IRI requested the agency's approval of the subcontract. The draft included the provision regarding the 2% BRT. Later that month, on May 31, the USAID Agreement Officer Representative preliminarily approved the Pilgrims subcontract, but included three detailed requests for clarification from IRI as to certain unrelated costs and services. USAID did not raise any questions about, or object to, the inclusion of the BRT. In June 2012, IRI responded to the USAID questions regarding the Pilgrims subcontract, and the USAID Agreement Officer Representative approved the subcontract. After USAID approved the contract, IRI signed the agreement with Pilgrims (in June 2012).

As with the back taxes, USAID thus was aware of and accepted IRI's treatment of the BRT taxes. Accordingly, there is no basis for Davis to recommend reimbursement. See, e.g., Lockheed Martin Western Devel. Labs., 02-1 B.C.A. ¶ 31803; District of Columbia Eligibility for Local Public Works Grant Funds, 1979 WL 11877 (the Government's acceptance and approval of grant applications in which the grantee indicated that it expected to be reimbursed for certain costs created a "binding obligation" on the Government).

Given the confusion arising from Afghan tax laws and the approval by local USAID officials of IRI's subcontract with Pilgrims, IRI properly charged these funds to the Cooperative Agreement. As mentioned above, if IRI is reimbursed BRT funds from Pilgrims, IRI will, in turn, refund those funds to USAID.

Finding Number: IRI 2

Audit Area: Material Weakness in Internal Control - Salary Withholding Taxes

Management Response

IRI does not agree with this draft Finding, the "material" weakness designation, or the proposed Recommendation because, as set forth below, IRI is already in compliance with the Recommendation with its existing procedures and controls.

As shared with Davis, IRI's Field Office Accounting Policy and Procedures provide for IRI's field office accounting staff, such as the local accountant/office manager, to be responsible for field office compliance with local laws including the "[w]ith[holding of] payroll taxes" and for "remit[ting] taxes to local tax authorities regularly." IRI's field offices use the accounting software Quicken for financial record keeping and reporting to, among other things, track field office expenditures. In the Afghanistan field office, IRI elected to appropriately supplement the Quicken records by using Excel software to precisely track each employee's specific withholdings because Excel spreadsheets provided a better method of tracking payroll withholding. Although an organization operating in the U.S. might select another method, this system for the field office reflected the realities of the infrastructure available in Afghanistan at the time and was a common practice used by other non-profit organizations stationed there. Thus, IRI's local accountant/office manager was tasked with maintaining a spreadsheet of salary withholdings of local tax for all local staff employees; the spreadsheet tracked each employee's gross salary and calculated the proper withholding amounts to be paid to the MOF. This employee also paid the appropriate taxes to the MOF and obtained a stamped bank deposit form showing proof of payment of the taxes. This record was kept separate from the payroll documents. The process took place in tandem with IRI's tracking of monthly program expenses via its monthly imprest. Consistent with IRI's Field Office Accounting Policy and Procedures, the monthly Excel spreadsheet reflected amounts that were reconciled to the Quicken gross amounts as well as amounts remitted to Afghan government for taxes withheld.

Moreover, contrary to the Draft Audit Report (at 37), IRI relied on more than one individual employee to comply with local salary withholding taxes. In describing its practices, IRI identified an employee by name who administered the practice in Kabul, but IRI never stated that this employee acted alone and without any supervision. This employee was subject to oversight by IRI staff onsite and in Washington, DC – as required by IRI's robust internal controls and accounting policies to ensure the appropriate use of Federal funding. IRI's internal controls include supervision and oversight of field accounting staff by the Regional Country Director, whose responsibilities include ensuring "Field Office's compliance with local law" including "taxes" and "[e]nsur[ing] correct tax withholdings and timely remittances" by field office staff. An IRI memorandum, authored by IRI's Regional Country Director during the operative time period and provided to Davis, confirms *that IRI implemented its internal controls for this grant, stating that the Regional Country Director's responsibilities "included oversight of IRI's withholding and paying of employment taxes for local national staff" and that IRI followed its practices and procedures for the remittance of those taxes. Furthermore, the local accountant/office manager worked closely with, and was managed by, IRI's Washington-based Accounting staff.1*

The documentation produced during the audit thus does not support Davis' findings that IRI "rel [ied] on one individual" to administer the withholding/payment of these taxes or that IRI "did not properly establish control over documenting, recording and reporting of [employee withholding taxes]." Draft Audit Report at 37. For the same reasons, IRI also disputes any suggestion that IRI's accounting process in Afghanistan took place outside of IRI's normal accounting procedures.

IRI also disputes the assertion that IRI "believed that only the employees are responsible for filing their taxes." Draft Audit Report at 37. This statement is not consistent with the information and documents IRI provided to Davis. IRI has repeatedly stated to Davis that IRI collected the employment taxes from employees and paid them to the Ministry of Finance, as evidenced by documents shared with the auditors. For example, IRI provided Davis with copies of the "Report[s] of Tax Withholding and Bank Deposit Form for Employees,: documents confirming IRI's submission of withheld taxes to the Ministry of Finance. IRI also provided a memo to Davis stating that "IRI has been withholding and remitting the appropriate amount [of employment taxes] since 2007."

Although Davis raises the specter of "the possibility of fraud and misuse of funds" in its draft report, it expressly concludes that "evidence of possible fraud or abuse was not indicated by tax withholdings as unallowable under the Cooperative Agreement.

In sum, IRI fully understood its obligations to withhold tax from its employees, and documented that it did so within the framework of robust institutional controls ensuring financial oversight. For the above reasons, IRI believes that the proposed Finding is not supportable and that the "material weakness" designation is not justified.

Finding Number: **IRI 3**

Audit Area: **Significant Deficiency in Internal Control - Employee payments Unsupported Costs**

<u>Management Response</u>

"Finding Number IRI 3" of the Draft Audit Report states that IRI did not verify certain payments with the requisite supporting documentation as to one local employee. Based on this Finding, the Draft Audit Report recommends that IRI refund $938 (including indirect costs as described above) and that IRI "ensure that no other unsubstantiated costs related to employees are billed to USAID."

As described in the Draft Audit Report, IRI provided an allowance of up to $100 per month for health and education allowances as part of the compensation package for its local national employees. IRI believes that these allowances are appropriate and consistent with the local market. In the case of one employee, IRI paid the allowance several times, but IRI could not locate documentation from the employee confirming the employee's actual incurrence of health and education costs.

IRI does not agree with the calculation of the questioned cost in the Draft Audit Report. Rather than determining the actual amount, the Draft Audit Report simply assumes an amount of $100 per month for the entire period of the employment contract, or eight months. According to IRI records, however, IRI provided the $100 allowance between the months of November 2012 and March 2013, with a partial allowance of $86 in April 2013. IRI did not provide any other allowance funds to the employee. Therefore, a correct calculation of this finding would be $721 ($586 in direct costs plus $131 for 22.28% IRI indirect c costs plus $4 for 0.56% CEPPS indirect costs).

IRI also does not believe that the facts related to this one instance support Davis' decision to describe this as a "Significant" deficiency in internal controls, especially since the Risk Level is deemed "Low." IRI also views as unnecessary the recommendation that it "ensure no other unsupported costs related to all IRI employees are billed to USAID" because this is the long-established policy of IRI.

Finding Number: **NDI 1**

Audit Area: **Material Non-Compliance -Purchase of Business Class Airfares – Unallowable Costs**

Management Response

The auditors disallowed costs relating to four business class airfares, claiming the reason for business class was not supported by OMB A-122 and further stating that they were not in line with NDI's own policy on business class travel.

NDI only uses business class on a limited basis; an overwhelming number of flights going to and from Afghanistan were taken under economy class. In line with OMB A-122, NDI's travel policy allows for the use of business class with prior internal authorization and justification. For further clarity on the "excessively prolonged travel," criteria referenced in OMB A-122, NDI and many other organizations refer to the Federal Travel Regulations (FTR) and establish a "14-hour rule" as a baseline for defining excessively prolonged travel. NDI's travel policy allows the use of business class if: "The scheduled flight time, including stopovers and plane changes, exceeds 14 hours, AND an additional compelling circumstance exists that necessitates the use of business class service. A compelling circumstance includes, but is not limited to: urgency or frequency of travel; an imperative to operate on the ground immediately upon arrival or a short duration of stay." NDI notes that this policy is consistent with industry standards, and, in fact, is more stringent than the FTR in that NDI requires a "compelling circumstance" rather than simply "work on the following day or sooner" in addition to travel in excess of 14-hours.

Based on a review of the four trips, NDI believes that all four were taken in compliance with its travel policy. However, NDI recognizes that the time spent by two of the travelers during a required layover in Dubai could be perceived as a full rest stop and therefore could have precluded those travelers from traveling business class.

However, the additional two trips were in compliance with NDI's travel policy without a full rest stop, and, therefore, the full costs for the tickets should be considered allowable. Below please find additional details on those two trips.

Trip costing $9,843.90: *This ticket was for a business class flight departing Washington, D.C. on September 20, 2013 and arriving in Kabul on September 22, 2013. As documented in NDI's travel authorization (TA) form, the trip exceeded 14 hours, did not have an overnight stop, and included a compelling circumstance that the* *traveler needed to perform essential security-related assessments on the ground immediately upon arrival (in addition, his stay was very short). This traveler arrived in Dubai at 3:35pm, September 21, 2013, and was required to be in the airport shortly after midnight for a 3:30 a.m. flight to Kabul on September 22. Therefore, in NDI's judgment, this did not constitute a rest stop or overnight stay. The purpose of the trip was to conduct a security assessment, including the security of having travelers arrive on the earliest flight into Kabul in the morning (previously deemed unsafe due to attacks), therefore the traveler was required to take a flight arriving in Kabul at 6:50 a.m. and it was essential that he be well rested and able to make sensitive judgments regarding the security situation immediately upon his arrival in Kabul.*

<u>Trip costing $7,292.79:</u> This ticket was for an economy class flight out of Washington, D.C. but the return from Kabul to D.C. was on business class. The return trip was an overnight flight lasting 14 hours and 20 minutes, arriving in Washington, D.C. at 6:30 a.m. The traveler was required to work that same day to prepare for a high-level event the following day. Therefore, as documented in the TA form, this trip also qualified under NDI's travel policy as it exceeded 14 hours, did not have an overnight stop, and included a compelling circumstance that the traveler needed to operate on the ground immediately upon arrival.

In conclusion, NDI maintains that the cost of the two tickets described above should be an allowable cost in full and requests your consideration of these facts.

Finding Number: **NDI 2**
Audit Area: **Significant Deficiency in Internal Control - Shared Costs Over-Charged to Election Project – Unallowable Costs**

<u>Management Response</u>

NDI concurs that the incorrect percentages for cost allocations between multiple grants were applied to three transactions. NDI will correct the allocation of costs for these transactions, resulting in a credit to USAID for Cooperative Agreement #306-A-00-08-00529-00.

However, NDI believes it has a strong system of internal control regarding the allocation of costs between multiple grants. Cost allocations for charges are reviewed on a detailed level for accuracy and reasonableness. NDI notes that the questioned costs are not significant relative to NDI's costs for the period of the audit.

Finding Number: **IFES 1**
Audit Areas: **Material Non-Compliance - Competitive Bid Process**

Auditor Further Response

Along with their Management Response, IFES submitted additional documentation in the form of a Modification Proposal which contains much of the same information and justifications contained in the Management Response. While the Modification Proposal does specifically request approval from USAID to enter into a subcontract for Security Services with Garda World, there is no documentation of direct approval from USAID accepting the selection of Garda World through a sole source selection process. Despite the subsequent adoption of Modification 4 as proposed, the modification makes no reference to the selection of Garda World. For an award of this size, there must be strong documentation for this selection. This documentation must include the explicitly expressed approval of the selection from USAID.

Regarding the $3,320 paid to an IT support contractor during the period under audit, we maintain that the prior-existing relationship between IFES and the subcontractor is not a proper justification for the lack of a competitive bid process.

In order to comply with Federal Regulations as stated in the Criteria section of Finding IFES 2 as well as IFES' own Field Office Policies and Procedures Manual, any subcontracts awarded exceeding the $5,000 threshold should be subject to a formal competitive bid process.

The entirety of our finding, recommendation and questioned costs will remain.

Finding Number: **IFES 2**

Audit Areas: **Material Weakness in Internal Control and Ineligible Costs - Currency Exchange Rates**

Auditor Further Response

We appreciate IFES’ concurrence with our finding number IFES 2.

Finding Number: **IRI 1**

Audit Area: **Material Non-Compliance with Local Tax Law Provision and Incurring Additional Costs in Tax Payments**

Auditor Further Response

Payment of $76,512 in back taxes: IRI repeatedly stated that they were confused about the applicability of the Afghanistan income tax law passed in 2009 on IRI's operations. However, the Afghanistan income tax law was initially passed in 2005 and subsequently amended in 2009. The law has included the provisions for salaries withholding tax since 2005. An income tax manual was issued by the Ministry of Finance in 2010 that provided detailed illustrations of how various taxes are applicable to local and foreign entities operating in Afghanistan. As a result of the income tax law, all entities were required to fully comply with local tax law and almost all entities in Afghanistan (including other CEPPS partners) were in compliance with all provisions of the Afghanistan income tax law.

Additionally, IRI as a tax exempt organization is fully exempt from income tax (taxes on IRI revenue), but is not exempt from withholding payroll taxes and BRT taxes imposed on its contractors' payments. As described under the Condition section of Finding IRI 1, IRI neglected to withhold taxes from March 2009 to March 2012 from its local national employees' salaries and contractors' payments, as was required by the income tax law. As a result of IRI's failure to perform its legal obligation under the income tax law, IRI employees and contractors owed $76,512 to the Afghan government, as determined by the independent legal consultant. However, IRI paid the $76,512 in outstanding taxes to the Afghan government instead of making an effort to recover this tax money from its employees and contractors and charged the full amount to USAID. Had IRI been fully compliant with article 58 and 72 of the income tax law, this cost would not have been incurred by IRI.

With regard to IRI's references to USAID approval of this tax payment, we were not provided with any documentation showing USAID's explicit approval for the payment and subsequent billing of these taxes. Therefore, we maintain that this cost and associated indirect costs are unallowable.

Payment of $18,004 in BRT taxes: We maintain that IRI incurred unnecessary costs by adding an additional 2% tax on top of their payments to Pilgrims rather than withholding 2% from the agreed upon price of services. We believe that the tax code, detailed in the Criteria section of Finding IRI 1, is clear in regards to the responsibility of the contractor (IRI) to withhold the taxes from its payments to the subcontractor (Pilgrims) and then remit those amounts directly to the government.

Regardless of the results of the ongoing audit of Pilgrims, we believe the cost to be unallowable.

In conclusion, our finding, recommendation and the questioned costs amount will remain.

Finding Number: **IRI 2**

Audit Area: **Material Weakness in Internal Control - Salary Withholding Taxes**

<u>Auditor Further Response</u>

We disagree with IRI's response that IRI properly recorded and had robust internal control over salary withholding tax. When we inquired about these processes during our fieldwork, IRI's U.S. based staff was unaware of how local employee taxes were withheld and they were not able to provide documentation and confirm whether any tax was withheld from their local employees. One month after our fieldwork at IRI, on January 11, 2015, IRI provided an excel spreadsheet and a scanned copy of a tax deposit slip, which was not supported by an IRI payment voucher properly authorizing the payment of salary withholding tax. In addition, the tax calculation in the spreadsheet maintained by IRI's office manager was not signed or dated. Furthermore, the signed local payroll sheet did not demonstrate the withholding of salary tax and the tax payments were not recorded in IRI's official accounting system – Quicken.

In its letter dated December 18, 2014, IRI stated, "*because the employees were responsible for the filing of their taxes, the transactions for employee withholding were not recorded in the accounting software, the accounting records simply show the amount for the gross salary payment*." This is contrary to Article 61.1a of the Afghanistan Income Tax Manual which tasks IRI with certain reporting obligations with respect to wage withholding. It states, "*a) Every year, the employer must prepare an Annual Salary and tax Statement for each employee subject to wage withholding*." IRI failed to provide documentation showing that they have fully complied with this requirement of the income tax law. Therefore, we retain our finding and recommendation.

Finding Number: **IRI 3**

Audit Area: **Significant Deficiency in Internal Control - Employee Payments Unsupported Costs**

Auditor Further Response

The Management Response from IFES claims that the actual amount paid to the employee for a health and education allowance was only $586 rather than the $800 stated in our finding. However, we have not been provided with any additional documentation that would lead us to adjust the questioned amount based on our observations during testing. Therefore, we are not able to adjust our finding nor are we able to reduce the questioned amount.

Finding Number: **NDI 1**

Audit Area: **Material Non-Compliance -Purchase of Business Class Airfares – Unallowable Costs**

Auditor Further Response

NDI has not been able to provide sufficient justification in support of the purchase of business class airfare. All four travel authorizations were accompanied by a brief note stating "*Need to immediately commence working upon arrival*". However, the compelling circumstance for each trip was not adequately described nor documented during the procurement phase to justify the purchase of these business class plane tickets.

Additionally, we believe NDI's purchase of business class airfare in August 2013 was not prudent, as required by OMB–A122 Attachment A.3.c-d, and results in a significant amount of excessive costs to the U.S. Government. Considering the fact that these tickets were booked well in advance of the trips, we believe NDI could have avoided incurring extra and excessive travel costs by making travel arrangements where the travelers could arrive at their destination cities one day earlier and not need to work immediately upon arrival. Moreover, the travelers did not arrive any sooner at their destination cities, despite purchasing business class airfare.

Furthermore, we only questioned the costs that we believe to be in excess of a reasonable coach class ticket for each individual itinerary. Therefore, we retain our finding and the questioned amount.

Finding Number: **NDI 2**
Audit Area: **Significant Deficiency in Internal Control - Shared Costs Over-Charged to Election Project – Unallowable Costs**

Auditor Further Response

We appreciate NDI’s concurrence to correct the three cost allocation errors noted in our finding and fully implement our recommendation accordingly, notwithstanding the significance of the amount we questioned.

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