

July 2011

AFGHANISTAN

Actions Needed to Improve Accountability of U.S. Assistance to Afghanistan Government

U.S. Government Accountability Office



YEARS

1921-2011

ACCOUNTABILITY ★ INTEGRITY ★ RELIABILITY

Report Documentation Page				Form Approved OMB No. 0704-0188	
Public reporting burden for the collection of information is estimated to average 1 hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to Washington Headquarters Services, Directorate for Information Operations and Reports, 1215 Jefferson Davis Highway, Suite 1204, Arlington VA 22202-4302. Respondents should be aware that notwithstanding any other provision of law, no person shall be subject to a penalty for failing to comply with a collection of information if it does not display a currently valid OMB control number.					
1. REPORT DATE JUL 2011		2. REPORT TYPE		3. DATES COVERED 00-00-2011 to 00-00-2011	
4. TITLE AND SUBTITLE Afghanistan: Actions Needed to Improve Accountability of U.S. Assistance to Afghanistan Government				5a. CONTRACT NUMBER	
				5b. GRANT NUMBER	
				5c. PROGRAM ELEMENT NUMBER	
6. AUTHOR(S)				5d. PROJECT NUMBER	
				5e. TASK NUMBER	
				5f. WORK UNIT NUMBER	
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES) U.S. Government Accountability Office, 441 G Street NW, Washington, DC, 20548				8. PERFORMING ORGANIZATION REPORT NUMBER	
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)				10. SPONSOR/MONITOR'S ACRONYM(S)	
				11. SPONSOR/MONITOR'S REPORT NUMBER(S)	
12. DISTRIBUTION/AVAILABILITY STATEMENT Approved for public release; distribution unlimited					
13. SUPPLEMENTARY NOTES					
14. ABSTRACT					
15. SUBJECT TERMS					
16. SECURITY CLASSIFICATION OF:			17. LIMITATION OF ABSTRACT Same as Report (SAR)	18. NUMBER OF PAGES 48	19a. NAME OF RESPONSIBLE PERSON
a. REPORT unclassified	b. ABSTRACT unclassified	c. THIS PAGE unclassified			

Why GAO Did This Study

The U.S. Agency for International Development (USAID) and the Department of Defense (DOD) award direct assistance to Afghanistan, using bilateral agreements and multilateral trust funds that provide funds through the Afghan national budget. GAO assessed (1) the extent to which the United States, through USAID and DOD, has increased direct assistance, (2) USAID and DOD steps to ensure accountability for bilateral direct assistance, and (3) USAID and DOD steps to ensure accountability for direct assistance via multilateral trust funds for Afghanistan. GAO reviewed USAID, DOD, and multilateral documents and met with U.S. officials and staffs of multilateral trust funds in Washington, D.C., and Afghanistan.

What GAO Recommends

GAO recommends that USAID (1) establish and implement policy requiring risk assessments in all cases before awarding bilateral direct assistance funds, (2) take additional steps to help ensure it implements controls for bilateral direct assistance, and (3) ensure adherence to its risk assessment policies for ARTF. In commenting on the first recommendation, USAID stated that its existing policies call for some form of risk assessment for all awards and that it has taken new steps to ensure risk assessment. GAO retained its recommendation because existing USAID policies do not require preaward risk assessments in all cases. USAID concurred with GAO's other recommendations.

AFGHANISTAN

Actions Needed to Improve Accountability of U.S. Assistance to Afghanistan Government

What GAO Found

The United States more than tripled its awards of direct assistance to Afghanistan in fiscal year 2010 compared with fiscal year 2009. USAID awards of direct assistance grew from over \$470 million in fiscal year 2009 to over \$1.4 billion in fiscal year 2010. USAID awarded \$1.3 billion to the World Bank-administered Afghanistan Reconstruction Trust Fund (ARTF) in fiscal year 2010, of which the bank has received \$265 million as of July 2011. DOD direct assistance to two ministries grew from about \$195 million in fiscal year 2009 to about \$576 million in fiscal year 2010, including contributions to fund police salaries through the United Nations Development Program-administered (UNDP) Law and Order Trust Fund for Afghanistan (LOTFA).

USAID and DOD have taken steps to help ensure the accountability of their bilateral direct assistance to Afghan ministries, but USAID has not required risk assessments in all cases before awarding these funds. For example, USAID did not complete preaward risk assessments in two of the eight cases GAO identified. Although current USAID policy does not require preaward risk assessments in all cases, these two awards were made after the USAID Administrator's July 2010 commitment to Congress that USAID would not proceed with direct assistance to an Afghan public institution before assessing its capabilities. In these two cases, USAID awarded \$46 million to institutions whose financial management capacity were later assessed as "high risk." USAID has established various financial and other controls in its bilateral direct assistance agreements, such as requiring separate bank accounts and audits of the funds. USAID has generally complied with these controls, but GAO identified instances in which it did not. For example, in only 3 of 19 cases did USAID document that it had approved one ministry's prefinancing contract documents. DOD personnel in Afghanistan assess the risk of providing funds to two security ministries through quarterly reviews of each ministry's capacity. DOD officials also review records of ministry expenditures to assess whether ministries have used funds as intended. DOD established formal risk assessment procedures in June 2011, following GAO discussions with DOD about initial findings.

USAID and DOD generally rely on the World Bank and UNDP to ensure accountability over U.S. direct assistance provided multilaterally through ARTF and LOTFA, but USAID has not consistently complied with its risk assessment policies in awarding funds to ARTF. For example, in March 2010, USAID did not conduct a risk assessment before awarding an additional \$1.3 billion to ARTF. During GAO's review, DOD established procedures in June 2011 requiring that it assess risks before contributing funds to LOTFA. The World Bank and UNDP use ARTF and LOTFA monitoring agents to help ensure that ministries use contributions as intended. However, security conditions and weaknesses in Afghan ministries pose challenges to their oversight. For example, the ARTF monitoring agent recently resigned due to security concerns. The World Bank is now seeking a new monitoring agent and does not anticipate a gap in monitoring. In addition, weaknesses in the Ministry of Interior's systems for paying wages to police challenge UNDP efforts to ensure that the ministry is using LOTFA funds as intended.

Contents

Letter		1
	Background	3
	The United States More Than Tripled Its Awards of Direct Assistance to Afghanistan in 2010 through USAID and DOD	6
	USAID and DOD Have Taken Steps to Help Ensure Accountability over Bilateral Direct Assistance, but USAID Has Not Required Risks to Be Assessed in Advance in All Cases	9
	USAID Has Not Consistently Assessed Risks of Contributions to ARTF, While DOD Has Recently Established Risk Assessment Guidance for LOTFA	18
	Conclusion	26
	Recommendations for Executive Action	27
	Agency Comments and Our Evaluation	27
Appendix I	Objectives, Scope, and Methodology	32
Appendix II	Comments from the U.S. Agency for International Development	36
Appendix III	GAO Contact and Staff Acknowledgments	43
Tables		
	Table 1: U.S. Allocations of Funds to Reconstruct Afghanistan, Fiscal Years 2002-2010	3
	Table 2: USAID Direct Assistance to Afghanistan, Fiscal Years 2009-2010	8
	Table 3: USAID Preaward Risk Assessments for Bilateral Direct Assistance	10
	Table 4: USAID Compliance with Selected Controls in Its Bilateral Direct Assistance Agreements, as of February 15, 2011	13
	Table 5: USAID Documentation of Approvals of Procurement Steps in Contracts Awarded under USAID-Financed Programs	15
Figures		
	Figure 1: Changes in the Levels of U.S. Direct Assistance Awards and Contributions, Fiscal Years 2009-2010	6

Figure 2: U.S. Direct Assistance Awards and Contributions, Fiscal
Year 2010

7

Abbreviations

ADS	Automated Directives System
ANA	Afghan National Army
ANP	Afghan National Police
ARTF	Afghanistan Reconstruction Trust Fund
CAO	Control and Audit Office
CSTC-A	Combined Security Transition Command—Afghanistan
DOD	Department of Defense
LOTFA	Law and Order Trust Fund for Afghanistan
MAIL	Ministry of Agriculture, Irrigation, and Livestock
MOD	Ministry of Defense
MOF	Ministry of Finance
MOI	Ministry of Interior
PIO	Public International Organization
SIGAR	Special Inspector General for Afghanistan Reconstruction
State	Department of State
Treasury	Department of the Treasury
UNDP	United Nations Development Program
USAID	U.S. Agency for International Development

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.



United States Government Accountability Office
Washington, DC 20548

July 20, 2011

Congressional Addressees

Since 2002, the United States has allocated about \$56 billion for programs to reconstruct Afghanistan. In January 2010, the Department of State (State) announced that the United States would lessen its reliance on contractors to implement reconstruction programs by providing more funds to the Afghan government itself. The United States also joined other donors in 2010 by pledging that within the next 2 years it would provide 50 percent or more of its Afghan development aid through the Afghan government's national budget. Such direct assistance is intended to help develop the capacity of Afghan government ministries. Direct assistance is currently being provided by two U.S. agencies, according to U.S. officials. The U.S. Agency for International Development (USAID) and the Department of Defense (DOD) do so (1) through bilateral agreements with individual Afghan ministries and (2) by providing funds to multilateral trust funds administered by the World Bank and the United Nations Development Program (UNDP). The prospect of increasing U.S. direct assistance to Afghanistan raises the issue of the accountability for such assistance.

We performed our work under the authority of the Comptroller General to conduct work on GAO's initiative because of broad congressional interest in the oversight and accountability of U.S. funds provided to Afghanistan. We assessed (1) the extent to which the United States, through USAID and DOD, has increased its direct assistance to Afghanistan, (2) USAID and DOD steps to ensure accountability for bilateral direct assistance, and (3) USAID and DOD steps to ensure accountability for direct assistance to multilateral trust funds in Afghanistan.

To address these objectives, we reviewed State, USAID, and DOD documents. We interviewed officials from the U.S. Department of the Treasury, State, USAID, DOD, and the World Bank in Washington, D.C., and Kabul, Afghanistan, as well as UNDP officials in Kabul. To identify the extent to which USAID and DOD had increased the level of direct assistance from fiscal year 2009 to fiscal year 2010, we obtained financial information from (1) USAID's mission in Kabul, Afghanistan, and (2) the Office of the Under Secretary of Defense (Comptroller). We determined these data to be sufficiently reliable for our purposes. We focused on awards or contributions of U.S. funds that are channeled through the Afghan government national

budget for use by Afghan ministries or other government entities, consistent with USAID and DOD definitions and practices.¹

To assess steps taken by USAID and DOD to help ensure the accountability of their bilateral and multilateral direct assistance to the Afghan government, we reviewed the policies and practices the agencies use to assess risks associated with direct assistance and to establish control mechanisms over the use of direct assistance funds. We applied criteria drawn from GAO's *Standards for Internal Control in the Federal Government*,² which defines risk assessment and control activities as key elements of an internal control framework to provide reasonable assurance that agency assets are safeguarded against fraud, waste, abuse, and mismanagement. Risk assessment includes identifying internal and external risks an organization faces and their potential effect. Control activities are the policies and procedures (such as approvals, reconciliations, and reviews) agencies implement to mitigate identified risks and are essential for accountability of government resources. We also used criteria from USAID and DOD guidance concerning direct assistance.

We conducted this performance audit from August 2010 to July 2011 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Details on our objectives, scope, and methodology are contained in appendix I.

¹DOD currently uses the term "direct contributions" to describe its direct assistance programs. For the purposes of this report, we are using the term "direct assistance" to describe both USAID and DOD programs that provide funds to Afghan government entities through the national budget. We did not include the State-funded Good Performer's Initiative because State officials informed us that State has not provided funds for this program through the Afghan government's national budget.

²GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

Background

Decades of conflict have left Afghanistan a poor nation with high illiteracy, weak government institutions, and a high level of corruption. According to Transparency International's index of perceived corruption, Afghanistan is tied with Burma as the world's second most corrupt nation.³ The United States has allocated about \$56 billion for fiscal years 2002 to 2010 to reconstruct Afghanistan, as shown in table 1.⁴ The United States allocated nearly half of these funds—about \$27 billion—in fiscal years 2009 and 2010 alone. For fiscal year 2011, DOD has allocated more than \$12.6 billion in additional funds for Afghan reconstruction. While the allocation of fiscal year 2011 State and USAID funds for Afghanistan had not been finalized as of June 2011, State's fiscal year 2011 budget request included more than \$5 billion for Afghan international affairs programs and operations.

Table 1: U.S. Allocations of Funds to Reconstruct Afghanistan, Fiscal Years 2002-2010

Dollars in millions										
Program category	2002	2003	2004	2005	2006	2007	2008	2009	2010	Total
International affairs programs ^a	890.4	764.3	1,969.0	2,749.0	1,061.2	1,909.6	2,211.5	2,770.9	4,177.9	18,503.8
International affairs operations ^b	31.7	35.3	119.8	136.1	131.9	210.2	448.8	1,073.5	1,728.2	3,915.5
Department of Defense and other ^c	0.6	167.9	401.7	1,946.1	2,311.1	8,008.2	3,476.4	6,453.1	10,755.9	33,521.0
Total	922.7	967.5	2,490.5	4,831.2	3504.2	10,128.0	6,136.7	10,297.5	16,662.0	55,940.3

Source: GAO analysis of Office of Management and Budget financial data.

^aThe category "international affairs programs" includes funds for economic support; foreign military financing; law enforcement; global health/child survival; anti-terrorism activities; and development, migration, and disaster assistance.

^bThe category "international affairs operations" includes funds for diplomatic and consulate operations, building operations, and inspectors general operations.

^c"Other" includes funding for training and equipping Afghan security forces and counternarcotics activities.

³Transparency International's corruption perceptions index included 178 nations and can be viewed at http://www.transparency.org/policy_research/surveys_indices/cpi/2010/results.

⁴For the purposes of this report, the term "allocations" includes funds that Congress has specifically appropriated for Afghan reconstruction, as well as additional funds that executive branch agencies have allocated for Afghan reconstruction from other appropriations.

In 2009, the executive branch adopted the Integrated Civilian-Military Campaign Plan to guide U.S. reconstruction activities in Afghanistan.⁵ The plan, which is currently being updated, categorizes reconstruction activities in terms of three overarching lines of effort—development, governance, and security. State officials have informed us that U.S. agencies do not track Afghan reconstruction funds by the lines of effort.⁶

U.S. agencies have used various means to implement Afghan reconstruction projects with these funds. In some cases, they have hired contractors and nongovernment organizations. In other cases, U.S. reconstruction funds have been provided directly to the Afghan government's national budget to be used by Afghan ministries and other government entities.

In 2010, the United States announced plans to increase direct assistance to Afghanistan. In January 2010, the Secretary of State announced that the United States would increase direct assistance to the Afghan government to help Afghan ministries and other government entities build their capacity to manage funds. At two international conferences in 2010, the United States and other donors pledged to provide half or more of their development aid in the form of direct assistance to the Afghan government within 2 years, contingent on Afghan actions to reduce corruption and strengthen public financial management capacity.⁷ In February 2011, DOD formally authorized direct contributions of DOD funds to two Afghan security ministries to build their capacity and support Afghan security forces.

USAID awards direct assistance to Afghanistan through two means. It awards direct assistance to several Afghan government entities through

⁵See GAO, *The Strategic Framework for U.S. Efforts in Afghanistan*, [GAO-10-655R](#) (Washington, D.C.: June 15, 2010).

⁶We requested a breakout of Afghan reconstruction funds in terms of the Integrated Civilian-Military Campaign Plan's lines of effort from State officials in August 2010. In February 2011, officials at the U.S. embassy in Kabul, Afghanistan, told us that they planned to develop such a presentation. We intend to pursue this matter as part of our upcoming review of the revised campaign plan (Public Law 111-84, *National Defense Authorization Act for Fiscal Year 2010*, Sec. 1226 – *Reports on Campaign Plans for Iraq and Afghanistan*).

⁷GAO is currently reviewing U.S. government efforts to build the capacity of the Afghan government's public financial management system and expects to issue a report on this subject in late 2011.

bilateral agreements overseen by its mission in Afghanistan. These entities include the Independent Directorate for Local Governance and the ministries of Agriculture, Irrigation, and Livestock; Communications and Information Technology; Finance; Public Health; and Transport and Civil Aviation. Some of the bilateral agreements finance Afghan government procurement of goods and services, while others fund a range of other government expenses and activities, including operating costs, salaries, agricultural development programs, and infrastructure projects. USAID also provides direct assistance by awarding funds to the multilateral World Bank-administered Afghanistan Reconstruction Trust Fund (ARTF). ARTF was established in 2002 as a vehicle for donors to pool resources and coordinate support for Afghanistan's reconstruction. As of April 2011, 32 donors had contributed about \$4.3 billion to ARTF. ARTF provides these funds through the Afghan government national budget to finance the government's recurrent operating costs (e.g., wages for civil servants, operations and maintenance costs) and national development programs.

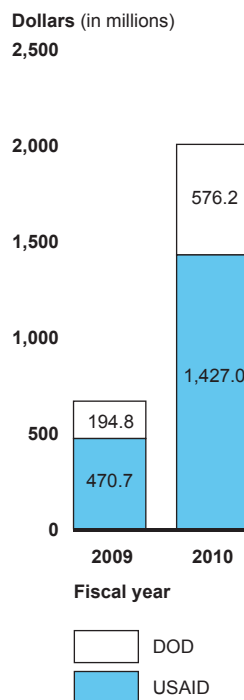
DOD provides direct assistance bilaterally to Afghanistan's Ministry of Defense (MOD) and Ministry of Interior (MOI) through contributions of funds overseen by DOD's Combined Security Transition Command–Afghanistan (CSTC-A).⁸ According to DOD guidance, these contributions are used to procure food, salaries, goods, services, and minor construction in direct support of the Afghan National Army (ANA) and the Afghan National Police (ANP). CSTC-A also contributes funds to the multilateral UNDP-administered Law and Order Trust Fund for Afghanistan (LOTFA), which receives contributions from several donor nations. Most LOTFA funds are used to provide salaries to ANP personnel.

⁸CSTC-A oversees the U.S. role in developing the Afghan National Security Forces. MOD is responsible for the Afghan National Army, while MOI is responsible for the Afghan National Police.

The United States More Than Tripled Its Awards of Direct Assistance to Afghanistan in 2010 through USAID and DOD

The United States more than tripled its awards and contributions of USAID and DOD direct assistance funds to the Afghan government in fiscal year 2010 compared with fiscal year 2009 (see fig. 1).

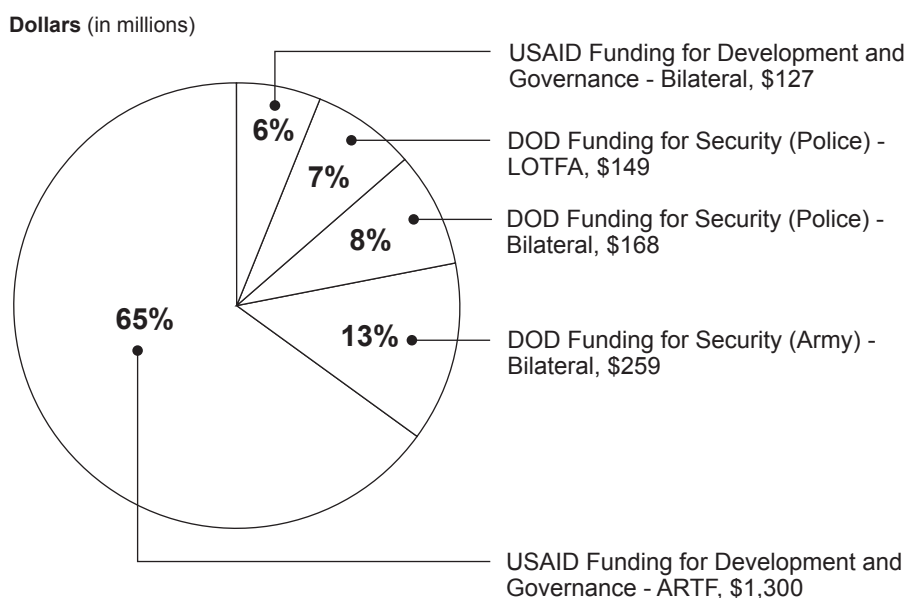
Figure 1: Changes in the Levels of U.S. Direct Assistance Awards and Contributions, Fiscal Years 2009-2010



Source: GAO analysis of USAID and DOD data.

In fiscal year 2010, most of the direct assistance funds (about 71 percent) were awarded by USAID for activities related to development and governance, either bilaterally (about 6 percent) or through preferred contributions to ARTF (about 65 percent), as shown in figure 2. For example, USAID has contributed funding to a community development and local governance program that is being implemented in all of Afghanistan's 34 provinces through ARTF. The remainder was contributed by DOD for security assistance, either bilaterally to MOD and MOI or through LOTFA.

Figure 2: U.S. Direct Assistance Awards and Contributions, Fiscal Year 2010



Source: GAO analysis of USAID and DOD data.

Note: Percentages may not add to 100 percent due to rounding.

As shown in table 2, USAID awards of direct assistance to Afghanistan increased from over \$470 million in fiscal year 2009 to more than \$1.4 billion in fiscal year 2010. These awards included a \$1.3 billion grant to ARTF, more than triple what it awarded to ARTF in 2009.⁹ USAID may obligate and disburse funds awarded to an Afghan entity or trust fund over multiple years, depending on the agreement's terms.¹⁰

⁹According to USAID, the \$1.3 billion award represented an increase in the ceiling of the grant to streamline the process for future contributions.

¹⁰For example, the World Bank informed us that as of July 2011 it had received \$265 million of the \$1.3 billion award. It also stated that it had received \$972 million in all from USAID from 2002 through July 2011. The total estimated value of USAID awards to the ARTF during that period was greater than \$2 billion. In contrast, DOD direct assistance contributions are awarded, obligated, and disbursed in close succession, according to the Office of the Under Secretary of Defense (Comptroller). For the value of each USAID award, we used what USAID refers to as the "total estimated contribution" that it has committed to provide, subject to the availability of funds in signing a direct assistance agreement. For the date, we used each agreement's signature date as the effective date of the award.

Table 2: USAID Direct Assistance to Afghanistan, Fiscal Years 2009-2010

Dollars in millions

Recipient	Program/project	Fiscal year 2009 awards	Fiscal year 2010 awards
Independent Directorate for Local Governance	District Delivery Program	\$0	\$40
Ministry of Agriculture, Irrigation, and Livestock	Agricultural Development Fund	0	85
Ministry of Finance	Salary Support Program	0	2
Ministry of Finance	Civilian Technical Assistance Plan	30	0
Ministry of Communications and Information Technology	Policy Capacity Initiative	1	0
Ministry of Public Health	Partnership Contracts for Health Services	18.2	0
World Bank	Afghanistan Reconstruction Trust Fund	421.5	1,300
Total		\$470.7	\$1,427

Source: GAO analysis of USAID data.

DOD direct assistance to MOD and MOI, including contributions to LOTFA, grew from about \$195 million in fiscal year 2009 to about \$576 million in fiscal year 2010. DOD contributions to LOTFA more than doubled from about \$68 million in fiscal year 2009 to about \$149 million in fiscal year 2010.¹¹

¹¹During 2009 and 2010, State's Bureau for International Narcotics and Law Enforcement Affairs contributed about \$12 million to LOTFA to support Afghan prison guards.

USAID and DOD Have Taken Steps to Help Ensure Accountability over Bilateral Direct Assistance, but USAID Has Not Required Risks to Be Assessed in Advance in All Cases

Risk assessments and internal controls to mitigate identified risks are key elements of an internal control framework to provide reasonable assurance that agency assets are safeguarded against fraud, waste, abuse, and mismanagement.¹² USAID conducted preaward risk assessments in most cases. However, we found that USAID's policies for assessing direct assistance risks do not require preaward risk assessments in all cases. USAID has not updated its policies to reflect the USAID Administrator's July 2010 commitment to Congress that USAID would assess all Afghan public institutions before providing them with direct assistance. We found that in August 2010 and January 2011, USAID did not complete preaward risk assessments before awarding funds to two Afghan government entities. USAID has established various financial and other controls in its bilateral direct assistance agreements with ministries that go beyond what is required by its policies. However, it has not always ensured compliance with those controls. DOD personnel in Afghanistan have assessed the risk of providing funds to MOD and MOI through quarterly reviews of each ministry's capacity. DOD established formal procedures on risk assessment for Afghan direct assistance in June 2011 after we informed DOD officials that DOD lacked such procedures. DOD officials also stated that they review records of MOD and MOI expenditures to assess whether funds have been used as intended, as required by DOD policies established in February 2011.

USAID Has Conducted Preaward Risk Assessments in Most Cases

USAID mission staff have complied with USAID risk assessment policies for awarding bilateral direct assistance funds to finance Afghan procurement activities under what USAID refers to as a host country contract. USAID policies, as outlined in its Automated Directives System (ADS), require USAID staff to conduct a preaward risk assessment for a host government entity if the entity is to use the award to procure goods and services.¹³ Specifically, staff are required under ADS to (1) assess the entity's procurement system and (2) obtain the Mission Director's certification of the entity's capability to undertake the procurement. Of USAID's eight bilateral direct assistance agreements, we identified two involving the financing of Afghan procurement activities. In both cases, we found that USAID mission staff, in compliance with ADS, had (1)

¹² [GAO/AIMD-00-21.3.1](#).

¹³ ADS 301.5.2 and 305.3. The preaward assessment requirement applies to cases in which USAID anticipates assigning a host government entity a procurement action to exceed \$250,000.

assessed the financial and procurement management capabilities of the Afghan recipients (the Ministry of Communications and Information Technology and the Ministry of Public Health) before awarding funds (see table 3) and (2) obtained the required certifications.

Of six bilateral direct assistance agreements that did not involve financing Afghan government procurement activities, we found that USAID had completed such assessments before awarding funds in four cases (see table 3). Although USAID did not conduct preaward assessments in two cases, it was in compliance with its risk assessment policies. Those policies state that USAID staff “should” assess the capacity (e.g., financial management, procurement, and personnel management capacity) of prospective recipients in cases that do not involve financing Afghan government procurement activities.

Table 3: USAID Preaward Risk Assessments for Bilateral Direct Assistance

Dollars in millions

Afghan government recipient	Program/project	Preaward risk assessment report date	Award date	Total award	Risk assessment completed before USAID awarded funds
Ministry of Transport and Civil Aviation	Regional Airports Project	March 2011	January 2011	\$6	No
Independent Directorate for Local Governance	District Delivery Program	January 2011	August 2010	40	No
Ministry of Agriculture, Irrigation, and Livestock	Agricultural Development Fund	June 2010	July 2010	85	Yes
Ministry of Finance	Transition Coordination Commission	July 2009	January 2011	0.45	Yes
	Salary Support Program	July 2009	June 2010	2	Yes
	Civilian Technical Assistance Plan	July 2009	September 2009	30	Yes
Ministry of Communications and Information Technology	Policy Capacity Initiative	May 2007 ^a	April 2009	1	Yes
Ministry of Public Health	Partnership Contracts for Health Services	July 2007 ^b	July 2008	18.2 ^c	Yes

Source: GAO analysis of USAID bilateral direct assistance agreements and pre-award assessments.

^aUSAID completed a follow-up assessment of the procurement management capabilities of the Ministry of Communications and Information Technology in March 2008.

^bUSAID also assessed the ministry’s financial management capabilities in October 2007 and revised it in May 2008.

^cThe total amount does not include a previous fiscal year 2008 award.

USAID Has Not Updated
Its Risk Assessment
Policies to Reflect the
Administrator's
Commitment to Assess All
Afghan Government
Recipients in Advance

USAID has not updated its risk assessment policies to reflect its Administrator's commitment that USAID would assess the capabilities of Afghan government recipients in all cases before awarding them direct assistance funds. On July 28, 2010, USAID's Administrator responded to concerns expressed by Members of the House Appropriations Committee's Subcommittee on State, Foreign Operations, and Related Programs regarding corruption and weak government capacity in Afghanistan by committing that USAID would not proceed with direct assistance to an Afghan public institution until USAID had ensured that the institution had an accountable organizational structure and sound financial management capabilities and met USAID standards. State's Office of the Special Representative for Afghanistan and Pakistan made a similar commitment in January 2010, when it stated that "to receive direct assistance, Afghan ministries must be certified as having improved accountability and transparency."¹⁴ However, we found that current USAID policy for direct assistance not involving the financing of Afghan government procurement activities does not require USAID to assess a prospective recipient's capacity to implement a proposed activity.¹⁵

We also found that following the Administrator's July 2010 commitment, USAID awarded direct assistance funds to two Afghan government recipients before completing risk assessments. As shown in table 3, USAID signed a \$40 million agreement with the Independent Directorate for Local Governance in August 2010, 5 months before completing an assessment of that entity.¹⁶ It also signed a \$6 million bilateral direct

¹⁴Department of State, Office of the Special Representative for Afghanistan and Pakistan, *Afghanistan and Pakistan Regional Stabilization Strategy* (January 2010 and updated February 2010).

¹⁵ADS 201.3.11.9.

¹⁶USAID also prepared a July 2010 memo to justify the provision of cash advances to the directorate, in which it identified potential risks and risk mitigation steps. With regard to the risk assessment report completed after USAID awarded funds to the directorate, the report did not focus on the directorate's capability to implement the funded project. It instead addressed a possible future directorate program. In November 2010, the USAID Office of Inspector General recommended to the mission that future reviews focus on the ministry's capacity to implement a specific proposed program (USAID, Office of Inspector General, Review of USAID/Afghanistan's Ministerial Assessment Process (Kabul, Afghanistan, Nov. 6, 2010)). In response, USAID mission officials stated that they had begun to assess ministries based upon specific programs and that assessments would be undertaken once host government entities were identified as appropriate partners and programs had been conceptualized.

assistance agreement with the Ministry of Transport and Civil Aviation in January 2011, 2 months before completing an assessment of the ministry.¹⁷ The completed risk assessments identified areas of high risk in both entities. For example, the Ministry of Transport and Civil Aviation was assessed as “high risk” in the four core function areas covered by the assessment—control environment, financial management and accounting, compliance with applicable laws and regulations, and accountability environment. Similarly, the Independent Directorate for Local Governance was assessed as “high risk” in 5 of 14 areas covered, including financial management and procurement. USAID officials told us that USAID awarded these funds before completing the risk assessments because the projects were urgently needed.

USAID Has Established Controls in Its Bilateral Direct Assistance Agreements but Has Not Always Ensured Compliance

USAID has established various financial and other controls in its bilateral direct assistance agreements, although USAID policies do not establish minimum standard conditions for such agreements, according to USAID officials. Shown in table 4 are selected examples of financial controls USAID has established within its bilateral direct assistance agreements. USAID also required Afghan government recipients to provide documentation demonstrating their compliance with the selected controls. As shown in table 4, in each applicable case, USAID ensured compliance with the selected controls.

¹⁷ USAID informed us in July 2011 that it did not disburse funds to the ministry until March 2011, the same month that the assessment report was completed.

Table 4: USAID Compliance with Selected Controls in Its Bilateral Direct Assistance Agreements, as of February 15, 2011

Afghan government recipient/program	Recipient must establish a separate, noncommingled bank account	Recipient must grant USAID access rights to the bank account	Recipient must have monitoring and evaluation plan	Recipient must comply with periodic reporting requirement	Recipient must maintain accounting books and records subject to audit
Ministry of Transport and Civil Aviation—Regional Airports Project	●	●	●	●	b
Independent Directorate for Local Governance—District Delivery Program	●	●	●	a	b
Ministry of Agriculture, Irrigation, and Livestock—Agricultural Development Fund	●	●	●	a	b
Ministry of Finance—Transition Coordination Commission	●	●	Not specified in agreement	Not specified in agreement	Not specified in agreement
Ministry of Finance—Salary Support Program	●	●	●	●	b
Ministry of Finance—Civilian Technical Assistance Plan	●	●	●	●	b
Ministry of Communications and Information Technology—Policy Capacity Initiative	●	Not specified in agreement	Not specified in agreement	Not specified in agreement	Not specified in agreement
Ministry of Public Health—Partnership Contracts for Health Services	●	Not specified in agreement	●	●	Not specified in agreement

● Control specified in agreement; USAID ensured compliance.

Source: GAO analysis of USAID bilateral direct assistance agreements and compliance documentation.

Notes: The five controls shown in table 4 were selected based on their reoccurrence across USAID bilateral direct assistance agreements. For GAO's methodology, see appendix I.

^aControl specified in agreement; USAID not able to ensure compliance pending disbursement of funds under the agreement (reporting is not required until after USAID has disbursed funds).

^bCompliance with this requirement could not be verified because USAID was in the process of conducting audits of Afghan entities' accounting books and records at the time of our review.

In two cases, USAID also hired contractors to help control risks identified in preaward assessments. For example, USAID's assessment of the Ministry of Agriculture, Irrigation, and Livestock (MAIL) determined that MAIL would not be able to independently manage and account for direct assistance funds. As a result, USAID awarded a \$49.1 million contract to a U.S.-based firm to establish a unit to manage a USAID-funded

agriculture development fund, to transition that unit to local control within 4 years, and to provide technical assistance. Similarly, USAID's October 2007 assessment of the Ministry of Public Health noted concerns that the ministry would continue needing technical assistance to effectively and efficiently manage donor funds. As a result, USAID amended an existing contract to an international nonprofit organization to improve the capacity of the ministry at the central level and in target provinces.¹⁸

USAID has also established procurement-specific controls in its bilateral direct assistance agreements with the Ministry of Communications and Information Technology and the Ministry of Public Health. These agreements provide funds to Afghan ministries to enter into contracts for goods and services and require USAID to monitor and approve certain steps of the procurement process for contracts over \$250,000, as applicable.¹⁹

While USAID generally complied with this requirement, USAID mission officials could not provide us with documentation showing that USAID had done so in all cases, as shown in table 5. Specifically, USAID mission officials either did not approve or document that they had approved prior to execution any of 6 contracts that the Ministry of Communications and Information Technology entered into (in table 5, see step 7 of the procurement process). In addition, USAID mission officials told us that USAID did not approve any of the ministry's 6 prefinancing contract documents (step 8 of the procurement process). USAID stated that no clearance or approval was provided because the final signed documents did not need concurrence. Similarly, USAID documented only three instances in which it had approved any of the Ministry of Public Health's 19 prefinancing contract documents. USAID also did not conduct follow-up reviews of the ministry to ensure its compliance with USAID contracting and financial management requirements, as called for in the assistance agreement.

¹⁸These contracts are not considered to be direct assistance and their costs are therefore not included in our totals of USAID's bilateral direct assistance.

¹⁹USAID ADS E305.5.1a, which applies when USAID finances contractual arrangements between another country and the supplier of goods or services, requires written USAID approval for certain steps in the contracting process for contracts over \$250,000. USAID's bilateral direct assistance agreements with the Ministry of Communications and Information Technology and the Ministry of Public Health contain the same requirement found in this ADS provision without mention of any financial threshold.

Table 5: USAID Documentation of Approvals of Procurement Steps in Contracts Awarded under USAID-Financed Programs

Procurement steps	Ministry of Communications and Information Technology—Policy Capacity Initiative	Ministry of Public Health—Partnership Contracts for Health Services
Step 1: notice to prospective offerors	4 of 4	19 of 19
Step 2: lists of prequalified offerors, if any, prior to issuance of the solicitation document	Not applicable	19 of 19
Step 3: complete solicitation document, prior to issuance	6 of 6	19 of 19
Step 4: the contractor selection method (may be part of the solicitation document)	6 of 6	19 of 19
Step 5: the selected contractor	6 of 6	19 of 19
Step 6: any decision to terminate negotiations with the highest ranked offeror and to initiate negotiations with the next ranked offeror or to reject all offers	Not applicable	2 of 2
Step 7: the contract, prior to execution	0 of 6	19 of 19
Step 8: signed contract documents, before financing	0 of 6	3 of 19
Step 9: contract administrative actions such as subcontracts, amendments, and change orders as determined by USAID	6 of 6	Not applicable

Source: GAO analysis of USAID documents.

USAID has taken steps to ensure that bilateral direct assistance awards are audited. USAID policy requires audits of recipients, including host government entities, that expend \$300,000 or more in USAID awards during a fiscal year. USAID has asserted its right to audit Afghan recipient use of funds in all of its bilateral direct assistance agreements, including those involving procurement. According to USAID mission officials, USAID has contracted with audit firms to initiate audits of three Afghan ministries (the Ministries of Finance, Communications and Information Technology, and Public Health) that disbursed a total of \$28.8 million in USAID awards in fiscal year 2010.

DOD Has Taken Steps to Help Ensure Accountability and Recently Established Procedures Requiring Risk Assessments

CSTC-A has recently established procedures that require CSTC-A personnel to assess the risks of direct assistance in advance of providing funds to Afghan ministries. On June 12, 2011, CSTC-A established standard operating procedures for direct assistance, as required under DOD guidance issued on February 4, 2011.²⁰ The CSTC-A procedures identify risk assessment as the first of four steps CSTC-A personnel must take before the direct contribution of the funds. CSTC-A adopted these procedures after we informed DOD officials that DOD lacked risk assessment guidance for bilateral direct assistance.

The CSTC-A procedures specify that the primary method CSTC-A is to use to assess risks is the Ministerial Development Board. The board oversees CSTC-A efforts to develop the capacity of MOD and MOI. CSTC-A officials informed us in January and February 2011 that CSTC-A has been using this method to assess the capacity of MOD and MOI in connection with direct assistance. They stated that CSTC-A advisers embedded in MOD and MOI participate in quarterly assessments of MOD and MOI progress toward meeting defined capability objectives. For example, CSTC-A assesses MOI development in 26 different areas, including finance and budget, procurement, and personnel management. The assessments focus on the extent to which the ministries are capable of achieving the objectives and identify specific strengths and weaknesses. For example, in April 2011, CSTC-A assessed the MOD budget and finance section responsible for ANA pay support operations. CSTC-A determined that its strengths included experienced staff and a willingness to tackle corruption and its weakness was a lack of budget authority.

DOD's February 4, 2011, guidance²¹ requires CSTC-A to establish financial controls for its contributions to MOD and MOI.

- The guidance specifically requires CSTC-A to conduct quarterly reconciliations of CSTC-A advance payments to MOD and MOI against records of MOD and MOI expenditures. CSTC-A officials

²⁰Under Secretary of Defense (Comptroller), *Interim Guidance on Afghanistan Security Forces Fund (ASFF) Contributions to the Government of the Islamic Republic of Afghanistan (GIRoA)* (Feb. 4, 2011).

²¹Under Secretary of Defense (Comptroller), *Interim Guidance on Afghanistan Security Forces Fund (ASFF) Contributions to the Government of the Islamic Republic of Afghanistan (GIRoA)* (Feb. 4, 2011).

informed us that CSTC-A reconciles CSTC-A advance contributions against MOD and MOI expenditure data drawn from the Ministry of Finance (MOF) Afghan Financial Management Information System and has adjusted future contributions accordingly. DOD officials acknowledged the reconciliation process does not address the extent to which aggregated line items from the system may contain inaccurate ANA and ANP payroll data.²²

- The guidance also requires CSTC-A to monitor MOD and MOI use of the contributed funds down to the subcontractor level. CSTC-A officials informed us that they would be unable to monitor MOD and MOI subcontractors, as called for in the DOD guidance. They stated that the risk of sending personnel to vet MOD and MOI subcontractors in certain regions of Afghanistan was too great.

In addition, CSTC-A advisers monitor MOD and MOI use of U.S. funds, according to CSTC-A officials. CSTC-A informed us that it has embedded about 500 advisers in MOD and MOI, including 6 in MOD financial offices and 13 in MOI finance and budget offices. Also, CSTC-A personnel participate in internal control teams that review ANA pay processes in a different ANA corps every month.²³

²²The Office of the Defense Inspector General is now reviewing ANA pay systems.

²³We reviewed reports prepared by three of these teams in December 2010, January 2011, and February 2011. In them, CSTC-A personnel identified problems with pay systems. These problems included poor collaboration between levels in the ANA, the lack of finance mentors at the corps level, inadequate training and promotion possibilities for finance officers, a manual payroll system that does not allow finance officers to check the accuracy of payroll data, and a shortage of bank branches where ANA soldiers may obtain their salaries. The reports included recommendations to address some of these issues.

USAID Has Not Consistently Assessed Risks of Contributions to ARTF, While DOD Has Recently Established Risk Assessment Guidance for LOTFA

USAID and DOD generally rely on the World Bank and UNDP to ensure accountability over U.S. direct assistance provided multilaterally through ARTF and LOTFA. USAID, however, has not consistently complied with its multilateral trust fund risk assessment policies in awarding funds to ARTF. For example, in March 2010, USAID did not conduct a risk assessment before awarding an additional \$1.3 billion to the World Bank for ARTF. During our review, DOD established procedures in June 2011 requiring that it assess risks before contributing funds to LOTFA. World Bank and UNDP controls over ARTF and LOTFA funds include the use of hired monitoring agents to help ensure that ministries use donor contributions as intended. However, these controls face challenges posed by security conditions and by weaknesses in Afghan ministries. For example, the ARTF monitoring agent resigned in June 2011 due to security concerns, while weaknesses in MOI's systems for paying wages to Afghan police challenge UNDP efforts to ensure that MOI is using LOTFA funds as intended.

USAID Has Not Consistently Assessed the Risk of Relying on the World Bank for Ensuring the Accountability of Its ARTF Contributions

USAID has not consistently followed its own policies for assessing the risk associated with its awards to the World Bank for ARTF, which have increased from \$5 million in 2002 to a total of more than \$2 billion. When the grant agreement and subsequent modifications between the World Bank and USAID were signed, USAID policies on grants to public international organizations (PIO), such as the World Bank, called for preaward determinations that the PIO was a responsible grantee.²⁴ This requirement applied to both the original grant and to any subsequent modification of the grant that significantly increased the amount of the award. Under USAID policy, the preaward determination should have addressed factors such as whether the grantee's program was an effective and efficient way to achieve a USAID objective and whether there were any reasons to consider the grantee to be "not responsible."

USAID could not provide us with a preaward responsibility determination of the World Bank prior to awarding ARTF an initial grant of \$5 million in 2002. While USAID did not follow its policies to complete a preaward determination for its initial \$5 million grant, it determined, after it signed the agreement, that (1) ARTF had a comprehensive system in place for managing the funds and (2) the World Bank had a long history in

²⁴Prior USAID ADS 308.3.2 (effective Feb. 5, 2004).

managing multidonor pooled funding mechanisms, in an approved 2002 memorandum requesting a deviation from incorporating its then-mandatory standard provisions into its ARTF grant agreement. However, USAID did not conduct preaward determinations for 16 of the 21 subsequent modifications to the grant. For the instance in which USAID increased the value of the award by \$1.3 billion in March 2010, USAID provided us with an unsigned and undated memorandum that applied to a \$15 million obligation.²⁵ For the 5 preaward responsibility determinations that were conducted, USAID documentation stated that the World Bank was a responsible grantee but did not document the analysis used to support the determinations.

In April 2011, in response to GAO recommendations and our follow-up meetings, USAID revised and expanded its guidance on how to conduct preaward determinations for all PIOs.²⁶ The revised guidance continues to require the USAID officer in charge of the agreement to document preaward responsibility determinations for PIOs.²⁷ Under the new guidance, a group of USAID headquarters officials²⁸ will first place the PIO, such as the World Bank, into one of three categories, based on USAID's experience with the PIO and its determination of the PIO's level of responsibility.²⁹ The revised guidance requires USAID to consider several factors in determining a PIO's level of responsibility, including the

²⁵ USAID also provided us with an August 2009 unsigned memorandum that stated that ARTF had sufficient safeguards in place to minimize the diversion or misuse of cash, goods, and services provided to Afghanistan and assessed the risk of financing terrorist activity through ARTF as being low in response to a mission requirement to conduct a terrorist financing risk assessment.

²⁶ We recommended that USAID develop and document its approach for assessing the eligibility of potential PIO grantees to help ensure accountability. See GAO, *UN Office for Project Services: Management Reforms Proceeding but Effectiveness not Assessed, and USAID's Oversight of Grants Has Weaknesses*, [GAO-10-168](#) (Washington, D.C.: November 19, 2009).

²⁷ USAID ADS 308.3.2.1, 308.3.2.2 (effective Apr. 19, 2011).

²⁸ The group, called the Delegated Cooperation Secretariat, will be coordinated by USAID's Bureau for Policy, Planning, and Learning and would include the offices of Acquisition and Assistance, General Counsel, Chief Financial Officer, and Legislative and Public Affairs.

²⁹ The categories designate PIOs as (1) generally major international PIOs or certain regional PIOs; (2) generally smaller, regional PIOs, and international organizations that are not frequent recipients of USAID assistance; or (3) PIOs that USAID headquarters officials have subjected to special restrictions or that are not currently eligible for USAID funding based on their financial or management performance.

quality of its past performance, its most recent audited financial statements, and any other information to fully assess whether it has the necessary management competence to plan and carry out the intended activity. After a responsibility determination has been made, the USAID officer in charge of the agreement must still document the determination before making an award.

USAID's policy is to generally rely on a PIO's financial management, procurement, and audit policies and procedures. The World Bank has established financial controls over donor contributions to ARTF. For example, the World Bank hired a monitoring agent responsible for monitoring the eligibility of salaries and other recurrent expenditures that the Afghan government submits for reimbursement against ARTF criteria.³⁰ According to the World Bank, it conducts advance reviews of ARTF development procurement contracts. The amount of prior review of Afghan government procurement by the bank varies according to the method of selection or procurement, the type of good or service being procured, and the bank's assessment of project risk, according to the bank. The World Bank also reports that it assesses projects semi-annually as part of regular World Bank supervision as per World Bank policies, procedures and guidelines based in part on project visits. Also, the bank informed us that it manages and administers ARTF according to a set of World Bank global policies and procedures. ARTF is part of a single audit of all trust funds administered by the bank, and includes both an annual management assertion over internal controls surrounding the preparation of trust fund financial reports and a combined financial statement for all modified cash basis trust funds.

³⁰ ARTF criteria for eligibility include the following: Eligible expenditures must be included in the Afghan government yearly budget; all goods and services must be procured and accounted for in accordance with Afghan government law and regulations; capitalized goods and works need to be procured in accordance with the World Bank procurement guidelines; and all military expenditures are not qualified for financing. In addition to the Afghan laws and regulations, the World Bank and the Afghan government have agreed on a set of additional requirements on the eligibility of expenditures.

Also, the Afghan government's external audit agency, the Control and Audit Office (CAO),³¹ conducts annual audits of ARTF-financed projects with the technical assistance of a firm of international accountants that are funded by the World Bank. As part of its supervision of ARTF-financed activities, a World Bank financial management team reviews the CAO audit reports, discusses its observations with government counterparts, and follows up to ensure resolution of any outstanding issues. Following the government's annual submission of CAO audit reports to the World Bank, the bank sends a letter to the donors summarizing the timeliness and results of the CAO's annual audits. The CAO's audits of 16 ARTF development projects for the Afghan fiscal year that began in March 2009 had 16 unqualified (or "clean") results. The World Bank shares CAO audit and monitoring agent reports with donors when requested.³²

World Bank financial controls over ARTF face challenges posed by oversight entities' limited movement in Afghanistan's high-threat environment and the limited capacity of Afghan ministries to meet agreed-upon procurement and financial management standards, as shown in these examples.

- Security conditions prevented CAO auditors from visiting most of the provinces where ARTF funds were being spent.³³ They were able to conduct audit tests in 10 of Afghanistan's 34 provinces from March 2009 to March 2010 and issued a qualified opinion of the financial

³¹The CAO is responsible for auditing the financial matters of the Afghan government. It focuses on assessing the financial reporting of Afghan government ministries and compliance with laws and regulations. The CAO reports directly to the President of Afghanistan. We did not assess the quality of the CAO's audits of ARTF.

³²In addition, the Special Inspector General for Afghanistan Reconstruction (SIGAR) is currently auditing the extent of ARTF controls to ensure accountability over donor contributions.

³³We have previously reported on the challenges U.S. agencies face due to the high-threat security environment in Afghanistan. See GAO, *Afghanistan's Security Environment*, [GAO-10-178R](#) (Washington, D.C.: Nov. 5, 2009); and *Afghan Army Growing, but Additional Trainers Needed; Long-term Costs Not Determined*, [GAO-11-66](#) (Washington, D.C.: Jan. 27, 2011).

statements of ARTF's salary and other recurrent expenditures as a result.³⁴

- According to the Department of the Treasury (Treasury), the ARTF monitoring agent recently resigned from its contract with the World Bank due to security concerns. USAID stated in July 2011 that the monitoring agent informed the bank in May 2011 that its contract should not be extended due to security concerns. The World Bank reports that it is seeking a new monitoring agent, has received many expressions of interest, and does not anticipate a gap in monitoring.
- Previously, security concerns prevented the ARTF monitoring agent from physically verifying ARTF salary and other recurrent expenditures outside of Kabul province from March 2009 through March 2010.³⁵ The World Bank had required the monitoring agent or its subcontractor to visit sites in at least 12 provinces to verify expenditures made during the Afghan fiscal year that began in March 2010.
- The CAO lacks qualified auditors and faces other capacity restraints, according to the Special Inspector General for Afghanistan Reconstruction (SIGAR) and USAID.³⁶ However, it uses international advisers and contracted auditors, funded by the World Bank, to help ensure that its audits of ARTF comply with international auditing standards. The World Bank recently reported that the overall timeliness of the CAO audits have been improving since 2006.

³⁴The World Bank informed us that this qualification referred to a limitation in scope in the review of the entire civilian recurrent costs. The CAO reviewed and gave positive assurance of \$425 million for that one year period against an ARTF ceiling of \$290 million.

³⁵From March 2009 to March 2010, the ARTF monitoring agent conducted monitoring through the review of documents submitted from eight provinces for operations and maintenance expenditures and carried out analytical procedures for the rest of the provincial expenditure. The monitoring agent used an audit sampling approach intended to ensure that it monitored enough expenditure to establish that ARTF recurrent cost funds were being used in line with eligibility criteria, according to the bank.

³⁶SIGAR, *Afghanistan's Control and Audit Office Requires Operational and Budgetary Independence, Enhanced Authority, and Focused International Assistance to Effectively Prevent and Detect Corruption* (Apr. 9, 2010); USAID, *Report on the Assessment of the Capability of the Ministry of Finance (MoF), Da Afghanistan Bank (DAB), and the Control and Audit Office (CAO) in regard to Managing Direct Donor Assistance* (July 27, 2009).

-
- The World Bank and donors have expressed concern over the level of ineligible expenditures submitted by the Afghan government for reimbursement.³⁷ While ineligible expenditures are not reimbursed, the bank considers the level of ineligible expenditures to be an indicator of weaknesses in the Afghan government's ability to meet agreed-upon procurement and financial management standards. The ARTF monitoring agent has questioned whether Afghan government civil servants have the experience and knowledge necessary to perform transactions in a manner eligible for reimbursement and whether ministries' internal procedures fully reflect Afghan government laws and regulations.³⁸

Partly as a result of recommendations from a 2008 independent evaluation of ARTF by a Norwegian-based firm and discussions with donors,³⁹ the World Bank is currently seeking to revise its 2002 grant agreements with donors to reflect its efforts to strengthen ARTF governance. According to the World Bank, the recommended changes include clarifying and strengthening donors' oversight roles and responsibilities over ARTF. In response to our inquiries, the World Bank stated in April 2011 that it is considering incorporating its current standard provisions, applicable to multidonor trust funds, in the amended grant agreements with donors. These provisions would allow donor countries greater access to accounting and financial records and information. Under the current agreement with all donors, the World Bank provides donors with periodic reports, such as quarterly status reports, and an annual management assertion together with an attestation from the bank's external auditors on the satisfactory performance of the bank's procedures and controls.

³⁷The ratio of ineligible recurring expenditures was 11.6 percent in the Afghan fiscal year beginning in March 2002. In the Afghan fiscal year beginning in March 2009, the level of ineligible expenditures was 20.1 percent.

³⁸The bank informed us that procurement of civilian goods and services over \$200,000 and works contracts of more than \$500,000 are centrally reviewed for compliance with agreed-upon procedures.

³⁹Scanteam, Afghanistan Reconstruction Trust Fund: External Evaluation (Oslo: August 2008).

CSTC-A Has Recently Established Procedures Requiring That It Assess Risks Associated with Contributions to LOTFA

During our review on June 12, 2011, CSTC-A issued new procedures for direct assistance that require CSTC-A to conduct pre-contribution risk assessments before contributing funds to LOTFA.⁴⁰ CSTC-A staff had previously informed us in February 2011 that CSTC-A had not assessed the risks of providing funds to LOTFA. Instead, CSTC-A had regularly assessed the capabilities and weaknesses of MOI. For example, CSTC-A assessed MOI's finance and budget section in March 2011 and determined that while the section's strengths included a responsiveness to pay issues, its weaknesses included a lack of well-trained staff and an unwillingness to change.

CSTC-A generally relies on UNDP's financial controls to ensure the accountability of funds it has contributed to LOTFA. CSTC-A contribution letters to LOTFA request that UNDP provide CSTC-A with quarterly reports, which UNDP posts on its Web site.⁴¹ CSTC-A officials informed us that CSTC-A reconciles its contributions to LOTFA annually. UNDP's LOTFA project manager in Kabul informed us that UNDP makes copies of audits of LOTFA available upon request. CSTC-A officials told us they have not requested LOTFA audits.

UNDP has established financial controls over the funds it provides to MOI for ANP expenses. It has stated that it reconciles its contributions with MOF records of MOI expenses on a quarterly and annual basis. UNDP recently reported that it deducted \$17.6 million from its contribution to MOI as a result of ineligible expenses identified during its annual reconciliation for March 2009 through March 2010. UNDP has also hired a monitoring agent to review and monitor ANP remunerations and generate independent reports. UNDP staff told us that the LOTFA monitoring agent has offices in all regional police zones, which cover all of Afghanistan's provinces. UNDP has reported that the monitoring agent operates in all ANP zones and conducts sample verifications of 30 percent of the total number of police.

Similar to the World Bank's controls over ARTF, UNDP's financial controls over LOTFA face challenges stemming from Afghanistan's

⁴⁰ CSTC-A adopted these procedures after we discussed the lack of such guidance with officials from CSTC-A and the office of the Under Secretary of Defense (Comptroller) in February 2011.

⁴¹ These reports can be found at http://www.undp.org.af/whoweare/undpinafghanistan/Projects/sbgs/prj_lotfa.htm.

security environment. SIGAR reported in April 2011 that security issues had impaired efforts by LOTFA's monitoring agent to (1) recruit staff in a high-threat province and (2) travel in 7 of Afghanistan's 34 provinces for half of 2010. SIGAR also reported that security concerns had delayed LOTFA's reconciliation of 2009 salaries.⁴² UNDP officials also told us that security concerns had restricted UNDP movements in Afghanistan.

UNDP's financial controls also face challenges stemming from MOI's institutional weaknesses. UNDP has reported that MOI's "insufficient ownership and capacity development" remains one of LOTFA's risks and that it has taken steps to mitigate this risk. Some problems that have been identified with MOI include the following:

- In 2009, we reported that MOI did not have an accurate staffing roster, according to CSTC-A, and that the number of ANP personnel was unclear.⁴³ We found that uncooperative ANP commanders were impeding State and MOI efforts to implement a new ANP identification card system to positively identify all police for pay purposes, according to State officials. According to State officials, these commanders were preventing State and MOI from determining the status of nearly 30,000 individuals whose names had been submitted to receive ANP identification cards.⁴⁴ We recommended that DOD and State consider provisioning future U.S. contributions to LOTFA to reflect the extent to which U.S. agencies had validated the status of MOI and ANP personnel to help ensure that the United States was not funding salaries of unverified personnel.⁴⁵

⁴² SIGAR, *Despite Improvements in MOI's Personnel Systems, Additional Actions Are Needed to Completely Verify ANP Payroll Costs and Workforce Strengths* (Apr. 25, 2011). The SIGAR report can be found at www.sigar.mil/pdf/audits/SIGAR%20Audit-11-10.pdf. UNDP did not agree with all of SIGAR's findings regarding LOTFA. Its comments on the SIGAR report are contained in appendix IV of that report.

⁴³ GAO, *Afghanistan Security: U.S. Programs to Further Reform Ministry of Interior and National Police Challenged by Lack of Military Personnel and Afghan Cooperation*, [GAO-09-280](http://www.gao.gov/products/GAO-09-280) (Washington, D.C.: Mar. 9, 2009).

⁴⁴ GAO noted that, in all, more than 103,000 names had been submitted for the identification cards, although the ANP at that time had an authorized strength of less than 79,000.

⁴⁵ DOD did not concur with our recommendation. State concurred with our recommendation.

-
- In 2011, SIGAR reported that MOI's payroll system provides little assurance that MOI is paying only working ANP personnel or that LOTFA funds are reimbursing only eligible ANP costs. MOI is also unable to pay all police through relatively secure systems. We have previously reported concerns regarding MOI pay systems.⁴⁶ UNDP and CSTC-A have worked with MOI to develop electronic systems to reduce opportunities for skimming and corruption. One such system transfers funds directly into individual bank accounts established by individual Afghan police. Although progress has been made in establishing these systems, more than 20 percent of ANP staff are still paid using manual cash systems that are more vulnerable to abuse.

Conclusion

The recent tripling of U.S. direct assistance awards to Afghan government entities, coupled with the vulnerability of this assistance to waste, fraud, and abuse in the uncertain Afghan environment, makes it essential that U.S. agencies assess risks before awarding funds and implement controls to safeguard those funds. Direct assistance to the Afghan government involves considerable risk given the extent of corruption, the weak institutional capacity of the Afghan government to manage finances, the volatile and high-threat security environment, and that the U.S. funds may be obligated months or years after they are awarded. Because conflict in many parts of Afghanistan poses significant challenges to efforts to ensure that funds are used as intended, the level of risk in Afghanistan warrants, to the extent feasible, sound internal controls and oversight over the billions of dollars that the U.S. government has invested in Afghanistan. Although risk assessment is a key component of internal controls, current USAID policy does not require preaward risk assessments of all Afghan government recipients of U.S. direct assistance funds. To safeguard U.S. direct assistance funds, it is important that (1) the USAID Administrator follow through on his July 2010 commitment to Congress to assess risks associated with each Afghan government entity before awarding funds, (2) USAID consistently implement controls it establishes in bilateral direct assistance agreements, and (3) USAID consistently adhere to its risk assessment policies for multilateral trust funds in awarding funds to ARTF.

⁴⁶ GAO, *Afghanistan Security: U.S. Programs to Further Reform Ministry of Interior and National Police Challenged by Lack of Military Personnel and Afghan Cooperation*, [GAO-09-280](#) (Washington, D.C.: Mar. 9, 2009).

Recommendations for Executive Action

We recommend that the Administrator of USAID take the following three actions:

- Establish and implement policy requiring USAID to complete risk assessments before awarding bilateral direct assistance funds to Afghan government entities in all cases.
- Take additional steps to help ensure that USAID consistently implements controls established in its bilateral direct assistance agreements with Afghan government entities, such as requiring the retention of documentation of actions taken.
- Ensure USAID adherence with its policies for assessing risks associated with multilateral trust funds in awarding funds to ARTF.

Agency Comments and Our Evaluation

We provided a draft of this report for comment to the Administrator of USAID, and to the Secretaries of Defense, State, and the Treasury. Defense, State, and the Treasury declined to provide comments. Treasury provided us with technical comments, which we incorporated in this report as appropriate. The World Bank and UNDP provided us with technical comments on the portions of the draft report that we provided them describing ARTF and LOTFA. We have incorporated these technical comments in this report as appropriate.

USAID provided written comments on a draft of our report, which are reprinted in appendix II.

With regard to our recommendation that USAID establish and implement policies requiring USAID staff to complete risk assessments before awarding bilateral direct assistance funds to Afghan government entities in all cases, USAID stated that its existing policies and procedures in ADS already include requirements for risk assessment for each form of government-to-government assistance mechanism. USAID noted that for host country contracts, ADS requires an advance assessment of a host government's procurement systems (ADS 305). USAID also stated that for cash transfer agreements, ADS requires an analysis of a host government's ability to comply with the agreements. USAID further stated that its general activity planning guidance contains a recommendation that USAID offices should consider the capacity of potential partners to implement planned functions (ADS 201).

Although USAID policy in ADS includes some form of risk assessment for the funding mechanisms in use in Afghanistan, it does not require that a risk assessment be conducted in all cases. Specifically, ADS 305's requirement for preaward assessment of host country contracts did not apply to six of the eight bilateral direct assistance cases we identified, because these six cases do not involve procurement. Further, according to the USAID comptroller, these six cases were not cash transfer agreements. As a result, these six cases fall under USAID's general activity planning guidance (ADS 201), which recommends—but does not require—that USAID offices assess the capacity of potential partners in advance. As noted in this report, the lack of specific requirement resulted in USAID making awards in two cases prior to completing a risk assessment. Therefore, we retained our recommendation that USAID establish and implement policies requiring preaward risk assessments in all cases in Afghanistan.

USAID also commented that it has taken additional steps to ensure that, going forward, risk assessments are completed in advance for each type of funding mechanism, in line with the Administrator's July 2010 statement to Congress. Further, these steps are being undertaken "in light of" the Department of State's July 14, 2011, certification to Congress that the U.S. and Afghan governments have established mechanisms within each implementing agency to ensure that certain fiscal year 2010 funds will be used as intended.⁴⁷ On July 14, 2011, State did make this certification to Congress. However, the certification applies only to certain fiscal year 2010 funds, underscoring the need for USAID to establish a requirement for preaward assessments in Afghanistan in all cases in its policies and procedures.

With regard to our recommendation that USAID take additional steps to help ensure that it consistently implements controls established in its bilateral direct assistance agreements with Afghan government entities, USAID agreed to take such steps concerning its host country agreements with Afghan government entities. In doing so, USAID noted that USAID policy is to be as sparing in exercising its prior approval rights as sound management permits.

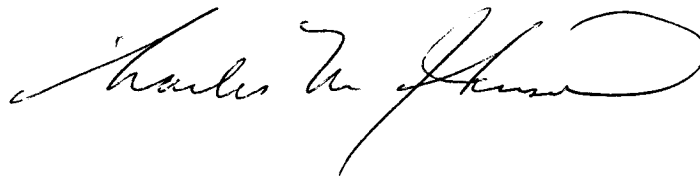
⁴⁷ State provided the certification in response to provisions of the Department of State, Foreign Operations, and Related Programs Appropriations Act, 2010, (Div. F., P.L. 111-117).

With regard to our recommendation that it adhere to its policies for assessing risks associated with multilateral trust funds in awarding funds to ARTF, USAID acknowledged that it had not always prepared or adequately documented its determinations for several ARTF grant amendments. USAID stated that it will follow its new procedures for such determinations, which it revised in April 2011.

USAID also provided us with technical comments, which we have incorporated as appropriate.

We are sending copies of this report to the appropriate congressional committees; the Secretaries of Defense, State, and the Treasury; the Administrator of USAID; and other interested parties. The report also is available at no charge on the GAO Web site at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact me at (202) 512-7331 or johnsoncm@gao.gov. Contact points for our Offices of Public Affairs and Congressional Relations may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix III.



Charles Michael Johnson Jr.
Director
International Affairs and Trade

List of Congressional Addressees

The Honorable Carl Levin
Chairman
The Honorable John McCain
Ranking Member
Committee on Armed Services
United States Senate

The Honorable John Kerry
Chairman
The Honorable Richard Lugar
Ranking Member
Committee on Foreign Relations
United States Senate

The Honorable Joseph I. Lieberman
Chairman
Committee on Homeland Security
and Governmental Affairs
United States Senate

The Honorable Daniel K. Inouye
Chairman
The Honorable Thad Cochran
Ranking Member
Subcommittee on Defense
Committee on Appropriations
United States Senate

The Honorable Buck McKeon
Chairman
The Honorable Adam Smith
Ranking Member
Committee on Armed Services
House of Representatives

The Honorable Ileana Ros-Lehtinen
Chairman
The Honorable Howard L. Berman
Ranking Member
Committee on Foreign Affairs
House of Representatives

The Honorable Kay Granger
Chairwoman
The Honorable Nita M. Lowey
Ranking Member
Subcommittee on State, Foreign Operations,
and Related Programs
Committee on Appropriations
House of Representatives

The Honorable John F. Tierney
Ranking Member
Subcommittee on National Security, Homeland Defense
and Foreign Operations
Committee on Oversight and Government Reform
House of Representatives

Appendix I: Objectives, Scope, and Methodology

This report assesses (1) the extent to which the U.S. Agency for International Development (USAID) and the Department of Defense (DOD) have increased direct assistance, (2) USAID's and DOD's steps to ensure accountability for bilateral direct assistance, and (3) USAID's and DOD's steps to ensure accountability for multilateral direct assistance.

To identify the extent to which USAID and DOD had increased their direct assistance, we first met with officials from the Department of State and USAID to define the scope of the term "direct assistance" for the purpose of this review.¹ We then adopted USAID's definition of direct assistance (or "on-budget" assistance) as U.S. funds provided through the Afghan government national budget for use by Afghan ministries or other government entities. This definition is consistent with guidance and procedures developed by the Office of the Under Secretary of Defense (Comptroller) and DOD's Combined Security Transition Command-Afghanistan (CSTC-A).² We focused on fiscal year 2009 and fiscal year 2010 to identify funding developments tied to the President's 2009 announcement of a new U.S. strategy for Afghanistan and subsequent pledges concerning direct assistance to the Afghan government.

- To identify the extent to which USAID had increased its direct assistance, we obtained financial information from USAID's mission in Kabul, Afghanistan. This information included USAID quarterly financial reports and USAID direct assistance agreements with Afghan government entities and the World Bank (including any modifications to the agreements). We used this information to identify the value of the direct assistance USAID awarded in fiscal years 2009 and 2010. For the value of each award, we used what USAID refers to as the "total estimated contribution" that it has committed to provide, subject to the availability of funds, in signing a direct assistance agreement. For the date, we used each agreement's signature date, in keeping with USAID's use of the signature date as the effective date of the funded activity. We used the signature dates to allocate each award's value to either fiscal year 2009 or fiscal year 2010. In

¹We also met with State officials to obtain Office of Management and Budget data regarding U.S. government funding for Afghan reconstruction.

²Under Secretary of Defense (Comptroller), *Interim Guidance on Afghanistan Security Forces Fund (ASFF) Contributions to the Government of the Islamic Republic of Afghanistan (GIROA)* (Feb. 4, 2011); and CSTC-A, *Standard Operating Procedure (SOP) for Direct Contributions* (June 12, 2011).

using this data in the report, we noted that once it has awarded funds on a specific date, USAID may obligate and disburse those funds over multiple years, depending on the terms of the agreement. We assessed these data to be sufficiently reliable for our purposes.

- To identify the extent to which DOD had increased its direct assistance, we obtained financial information from DOD's Office of the Under Secretary of Defense (Comptroller). This information included funds contributed to the Afghan Ministry of Defense (MOD) and the Afghan Ministry of Interior (MOI) by CSTC-A and the Defense Security Cooperation Agency. According to the Office of the Under Secretary of Defense (Comptroller), each DOD contribution to MOD, MOI, and the Law and Order Trust Fund for Afghanistan (LOTFA) was awarded, obligated, and disbursed in close succession. We allocated each contribution's value to the fiscal year in which the contribution was made. We assessed these data to be sufficiently reliable for our purposes.

To assess steps taken by USAID and DOD to help ensure the accountability of their bilateral direct assistance to Afghan ministries and other government entities, we reviewed the policies and practices the agencies use to assess risks associated with direct assistance and to establish control mechanisms over the use of direct assistance funds.

- Our assessments were based on criteria drawn from GAO's *Standards for Internal Control in the Federal Government*.³ *Standards for Internal Control in the Federal Government*, issued pursuant to the requirements of the Federal Managers' Financial Integrity Act of 1982, provides the overall framework for establishing and implementing internal control in the federal government. Minimum internal control standards for providing reasonable assurance that agency assets will be safeguarded against fraud, waste, abuse, and mismanagement include risk assessment and control activities. *Standards for Internal Control in the Federal Government* defines risk assessment and control activities as key elements of an internal control framework. Risk assessment includes identifying internal and external risks an organization faces and their potential effect. Control activities are the policies and procedures (such as approvals, reconciliations, and

³GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999).

reviews) agencies implement to mitigate identified risks and are essential for accountability of government resources.

- To evaluate relevant USAID policies and practices against these criteria, we reviewed information from both headquarters and the USAID mission in Afghanistan. We reviewed USAID agencywide policies for awarding bilateral direct assistance funds to host government entities, as outlined in (1) USAID's Automated Directives System (ADS)⁴ and (2) interim guidance USAID provided to its mission on the use of direct assistance. We reviewed bilateral direct assistance program information from the USAID mission in Afghanistan, including preaward assessment procedures and reports, training material, direct assistance agreements, compliance documentation, approval memorandums, memorandums of understanding, and mission orders. To identify USAID controls established over the use of direct assistance funds and determine whether USAID ensured compliance with its controls, we (1) reviewed all USAID bilateral direct assistance agreements, (2) identified the controls USAID established in each agreement, and (3) reviewed documentation USAID provided to us to demonstrate it had ensured compliance with its controls. We limited our analysis to controls triggered per the terms of each agreement before February 15, 2011. We also reviewed information from the USAID Office of Inspector General in Afghanistan regarding the mission's preaward assessment process. We interviewed USAID officials in Washington, D.C., and in Kabul, Afghanistan.
- To assess DOD policies and practices, we reviewed information from the Office of the Undersecretary of Defense (Comptroller) and CSTC-A. This information included the Under Secretary's February 4, 2011, *Interim Guidance on Afghanistan Security Forces Fund (ASFF) Contributions to the Government of the Islamic Republic of Afghanistan (GIROA)*, CSTC-A's standard operating procedures for direct contributions, DOD contribution letters to MOD and MOI, and DOD assessments of the strengths and weaknesses of these ministries. We also interviewed DOD officials in Washington, D.C., and Kabul.

⁴USAID ADS 201, 301, 305, and 591.

To assess steps taken by USAID and DOD to help ensure the accountability of their direct assistance to Afghan ministries through multilateral trust funds, we reviewed the policies and practices the agencies use to assess risks associated with direct assistance and to establish control mechanisms over the use of direct assistance funds.

- Our assessments were again based on criteria drawn from GAO's *Standards for Internal Control in the Federal Government*,⁵ which defines risk assessment and control activities as key elements of an internal control framework.
- To evaluate relevant USAID policies and practices regarding multilateral trust funds against these criteria, we reviewed USAID agencywide policies for awarding direct assistance to multilateral trust funds such as the World Bank-administered Afghanistan Reconstruction Trust Fund (ARTF), as outlined in USAID's Automated Directives System.⁶ We also reviewed ARTF-related program and budget documents from the USAID mission in Afghanistan, including USAID's 2002 grant agreement with ARTF and modifications to the agreement. We also met with officials of the Department of the Treasury to coordinate our work regarding the World Bank. We reviewed World Bank documents concerning ARTF and interviewed USAID and World Bank officials in Washington, D.C., and in Kabul.
- To assess DOD policies and practices regarding multilateral trust funds against these criteria, we reviewed information from the Office of the Undersecretary of Defense (Comptroller) and CSTC-A. This information included the Under Secretary's February 4, 2011, *Interim Guidance on Afghanistan Security Forces Fund (ASFF) Contributions to the Government of the Islamic Republic of Afghanistan (GIROA)* and CSTC-A's standard operating procedures for direct contributions. We also reviewed United Nations Development Program (UNDP) documents and reports concerning the Law and Order Trust Fund for Afghanistan and interviewed DOD officials in Washington, D.C., and in Kabul, as well as UNDP officials in Kabul.

⁵ GAO/AIMD-00-21.3.1.

⁶ USAID ADS 308.

Appendix II: Comments from the U.S. Agency for International Development



July 14, 2011

Charles M. Johnson, Jr.
Director, International Affairs and Trade
U.S. Government Accountability Office
Washington, DC 20548

Dear Mr. Johnson:

I am pleased to provide the U.S. Agency for International Development's formal response to the GAO draft report entitled "AFGHANISTAN: Actions Needed To Improve Accountability of U.S. Assistance To Afghanistan Government" (GAO-11-710).

The enclosed USAID comments are provided for incorporation with this letter as an appendix to the final report.

Thank you for the opportunity to respond to the GAO draft report and for the courtesies extended by your staff in the conduct of this audit review.

Sincerely,

Sean C. Carroll /s/
Chief Operating Officer
U.S. Agency for International Development

Enclosure: a/s

The U.S. Agency for International Development letter was signed electronically by Sean C. Carroll, Chief Operating Officer.

- 2 -

USAID COMMENTS ON GAO DRAFT REPORT No. GAO-11-710

General Comments:

Recommendation 1: We recommend that the Administrator of USAID “establish and implement policy requiring USAID to complete risk assessments before awarding bilateral direct assistance funds to Afghan government entities in all cases.” (emphasis added)

Management Comments: Consistent with the definition used by GAO, USAID defines “risk assessment” as an internal management process for identifying, analyzing and managing risks relevant to achieving the objectives of safeguarding assets, compliance with relevant laws and regulations and reliable financial reporting.

It should be noted that existing USAID policies and procedures, as described below, set forth in our Automated Directive System (ADS) already include requirements for risk assessments that are targeted, in large part, to the type of direct government-to-government assistance mechanism proposed. As explained below, each type of USAID direct government-to-government assistance mechanism includes some form of risk assessment. Consistent with USAID’s Implementation and Procurement Reform objective of strengthening host country capacity to improve aid effectiveness and sustainability by increasing use of reliable host country systems and institutions to provide support to host countries, USAID has taken additional steps to ensure that, going forward, risk assessments are completed in advance not just for each type of funding mechanism as described above, but also for each and every GIRA institution proposed as an implementing agency for a direct government-to-government assistance mechanism.

These additional steps being taken by USAID are in line with the Administrator’s July 2010 statement to Congress. Furthermore, with respect to Afghanistan, these measures are being undertaken in light of the certification required under the Economic Support Fund header of the Department of State, Foreign Operations, and Related Programs Appropriations Act, 2010 (Division F of P.L. 111-117) which includes, inter alia, a requirement that the United States Government and the Government of the Islamic Republic of Afghanistan (GIRA) have established mechanisms within each GIRA implementing agency to ensure that ESF funds

- 3 -

used for the purposes for which they were intended prior to the provision of direct government-to-government assistance.

As referenced above, USAID has several different types of direct government-to-government assistance mechanisms. Among those most widely used are host country contracts, fixed amount reimbursement agreements, implementation letter financing, general budget and balance of payment support, sector program assistance, and multi-donor pooled funding in a segregated host government account. All include some form of risk assessment of the host government systems or institutions. Below is a brief description of the USAID policies and procedures that include some form of assessment of host government systems or institutions for the direct government-to-government assistance mechanisms used or proposed for use in Afghanistan:

- 1) Host Country Contracts and Fixed Amount Reimbursements: a requirement to assess, in advance, a host government's procurement system under host country contracts (ADS 305), as noted in GAO's draft report, as well as fixed amount reimbursement agreements (FARAs) (ADS 317). It is important to note that USAID's assessment of host government procurement system is not simply a review and assessment of its procurement functions, but it also includes a review to determine if associated host government accounting system and internal controls are adequate. In addition, before a host country procurement authority is assigned a procurement action in excess of \$250,000 in USAID's host country contracting process, the USAID Mission Director must certify, in writing, that the Contracting Agency has the capability to undertake the specific procurement action. ADS E301.5.2b.
- 2) Cash Transfer Agreements: a requirement in ADS 350.3.4.2 to conduct and document an analysis to assess a host government grantee's ability to comply with the requirements set forth in cash transfer agreements, including the preparation of a decision memorandum summarizing the findings of the assessment and recommendations on the need for any third party authorizations that may be necessary to monitor the grant award. This written analysis should take into account the following: a) the purpose (balance of payments support, debt buy-down, etc.) and structure (direct payment to creditors, direct transfer to central government bank account, etc.) of the cash transfer; b) the existence, or lack thereof, of adequate provisions for auditing the agreement by

- 4 -

USAID's Office of the Inspector General or other U.S. Government auditors; c) the host government grantee's prior history, or lack thereof, with USAID cash transfer grant agreements; and d) the political context and U.S. foreign policy considerations.

- 3) Sector Program Assistance: a requirement to undertake detailed analysis as part of the special planning requirement for sector program assistance under USAID's February 1996 Program Assistance Policy Paper. This document specifies that "[r]igorous analysis is crucial to a successful sector program assistance effort. Planners must be concerned with cost/benefit, feasibility, and sustainability questions from six analytical perspectives, including, inter alia: "institutional, which frankly examines the capacity within the host government and other involved organizations to develop, agree upon, and implement all aspects of the assistance (including sectoral reform measures, ... cash disbursements, programming and accounting for [host country owned local currency])." This policy document further specifies that USAID "[p]lanners must have a clear understanding of ... any risks associated with the activity either in terms of implementation or sustainable development impact.
- 4) General Activity Planning Guidance: a recommendation, as part of the USAID activity planning processes set forth at ADS 201.3.11.9 to assess the capacity of potential implementing partners, including host government ministries and agencies. This policy guidance states that USAID "offices should consider the capacity of potential partners to implement planned functions, including, but not limited to, their capacity for financial management, procurement, and personnel management. Two related but different capacities are important: the ability to produce the desired outputs and the ability to meet USAID financial accountability requirements."

In addition to the above, Article 6 (Special Covenants) of all current USAID Strategic Objective Agreements with GIROA, includes the following:

- Results Orientation. The Parties agree to work together to use systems and structures that help staff and partners manage programs effectively and efficiently. An ability to adjust systems and structures when appropriate will enable the Parties to achieve results within agreed-upon schedules.

- 5 -

- Transparency and Accountability. The Parties agree to follow standards and regulations that ensure transparency and accountability. The Parties will endeavor to work in an honest, open and direct manner with all partners.

In addition to these existing safeguards, as part of our Implementation and Procurement Reform objective to strengthen host country capacity to improve aid effectiveness and sustainability by increasing use of reliable host country systems and institutions to provide support to host countries, USAID, led by the Office of the Chief Financial Officer, is leading the development of a Public Financial Management Risk Assessment Framework tool, which has been applied in several countries.

This tool includes several steps or stages in assessing the risk associated with using a host government system, including a Stage 1 Rapid Appraisal of Public Financial Management (PFM) Risk; a Stage 2 Questionnaire for the Public Financial Management Risk Assessment, negotiation with the host government at Stage 3 and implementation at Stage 4. Preparation of final guidance on each stage is underway, including a revision to the Agency's Automated Directives System. The Stage 1 guidance is attached.

Recommendation 2: We recommend that the Administrator of USAID take additional steps to help ensure that USAID consistently implements controls established in its bilateral direct assistance agreements with Afghan government entities, such as requiring the retention of documentation of actions taken.

Management Comments: USAID agrees to take additional steps to ensure compliance with the requirements set forth in our host government grant agreements with GIRoA. However, with respect to consistently implementing controls, USAID would like to draw GAO's attention to ADS 305.5.1 with respect to USAID approvals of contracting steps. That provision states that "As financier of host country procurement transactions, USAID reserves in its grant agreements and Implementation Letters the right to prior approval of most critical steps . . . It is, however, USAID policy to be as sparing in its exercise of its rights of prior approval as sound management of its interests permits. The exercise of USAID approval rights is not to be construed in any case as making USAID a party to a contract."

- 6 -

As to additional steps that USAID will take with respect to Afghanistan, USAID/Afghanistan is reviewing all host government grant agreements with the GIRoA to assess GIRoA's compliance with the terms and conditions set forth in these agreements and will issue implementation letters under these agreements to remind GIRoA of its specific, affirmative obligations under the agreements which we determine have not been met.

In addition, USAID/Afghanistan is developing a Mission Order that, among other things reminds USAID staff of the obligation to monitor our own and GIRoA's compliance with the terms and conditions in our host government grant agreements with GIRoA, designating this responsibility to the Mission Program Office. As part of the same or a separate Mission Order, and as a supplement to, but not a substitute for, the policy and procedures set forth in USAID's ADS, we plan to outline the general requirements, roles and responsibilities that apply to each form of direct government-to-government assistance mechanism. These responsibilities include the obligation of the technical office staff in managing the direct government-to-government assistance mechanism in partnership with a GIRoA institution, as well as the roles and responsibilities of USAID's program, financial management, procurement and legal staffs.

Recommendation 3: We recommend that the Administrator of USAID ensure USAID's adherence with its policies for assessing risks associated with multilateral trust funds in awarding funds to ARTF.

Management Comments: USAID acknowledges that, in the past, determinations were not prepared or adequately documented for several of the amendments to the USAID public international organization (PIO) grant agreement with the World Bank for ARTF. In response to GAO recommendations and follow up meetings and USAID's Implementation and Procurement Reform, USAID issued revised ADS 308 in April 2011, which lays out detailed procedures on responsibility determinations for PIOs. USAID will follow such new procedures for all future PIO grants, including grants to the World Bank and the ARTF, which may be conducted centrally by the Agency's new Delegated Cooperation Secretariat (DCS).

Additionally, as part of Implementation and Procurement Reform, USAID will also require not just an initial assessment using the PFMRAF of any host country system that may be used for direct USAID funded project implementation, but also periodic reassessments of those systems, as well as a new assessment in the event

- 7 -

of a significant increase of funding (and thus associated risk) for implementation using those systems. This requirement will extend to 3rd party agreements, such as the PIO grant at issue, that will make use of host country systems for project implementation.

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

Charles Michael Johnson Jr., (202) 512-7331 or johnsoncm@gao.gov

Staff Acknowledgments

Major contributors to this report were Tetsuo Miyabara, Assistant Director; Emily Gupta; Bruce Kutnick; Esther Toledo; and Pierre Toureille. Ashley Alley, Pedro Almoguera, Diana Blumenfeld, Jeffrey Baldwin-Bott, Gergana Danailova-Trainor, Martin De Alteriis, Karen Deans, Christopher Mulkins, Mona Sehgal, and Eddie Uyekawa also provided technical assistance.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday afternoon, GAO posts on its Web site newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's Web site, <http://www.gao.gov/ordering.htm>.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm

E-mail: fraudnet@gao.gov

Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Ralph Dawn, Managing Director, dawnr@gao.gov, (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

