

# Afghanistan's National Solidarity Program Has Reached Thousands of Afghan Communities, but Faces Challenges that Could Limit Outcomes



**March 22, 2011**



## OFFICE OF THE SPECIAL INSPECTOR GENERAL FOR AFGHANISTAN RECONSTRUCTION

March 22, 2011

The Honorable Hillary Rodham Clinton  
Secretary of State

The Honorable Karl W. Eikenberry  
U.S. Ambassador to Afghanistan

The Honorable Rajiv Shah  
Administrator  
U.S. Agency for International Development

Mr. Earl Gast  
USAID Mission Director to Afghanistan

This report discusses the results of the Office of the Special Inspector General for Afghanistan Reconstruction's (SIGAR) review of Afghanistan's National Solidarity Program (NSP). The report includes six recommendations to help ensure that U.S. and other donor contributions to NSP are used as intended and that the program addresses challenges that could limit outcomes.

A summary of this report is on page ii. SIGAR conducted this performance audit under the authority of Public Law No. 110-181, the Inspector General Act of 1978, as amended, and the Inspector General Reform Act of 2008. When preparing the final report, we considered comments from the U.S. Embassy Kabul, the World Bank, and the Afghan government's Ministry of Rural Rehabilitation and Development. These comments are reproduced in appendices V-VII.

A handwritten signature in black ink that reads "Herbert Richardson". The signature is written in a cursive style.

Herbert Richardson  
Acting Special Inspector General  
for Afghanistan Reconstruction



# SIGAR

Special Inspector General for Afghanistan Reconstruction

SIGAR Audit-11-8

March 2011

## Afghanistan's National Solidarity Program Has Reached Thousands of Afghan Communities, but Faces Challenges that Could Limit Outcomes

### What SIGAR Reviewed

SIGAR reviewed the multi-billion dollar National Solidarity Program (NSP) to assess the Afghan government's ability to manage and account for direct assistance from the United States and other international donors. This report addresses (1) the extent and use of U.S. and other donor assistance to the NSP, (2) the level of oversight and internal controls over donor funds, (3) whether NSP is achieving its intended results, and (4) key challenges facing NSP as it enters its third phase. To accomplish these objectives, we collected and analyzed documents, data, contracts, and agreements from NSP, MRRD, the World Bank, NSP facilitating partners, rural Afghan community development councils, Afghanistan's Control and Audit Office, USAID, and other NSP donors, including Denmark, Italy, and the United Kingdom. We conducted our work in Washington, D.C., and in Kabul and Parwan provinces in Afghanistan, from April 2010 to January 2011, in accordance with generally accepted government auditing standards.

### What SIGAR Found

International donors provided nearly all of the \$1.5 billion that the NSP received in funding from June 2002 to September 2010. The United States, the single largest donor to NSP, contributed \$528 million (35 percent) of that amount. Most NSP contributions have been made through the multilateral Afghanistan Reconstruction Trust Fund (ARTF), which is administered by the World Bank. The majority of NSP funds (72 percent) have been used as block grants to finance small-scale community development projects. Of the remaining 28 percent, about 19 percent has gone to pay facilitating partners to oversee the election and training of community development council (CDC) members, and about 9 percent has covered administrative costs.

Donor funds provided to NSP are subject to numerous oversight and internal controls implemented by the World Bank, the Afghan government, and members of rural Afghan communities. We found that these controls provided reasonable assurance that NSP funds would be used as intended. However, in one case, as reported by MRRD/NSP to Afghan authorities and donors, about \$2.8 million in NSP block grants were retained by a hawalla dealer and not delivered to the intended communities in one province. MRRD, NSP, and the World Bank have taken actions to address this issue, but it remains unresolved.

While NSP has reported meeting or exceeding most of its quantitative targets, it lacks data and reporting on one of its primary objectives—improving local governance. Without regularly measuring improvements in this area, it is difficult to determine the extent to which NSP has or will achieve this objective. Further, the future role of the Community Development Councils (CDCs) as official local governance bodies remains uncertain. As the NSP enters its third phase, the program faces several operational challenges, including delayed receipts of block grants, late payments to facilitating partners, and expansion to insecure areas of Afghanistan.

### What SIGAR Recommends

SIGAR is making 6 recommendations to help ensure that U.S. and other donor contributions to NSP are used as intended and that the program addresses challenges that could limit outcomes. Specifically, SIGAR recommends that the U.S. Ambassador to Afghanistan urge the Afghan government to take action to ensure that NSP funds retained by a hawalla dealer in Paktika Province are recovered and refunded to the ARTF, strengthen the monitoring system to measure and report on improvements in local governance, determine whether NSP-funded CDCs should become village councils, address the challenges of delayed payments for block grants and facilitating partners, and monitor expansion into insecure areas. In commenting on a draft of this report, the Embassy generally concurred with the report's findings and provided some additional information regarding the recommendations. SIGAR also considered comments from the World Bank and MRRD. Finally, SIGAR is also conducting a broader audit of the ARTF, which is currently the principal mechanism for providing direct assistance to Afghanistan.

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**ACRONYMS**

ANDS	Afghanistan National Development Strategy
ARTF	Afghanistan Reconstruction Trust Fund
CAO	Control and Audit Office
CDC	Community Development Council
CDP	Community Development Plan
DAB	Da Afghanistan Bank
FCPRTF	Food Crisis Policy Response Trust Fund
FMA	Financial Management Agent
IDA	International Development Association
IDLG	Independent Directorate of Local Governance
JSDF	Japanese Social Development Fund
MoF	Ministry of Finance
MRRD	Ministry of Rural Rehabilitation and Development
NGO	Non-governmental organization
NSP	National Solidarity Program
SIGAR	Special Inspector General for Afghanistan Reconstruction
USAID	U.S. Agency for International Development



## **Afghanistan's National Solidarity Program Has Reached thousands of Afghan Communities, but Faces Challenges that Could Limit Outcomes**

The National Solidarity Program (NSP), identified in Afghanistan's National Development Strategy as the government's principal community development program, is a multi-billion dollar community development and local governance program managed by the Afghan Ministry of Rural Rehabilitation and Development (MRRD). It is funded primarily through the multilateral Afghanistan Reconstruction Trust Fund (ARTF) which is administered by the World Bank.<sup>1</sup> From June 2002 to September 2010, U.S. contributions to the NSP totaled about \$528 million, making the United States the single largest donor. ARTF contributions flow through the Afghan national budget and provide a means by which the United States and other donors can channel development assistance directly through the Afghan government. During the 2010 donor conferences in London and Kabul, the U.S. government, along with other members of the international donor community, committed to channeling at least 50 percent of development assistance through the national budget of the Afghan government. Achieving this goal will depend to a large degree on whether the Afghan government is able to manage and account for the donor funds it receives for programs such as the NSP. We are also conducting a broader audit of the ARTF, which is currently the principal mechanism for providing direct assistance to Afghanistan.

This report includes the results of SIGAR's audit to (1) identify the extent and use of U.S. and other donor assistance to the NSP, (2) assess the level of oversight and internal controls over donor funds, (3) determine whether NSP is meeting its targets, and (4) highlight key challenges facing NSP as it begins its third phase. This report is part of a series of audits by SIGAR to address U.S. efforts to build Afghan capacity for enhancing accountability and preventing corruption. To accomplish these objectives, we collected and analyzed documents, data, contracts, and agreements from NSP, MRRD, the World Bank, NSP facilitating partners, community development councils, and Afghanistan's Control and Audit Office (CAO).<sup>2</sup> We reviewed a random sample of NSP files maintained at NSP headquarters in Kabul to verify that implementation procedures were followed, and reviewed independent evaluations of the NSP and facilitating partners. We also interviewed officials from the U.S. Agency for International Development

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<sup>1</sup> The ARTF was established in 2002 to provide a vehicle for international donors to pool resources and coordinate their support for the reconstruction of Afghanistan. Donor contributions enable the ARTF to finance both the essential operating costs of the Afghan government (recurrent cost window) and key national programs (such as NSP) under the Afghan National Development Strategy (investment window). The ARTF is governed by a management committee, consisting of representatives of the Asian Development Bank, Islamic Development Bank, UNDP, Afghanistan's Ministry of Finance, and the World Bank, with day-to-day administration of the fund performed by the World Bank. A monitoring agent has been appointed by the World Bank to ensure proper fiduciary management. A donor committee is regularly convened to discuss the management and administration of ARTF and to provide policy guidance.

<sup>2</sup> As Afghanistan's Supreme Audit Institution, the CAO is responsible for auditing the financial matters of the government, including international donor funds channeled through the Afghan government.

(USAID), the U.S. Embassy in Kabul, the World Bank, the Asian Development Bank, and the United Nations Assistance Mission in Afghanistan. In addition, we met with officials representing other donors to the NSP, including Denmark, Italy, and the United Kingdom. Further, we met with Afghan government officials who manage the program, as well as with officials from 9 of NSP's 28 facilitating partners. We conducted our work in Washington, D.C., and in Kabul and Parwan provinces in Afghanistan, from April 2010 to January 2011 in accordance with generally accepted government auditing standards. A discussion of our scope and methodology is included in appendix I.

## BACKGROUND

In 2003, the Afghan government launched the NSP to lay the foundation for a sustainable form of inclusive local governance, rural reconstruction, and poverty alleviation. The primary objectives of the NSP are to build local governance by setting up community development councils (CDCs) and training them to manage small-scale projects funded by block grants. NSP activities are grouped under four program elements:

1. **Governance:** assisting communities in establishing inclusive governance through democratic elections, reaching consensus on priorities and corresponding activities, and developing projects.
2. **Capacity building:** building the capacities of community members and community development councils in consensus building, financial management, operations and maintenance, and monitoring.
3. **Community block grants:** providing block grants to communities to fund NSP-approved projects.
4. **Linkages and service provision:** linking CDCs to government agencies, non-governmental organizations, and donors to improve access to services and resources.

The NSP is being implemented in 351 of Afghanistan's 398 districts and is located in all 34 provinces. The NSP contracts with facilitating partners (international and local non-governmental organizations) to work in specific districts. These partners are responsible for mobilizing communities to undertake development activities and promoting community adherence to NSP guidelines. Patterned after an earlier community empowerment and public works project<sup>3</sup> managed by MRRD, the NSP has been implemented in phases: NSP I, from May 2003 to March 2007; NSP II, from April 2007 to September 2011; and NSP III, from September 2010 to September 2015. Expected funding for all three phases will total about \$2.7 billion, excluding community contributions. Community contributions, mandated as part of NSP implementation, must equal at least 10 percent of project costs. Contributions can be in cash, labor, or in-kind.

Managed by MRRD, the NSP employs over 800 Afghan staff members at its headquarters in Kabul and in provincial offices throughout Afghanistan. NSP management oversight is provided by an inter-

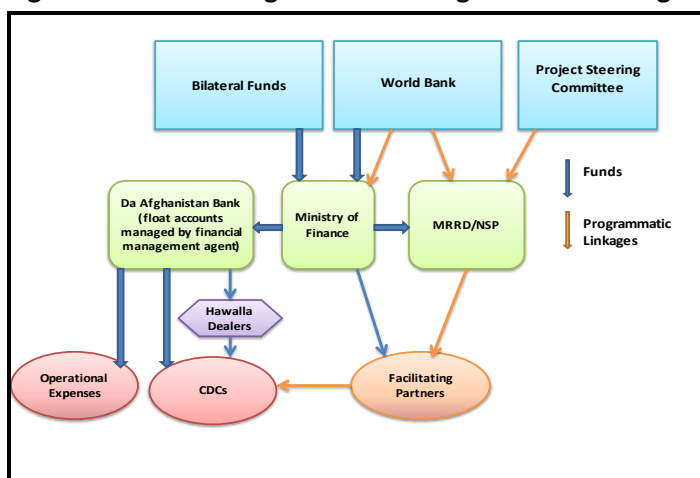
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<sup>3</sup> The Emergency Community Empowerment and Public Works Project, which began in 2002, formed the foundation of what would later become NSP.

ministerial project steering committee chaired by Afghanistan’s second vice-president, and is subject to requirements tied to international funding sources.

NSP activities are implemented by 28 facilitating partners,<sup>4</sup> made up of 26 non-governmental organizations (6 Afghan and 20 international), a U.N. agency, and a U.S. for-profit company. NSP staff members supervise the work of the facilitating partners, which are responsible for program facilitation at the village level. Elected members of CDCs manage block grants and implement community development projects, which are based on community development plans. The block grants are provided from NSP contributions transferred to CDCs by the Ministry of Finance (MoF) principally through Afghanistan’s central bank (Da Afghanistan Bank), but occasionally through traditional hawalla<sup>5</sup> dealers (see figure 1).

**Figure 1: NSP Funding Flows and Programmatic Linkages**



As of January 31, 2011, the NSP reported the following achievements:

- 26,110 communities mobilized;
- 53,610 project proposals funded; and
- \$793 million in block grants disbursed to CDCs.

In its third phase, the NSP is slated to reach an additional 15,800 communities, many of which are in insecure areas not covered by the two earlier phases. There are also plans to provide 11,900 of the CDCs already mobilized under the first two phases with a second round of block grants.

<sup>4</sup> This represents the number of facilitating partners at the time of our audit. The number has increased over time and can expand or contract according to need and performance. See appendix III for a complete list of NSP facilitating partners.

<sup>5</sup> Hawalla dealers are individuals engaged in an informal money transfer system common in the Middle East and South Asia.



## NSP HAS BEEN FUNDED ALMOST ENTIRELY BY INTERNATIONAL DONORS, OF WHICH THE UNITED STATES IS THE LARGEST CONTRIBUTOR

All NSP funding, with the exception of community contributions,<sup>6</sup> has been provided by international donors. As of September 2010, international donor contributions to NSP totaled more than \$1.5 billion. As shown in table 1, most NSP contributions were made through the ARTF, a multilateral trust fund administered by the World Bank. Another major source of NSP funding has been the World Bank's International Development Association (IDA).<sup>7</sup> In addition to multilateral trust funds and grants, international donors have provided about \$100 million in bilateral contributions directly to NSP.

**Table 1: NSP Contributions by Donor Category, 2002 to 2010**

Funding Source	As of September 2010 (USD millions)
ARTF (administered by World Bank)	\$940
IDA (World Bank)	\$436
Bilateral Donors	\$100
Japanese Social Development Fund (administered by World Bank)	\$42
Food Price Crisis Response Trust Fund (administered by World Bank)	\$8
<b>Total</b>	<b>\$1,526</b>

Source: SIGAR analysis of ARTF Monthly Report for September 22, 2010.

### The United States Is the Largest Donor of NSP Funds

The United States has contributed over one-third of all NSP international donor funding, making it the largest donor.<sup>8</sup> As of September 2010, the United States had provided about \$528 million to the NSP through direct and indirect funding (see table 2). This represents about 35 percent of total international donor contributions to NSP. The majority of U.S. funding for the NSP has been through the ARTF. U.S. contributions to the ARTF are made through a grant agreement<sup>9</sup> between USAID and the World Bank.

<sup>6</sup> According to World Bank officials, community contributions to NSP projects were supposed to be 10 percent, though they have averaged 17 percent.

<sup>7</sup> IDA is the part of the World Bank that helps the world's poorest countries. IDA complements the World Bank's other lending arm—the International Bank for Reconstruction and Development, which provides middle-income countries with capital investment and advisory services.

<sup>8</sup> Canada is currently the second largest donor, providing contributions of \$148.5 million--\$147.4 million through the ARTF for NSP and \$1.1 million bilaterally.

<sup>9</sup> USAID Grant Agreement No. EEE-G-00-02-00025-00, dated June 20, 2002.

The grant agreement, signed in 2002, provided an initial \$5 million in support of the ARTF. As of September 2010, the agreement had been modified 35 times, raising the total amount of U.S. contributions to \$972 million. Of that amount, \$490 million was provided to the NSP based on preferencing language in the grant modifications. Donors use preferencing language to designate the specific ARTF-funded investment programs they wish to support. Although the World Bank does not guarantee that these preferences will be honored, USAID officials confirmed World Bank statements that showed all U.S. preferences for NSP have been honored by the ARTF.

**Table 2: Total U.S. Contributions to NSP Since 2002**

Type of Funding	Total U.S. Contributions to NSP (USD millions)
U.S. Preferences to NSP through ARTF	\$490
U.S. Portion of IDA Grants to NSP	\$37
Bilateral U.S. Funding to NSP	\$1
<b>Total</b>	<b>\$528</b>

Source: SIGAR analysis of USAID and World Bank data as of September 23, 2010.

U.S. funding for the ARTF and the NSP has been provided, for the most part, from Economic Support Fund appropriations based on congressional directives. For example, the 2009 Supplemental Appropriations Act<sup>10</sup> directed that not less than \$70 million of Economic Support Funds be made available for NSP. The 2010 Consolidated Appropriations Act<sup>11</sup> directed that another \$175 million of Economic Support Funds be made available to NSP. USAID met these directives by providing \$140 million and \$175 million in Economic Support Funds for fiscal years 2009 and 2010, respectively. In addition, the 2010 National Defense Authorization Act authorized the U.S. Secretary of Defense to transfer up to \$50 million of Commander’s Emergency Response Program funds to the U.S. Secretary of State for NSP. This brought the total U.S. contribution for fiscal year 2010 to \$225 million.

In addition to USAID contributions to the ARTF, we estimate that the United States has contributed another \$36.7 million to NSP through its contribution to the World Bank’s IDA. Although the World Bank does not track assistance by donor to specific IDA-funded programs, we developed a methodology with the Office of the U.S. Executive Director at the World Bank for estimating U.S. IDA contributions to NSP.<sup>12</sup> In addition to its contributions through the World Bank-administered ARTF and IDA, the United States also provided about \$1.1 million in direct funding for NSP programming in Kandahar province. These funds were provided bilaterally, rather than through the ARTF, as the ARTF does not accept funds designated for specific geographic areas.

<sup>10</sup> Public Law 111-32, Supplemental Appropriations Act, 2009.

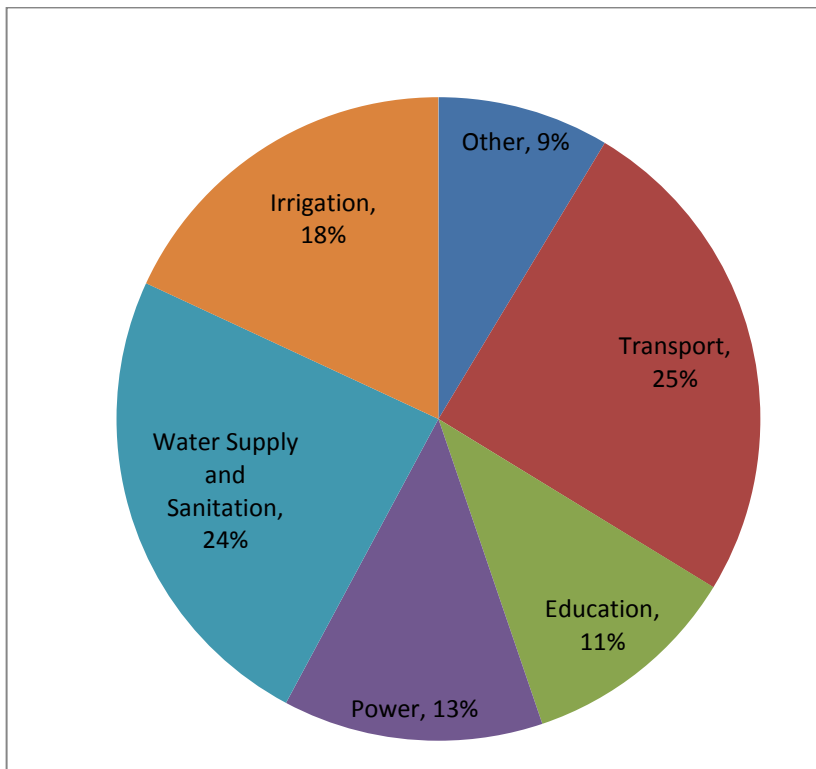
<sup>11</sup> Public Law 111-117, Consolidated Appropriations Act, 2010.

<sup>12</sup> According to the Office of U.S. Executive Director to the World Bank, the estimated U.S. portion of the IDA grants provided to NSP was approximately 8.4 percent of the total amount of \$436 million of IDA grants provided from 2002 to 2010. Thus, the U.S. portion was calculated to be about \$36.7 million.

## NSP Funds Are Primarily Used for Community Block Grants

The majority of NSP funds (about 72 percent) are used for community block grants. Community block grants finance small development projects managed by CDCs. Projects are typically for infrastructure development in areas such as transportation (e.g., tertiary roads), water supply and sanitation, small-scale electric power, and irrigation (see figure 2). Block grant amounts, limited to \$60,000 per community, are determined by the number of families in a given community (up to 300 families, multiplied by \$200 per family).

**Figure 2: Sectoral Allocation of NSP I and NSP II Block Grant Funding**



Source: SIGAR analysis of World Bank data as of January 2011.

Note: "Other" category includes projects in agriculture, health, livelihoods, public building, and emergency response.

Approximately 19 percent of NSP funds pay for facilitating partner costs, which include overseeing the election and training of CDC members, providing assistance to draft community development plans, and implementing projects. The remaining 9 percent covers the administrative costs of NSP staff, including salaries, offices, benefits, travel, and general operating expenses (see table 3).

**Table 3: NSP Costs by Expenditure Category**

Expenditure Category	NSP I & II (percentage)
Community Block Grants	72
Facilitating Partner Costs	19
NSP Administration	9
<b>Total</b>	<b>100</b>

Source: SIGAR analysis of NSP Finance Department data.

Since 2005, the NSP's financial statements have been audited on an annual basis by Afghanistan's supreme audit agency, the Control and Audit Office (CAO). The audited statements show that, as of March 20, 2010, the NSP had expended a total of \$789 million. See table 4 for reported annual expenditures.

**Table 4: NSP Annual Expenditures, SY1383-1388**

Annual Expenditures	
Year	USD millions
SY 1383	\$26
SY 1384	\$48
SY 1385	\$123
SY 1386	\$239
SY 1387	\$196
SY 1388	\$157
<b>Total</b>	<b>\$789</b>

Source: SIGAR analysis of annual NSP financial statements audited by CAO.

Note: The Afghan solar year (SY) typically ends on March 20. The period in Table 4, SY1383-1388, equates to March 20, 2004 – March 20, 2010. All expenditures in the table occurred during NSP I and NSP II.

According to NSP III documentation, the proposed budget for the final phase of the program from September 2010 to September 2015 is about \$1.5 billion, or about \$300 million per year. This represents a substantial increase in planned expenditures over prior years and provides additional funding opportunities for donors.

## **NSP FUNDS ARE SUBJECT TO A WIDE RANGE OF OVERSIGHT MECHANISMS AND INTERNAL CONTROLS, BUT USE OF A HAWALLA DEALER LED TO DIVERSION OF FUNDS IN ONE PROVINCE**

The NSP operates under a series of oversight mechanisms and internal controls that are detailed in its implementing documentation, contracts, agreements, and operational manual. International standards for internal control and auditing help organizations provide reasonable assurance that objectives relating to effectiveness, accountability, compliance, and safeguarding of resources are being achieved.<sup>13</sup> However, those same standards also indicate that an effective internal control system, no matter how well conceived and operated, can provide only reasonable – not absolute – assurance to management about the achievement of an entity's objectives. World Bank mechanisms provide one level of oversight through management committees, supervision missions, and regular reporting. Because NSP funds are channeled through the Afghan national budget, they are subject to government-wide controls, including annual financial audits. Further, MRRD/NSP officials manage facilitating partners and activities that must follow the NSP operational manual. Communities provide oversight of NSP activities by participating in CDC elections, following NSP spending information posted on signboards, and social audits. We found that these controls provided reasonable assurance that NSP funds were used as intended. While our tests for compliance with documentation requirements were positive, MRRD/NSP identified fraudulent activity involving about \$2.8 million in NSP funds that occurred in a particular Afghan province even though all the required paperwork had been submitted and filed.

### **World Bank Agreements and Policies Mandate Oversight of NSP**

The NSP is subject to a wide range of internal control mechanisms mandated by the World Bank in grant agreements and its own policies to monitor and account for donor funds. For example, donor funds provided to the NSP through contributions to the ARTF are subject to several oversight mechanisms applied to those trust funds by the Afghan government and the World Bank. Afghan public expenditures are subject to government-wide controls that are periodically assessed by the World Bank.<sup>14</sup> ARTF funds, which are a sub-set of on-budget funds, are subject to additional fiduciary oversight by the World Bank and its agents. These additional oversight mechanisms include management and donor committees, periodic mid-term reviews, preparation and supervision missions conducted by the World Bank, and

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<sup>13</sup> According to the International Organization of Supreme Audit Institutions' Guidelines for Internal Control Standards for the Public Sector, internal controls are defined as an integral process that is affected by an entity's management and personnel and are designed to address risks and provide reasonable assurance that, in pursuit of the entity's mission, objectives relating to effectiveness, accountability, compliance, and safeguarding of resources are achieved.

<sup>14</sup> According to the World Bank, these controls comprise a framework whereby public funds in the Afghan government are controlled through a single budget that is prepared in an orderly and transparent manner, approved by Parliament, and under which all uses are permitted only against due approvals of the appropriation holder. Accounting and payments for all transactions under the budget is concentrated in the Treasury Department of the Ministry of Finance, which has contributed to sound financial reporting. This reporting is subject to oversight by the Parliament and the external auditor. See "Afghanistan: Public Financial Management Performance Assessment" (World Bank and United Kingdom's Department for International Development, June 2008).

specific financial and procurement requirements included in the grant agreements between the World Bank and the Afghan government that call for periodic financial reporting, including annual financial audits of NSP expenditures.

The World Bank's governance and fiduciary framework for the ARTF, including NSP, indicates that separate donor agreements set out the fiduciary and management responsibilities of the World Bank in its role as administrator of the fund.<sup>15</sup> The World Bank is responsible for tracking contributions and maintaining records and accounts of the trust fund. The ARTF management committee, consisting of representatives of the Asian Development Bank, the Islamic Development Bank, the UN Development Program, the World Bank, and the Afghan Ministry of Finance (MoF)<sup>16</sup> meets monthly to make resource allocations and report to donors on the use of funds. Also, an ARTF donor committee is responsible for meeting quarterly, reviewing ARTF progress, and guiding the management committee on ARTF allocation strategies.

The ARTF management committee meets monthly to discuss ARTF issues, including NSP problems and solutions. For example, minutes from a September 2010 management committee meeting reported that members raised concerns about the low disbursement rate for NSP II and whether the program could absorb an increase in funding; the accessibility of 10,000 communities not yet reached by the program; the costs of CDC capacity building; the impact and sustainability of the investment; and links with other national programs. Based on these discussions, the management committee approved in principle the provision of \$250 million for NSP. However, the chair noted that the World Bank would not sign the agreement until after a supervision mission to ensure that outstanding issues were addressed to the satisfaction of the World Bank.

A committee of ARTF donors also provides oversight to help ensure that NSP funds are used for intended purposes. For example, minutes of a November 2009 ARTF donor committee meeting indicated that the NSP director presented the findings of an MRRD investigation into media allegations that 40 percent of NSP funds in Farah province were going to the Taliban. According to the minutes, the donors welcomed the findings of the investigation, which concluded that the allegations were baseless. U.S. oversight on this committee is provided by a USAID staff member assigned as the Grant Officer's Technical Representative for the ARTF cooperative agreement. The official monitors U.S. funds contributed to ARTF, including those for NSP. The USAID official reported attending ARTF donor committee meetings and reviewing ARTF reports. USAID's active participation in the committee was confirmed by the World Bank.

As a condition of accepting World Bank funds, the Afghan government agreed to periodic reviews of the use of those funds. The World Bank conducted a completion review of NSP I in 2007 and undertook a mid-term review of NSP II in 2008 to determine the status of the program and identify areas of focus for an interim supervision mission scheduled for September of that year. The review resulted in two principal recommendations—to improve the quantity and quality of NSP services, as well as their cost

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<sup>15</sup> The World Bank produces quarterly and annual reports for ARTF that provide financial and program updates on NSP for ARTF donors and discuss implementation challenges.

<sup>16</sup> The MoF attended the ARTF management committee as an observer until January 2011 when it became a full member.

effectiveness. In addition, the review made 30 specific recommendations. In response to the review, NSP officials formed working groups that developed plans to address the recommendations. The reviews are available on the World Bank's public web site.

The World Bank also conducts supervision missions to periodically assess progress in meeting development objectives. For example, a mission in April 2009 to Bamyan Province found that NSP was likely to achieve its development objectives, but identified issues, including the lack of timely payments to facilitating partners and block grants to communities, that required attention. Another mission, in November 2009, was to take place in Badakhshan Province, but ended up going to Kandahar, a less secure area, as suggested by USAID. A third mission took place between December 2009 and February 2010 in Kabul. The objective of the Kabul mission was to outline key strategic decisions, explore new implementation methods, and continue formal project preparation of NSP III. The mission included broad participation of various stakeholders, including community development councils, NSP facilitating partners, and donors. The mission resulted in the documentation of key agreements and key tasks and dates to be completed by NSP management.

### **Afghan Government Provides Oversight as Management of NSP Is Increasingly Undertaken by Afghan Officials**

Until September 2006, management of the NSP was primarily in the hands of an international oversight consultant contracted by MRRD. After that date, management began shifting to Afghan nationals who now fill all senior NSP positions, with the exception of the finance department whose leadership is outsourced to an international consulting firm. According to the ARTF governance and fiduciary framework, monitoring and evaluation is the responsibility of the implementing partner, the Afghan government. The grant agreement between the Afghan government and World Bank for NSP II requires MRRD to monitor and evaluate the program, submit quarterly progress reports and ensure that a financial management system produces quarterly financial statements that are audited annually. The agreement also includes provisions requiring MRRD to be responsible for policy and strategy development and application, coordinating with other ministries, managing relations with facilitating partners, approving and ensuring the quality of community projects, capacity development, and financial management with the assistance of an external management consultant firm. Among other things, the agreement also requires the Afghan government to maintain an inter-ministerial steering committee to provide strategic and managerial guidance to the MRRD. Further, the agreement requires the MRRD to carry out program activities in accordance with operational and financial management manuals that cannot be amended or waived without World Bank approval. Finally, the agreement places limitations on the MRRD's procurement of goods and services, as well as its withdrawal of grant funds, and requires the Afghan government to conduct a survey of institutional and social indicators, impact evaluations, and evaluations of facilitating partners.

According to facilitating partners, the transfer of NSP management from international oversight consultants to Afghan nationals is a positive development for the NSP. Afghans now hold all senior management positions, with the exception of those in the finance department. This "Afghanization" is in line with the reaffirmation of Afghan leadership called for by participants at the 2010 conferences in London and Kabul. In both conferences, participants expressed support for Afghan leadership to improve Afghanistan's security, development, and governance.

Since the MRRD lacked capacity and experience with community-driven development programs when the NSP was initially designed, a management structure that included an international management consultant that would work with NGO and UN facilitating partners was created. Once the NSP was officially launched as a nationwide program in 2003, the first management consultant contracted was GTZ-IS, German Technical Cooperation International Services (September 2003 to March 2007), with 17 international positions. Consulting firm Maxwell Stamp followed (April 2007 to March 2010), with 10 international positions. However, the number of NSP management positions filled by non-Afghans has decreased significantly since then. In March 2010, the MRRD contracted with Deloitte Consulting Overseas Projects to manage NSP's Finance Department, but Deloitte employs only two international personnel in that department. Afghans have been appointed to leadership roles for all other NSP units.

Facilitating partners reported satisfaction with the Afghan-led management. For example, facilitating partners interviewed by SIGAR praised NSP management's for both its responsiveness to issues they raised and for the increased services provided to assist them. The increased services included the establishment of a facilitating partner management department, monthly coordination meetings, and a working group to discuss facilitating partner contract issues. A member of the ARTF management committee stated that "MRRD is a government within a government and the only ministry with functioning provincial offices and a developed core of expertise." NSP staff in particular have developed and carried their capacity to other ministries. The official added that higher salaries attract better qualified people. MRRD/NSP employees are contractors, not civil servants. As such, they are paid about five times that of civil servants.<sup>17</sup> Their salaries are paid entirely from donor contributions to NSP.

Program management also includes an NSP monitoring and evaluation department to oversee project implementation. This department is responsible for coordinating the collection and reporting of data relating to program performance indicators defined in the results framework in the NSP operational manual. According to the head of the department, each NSP Provincial Management Unit had a 2-person team to monitor and evaluate NSP projects within their province. The information collected by these teams is fed into the NSP management information system, which uses the information to report on community project progress and problems.

### **NSP Expenditures Are Audited Annually, although Prior Audit Reports Were Not Completed in a Timely Manner**

NSP donors rely on financial audits of NSP funds to provide assurance that those funds are properly used. The financing agreement between the World Bank and the Afghan government requires the CAO to conduct annual financial audits of NSP financial statements. According to a prior SIGAR audit report, the CAO relies on international consultants and advisors to conduct audits in accordance with international auditing standards.<sup>18</sup>

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<sup>17</sup> The example cited was that MRRD/NSP staff would earn about \$1,000 for a month, where a civil servant would make about \$200 per month.

<sup>18</sup> See SIGAR Audit-10-8, *Afghanistan's Control and Audit Office Requires Operational and Budgetary Independence, Enhanced Authority, and Focused International Assistance to Effectively Prevent and Detect Corruption*, April 9, 2010.



The CAO has audited NSP financial statements annually since 2005. Those audits, conducted in accordance with standards issued by the International Organization of Supreme Audit Institutions, have identified numerous issues that have been addressed and resolved by NSP management. However, the CAO has not always issued its NSP audit reports in a timely manner. International Organization of Supreme Audit Institutions audit standards on timeliness indicate that the audit opinion or report should be available promptly to be of greatest use to readers and users, particularly those who have to take necessary action. The terms of the financial agreement between the Afghan government and the World Bank, signed on April 24, 2006, states that NSP financial statements would be audited annually and that audited financial statements would be provided to the World Bank as soon as available, but in no case later than 6 months after the end of the fiscal year. The CAO's audit report for the year ending March 19, 2008 (SY 1386), was due by September 19, 2008, but was not issued until June 30, 2009, over 9 months late. Similarly, the CAO's audit report for the year ending March 20, 2009 (SY 1387) was issued on January 21, 2010, over 4 months later than the date stipulated by the same agreement. According to NSP records, the audits were delayed due to the late preparation of consolidated financial statements and the unusually long time it took to find an international public accounting firm acceptable to the World Bank to help the CAO audit the NSP's financial statements.

The effect of these delays was that the MRRD was unable to take timely action on audit findings that included millions of dollars of questionable and potentially ineligible costs identified during both audits. For example, the audit report for SY 1386 included a qualified opinion due to \$6.3 million in potentially ineligible or unsupported costs. The audit report for SY 1387 also included a qualified opinion due to \$3.6 million in questioned costs. Further, the report for SY 1387 disclosed that more than 1,900 completed projects with approximately \$25.7 million of advance payments made since 2004 took more than one year to complete. Both audits questioned payments to the MRRD for staff members who did not work directly for the NSP. A senior MRRD official stated that the MRRD had resolved this issue by obtaining approval from the World Bank to pay a portion of contracted MRRD staff costs from NSP funds. The amount allocated was \$187,665 per month.

Subsequent to our audit fieldwork, SIGAR received a copy of the NSP's audit report for SY 1388, the annual period ending March 20, 2010. That report included an unqualified opinion and was submitted by the CAO within the 6-month period required by the World Bank financing agreement. Consequently, SIGAR is not including a recommendation to improve the timeliness of NSP financial audit reports.

### **Implementation of NSP Has Been Enhanced by Experienced Facilitating Partners**

According to MRRD, NSP, and ARTF management committee members, the use of facilitating partners with prior experience in Afghanistan provides a number of advantages:

- Gives the MRRD/NSP's an ability to "buy" ready implementation capacity from organizations with decades-long presence in Afghanistan, established community linkages, and specific expertise.
- Provides the NSP with a continuous presence by co-locating non-NSP activities with NSP activities, which provides de facto additional NSP resources and allows the NSP work to continue during periods when facilitation payments to facilitating partners are delayed.

- Builds upon the facilitating partners willingness to go to great lengths to implement the NSP, including traveling to remote areas on foot or by donkey, and risking their lives by working in insecure environments.

Facilitating partners provided the NSP with immediate capacity, outreach, and a measure of trust in the early days of the program. The NSP management structure, on the other hand, had to be created. Facilitating partners also provided a deeper reach into communities as they had offices in districts, whereas the MRRD/NSP established its offices in provincial capitals and Kabul, urban areas where NSP is not normally implemented.

Facilitating partners receive payments of fixed amounts from the NSP as compensation for facilitation work according to specific milestones outlined in their contracts. NSP officials have conducted two evaluations of facilitating partners. The results of the evaluations indicated that facilitating partners with long-term experience in Afghanistan were able to become leaders in NSP facilitation because they built upon their local experience with rural development. Moreover, they added value to a range of NSP activities, including social mobilization.

### **Community Members Oversee Block Grant Spending**

Communities also provide oversight of NSP funds spent in their villages through community participatory monitoring of the use of block grants funds. During project implementation, public notice boards announce NSP projects and funding amounts. Signboards are often posted at local mosques where community members gather regularly. Following project completion, members of some communities, assisted by facilitating partners, form a committee to audit NSP development projects, explain their findings to the rest of the community, and hold CDC members to account for their spending. While these “social” audits will be more widely introduced under NSP III, facilitating partners reported that such audits under NSP I and II identified instances of fraud when reviewing project receipts, including those for travel and meals of CDC members.

The high level of community involvement in NSP activities—CDC elections, social audits, and community contributions—has resulted in a degree of local ownership of NSP-funded projects which helps safeguard assets. Facilitating partners reported that, in some cases, community members intervened and recovered money when block grant funds were stolen by thieves or embezzled by CDC members. According to one facilitating partner, the Taliban are less likely to burn NSP schools because communities defend them.

### **NSP Files Show Evidence of General Compliance with Operational Manual**

Many of the NSP’s internal controls over implementation are detailed in its operational manual. The operational manual guides NSP communities, CDCs, NSP facilitating partners, and NSP management in their day-to-day implementation of the program. Mentioned specifically in the Afghan government’s grant agreement with the World Bank, the operational manual is a legally binding document. The manual details the program’s objectives and provides guidelines, forms, and a timeline for all implementation processes and procedures. The operational manual is revised periodically to

incorporate lessons learned and the program's changing dynamics.<sup>19</sup> The World Bank must approve any changes to the operational manual.

To assess NSP compliance with the operational manual, we randomly selected a sample of 62 projects, drawn from a universe of 664 projects initiated after September 1, 2009,<sup>20</sup> and completed by July 29, 2010. (See appendix I for details on our scope and methodology.) For each of the 62 projects, we reviewed administrative, accounting, and procurement files located at NSP headquarters in Kabul, Afghanistan. We tested the files for existence and completeness, including appropriate approvals, stamps, and signatures. We found that required forms for the sampled projects were in place and complete more than 90 percent of the time.

Additionally, we randomly selected 10 projects from the 62 sampled projects to conduct a more detailed review of project documentation. We found that all of the required project completion forms for the ten projects had been completed. Due to security concerns, we were unable to visit any of the selected project sites, but NSP officials provided us with copies of site inspection reports and photographic evidence for nine of the projects to show that they had been completed as planned.

### **About \$2.8 Million in NSP Block Grants Did Not Reach Intended Beneficiaries**

According to a World Bank report of a supervision mission that occurred during October-November 2009, the NSP reported that a diversion of block grant funds had occurred. According to NSP records, in June 2009, program officials became aware that approximately \$2.8 million<sup>21</sup> in NSP funds for 295 communities in Paktika Province were retained by a hawalla dealer and not transferred to the CDCs for whom they were intended. Despite investigations by NSP officials and interventions on the part of the Afghan Attorney General's Office, the hawalla dealer continues to retain the majority of these funds and refuses to deliver them to the intended communities.<sup>22</sup>

NSP records indicate that, contrary to the standard practice of distributing NSP block grants to participating communities through a provincial branch of Da Afghanistan Bank, the NSP's Finance Department<sup>23</sup> agreed to make disbursements to certain communities in Paktika Province using a hawalla dealer. This decision was based on requests from community members who found it difficult and dangerous to retrieve cash from the bank, which was located in the provincial capital. In September 2005, a contract was finalized between the NSP Finance Department and a hawalla dealer to provide

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<sup>19</sup> Version V, which became effective on August 15, 2009, is the current version of the operational manual.

<sup>20</sup> We selected projects that started after September 1, 2009, to ensure that they were implemented after the current version of the operational manual (version V) became effective.

<sup>21</sup> The actual amount misappropriated was in Afghan currency (Afghanis). Fluctuations in the U.S. dollar/Afghani exchange rate over the last three years resulted in the amount varying from \$2.8 to \$3.2 million.

<sup>22</sup> Due to its urgent nature, SIGAR informed the U.S. Ambassador to Afghanistan of this issue in December 2010 through a separate letter prior to completing this audit report.

<sup>23</sup> During this period, the NSP Finance Department was managed by Maxwell Stamp PLC (a British company which was then serving as the NSP Management Support Consultant, and to whom the NSP Finance Department was entirely outsourced at the time of the incident).

block grants to those communities. The contract authorized the hawalla dealer to be paid a transfer fee of 2 to 3 percent of the amount of block grants delivered.

According to an NSP investigative report, after verifying that the hawalla dealer was retaining the funds, the NSP pressured him to sign a detailed agreement on how he would reimburse the undelivered money. NSP documents indicate that, under this agreement, he made initial payments equivalent to about \$122,000, but that he refused to repay the remaining amount. Additional NSP documentation shows that the hawalla dealer received the equivalent of \$84,648 in transfer fees related to the \$2.8 million in undelivered block grants. According to the NSP, the MRRD has hired lawyers to follow up on this case and to recover the funds.

NSP investigating officials concluded that although the hawalla dealer didn't transfer the funds as agreed, provincial government officials, private facilitating partners, and the respective community development councils also circumvented internal controls. Although the MRRD, the NSP, and the World Bank have taken actions to address this issue, it remains unresolved. Because NSP does not typically use hawalla dealers to transfer block grant funds, we note that this situation appears to be an isolated case.

## **NSP REPORTS MEETING QUANTITATIVE TARGETS, BUT MEASUREMENT OF CHANGES IN LOCAL GOVERNANCE NEEDS STRENGTHENING AND THE FUTURE OF CDCS IS UNCERTAIN**

At the conclusion of its first phase, the NSP reported meeting or exceeding the majority of its quantitative targets, such as the numbers of communities mobilized and projects implemented; however, the NSP has not effectively measured progress toward its qualitative objective of improving local governance in Afghanistan. Without obtaining data on specific indicators to track changes in local governance, it is difficult to determine whether the NSP is making progress toward achieving its desired outcome in this area. Additionally, it is difficult to know whether CDCs are best placed to assume the duties of not-yet-elected local government bodies known as village councils.

### **NSP Reports Meeting or Exceeding Its Quantitative Targets**

The NSP reported achieving, and sometimes exceeding, the majority of its quantitative targets, such as the number of communities mobilized and projects funded, during its first phase of program implementation. A report issued by the World Bank at the conclusion of NSP I showed that the program had exceeded 4 important project development objectives.<sup>24</sup> According to the report, as of March 2007, NSP I had resulted in the election of 10,321 CDCs compared to a target of 8,334—achieving 124 percent of that goal. The report stated that NSP I assisted 10,082 villages prepare community development plans, achieving 126 percent of the target of 8,000 villages. Against a goal of having 40 percent of women participate in CDC elections, NSP I reported achieving a rate of more than 50 percent. Finally, the target of having 90 percent of NSP I communities contributing 10 percent of project costs was exceeded when 100 percent of communities met that mark with contributions averaging about 14.5 percent of project costs. (See appendix II for a more complete list of NSP I accomplishments.)

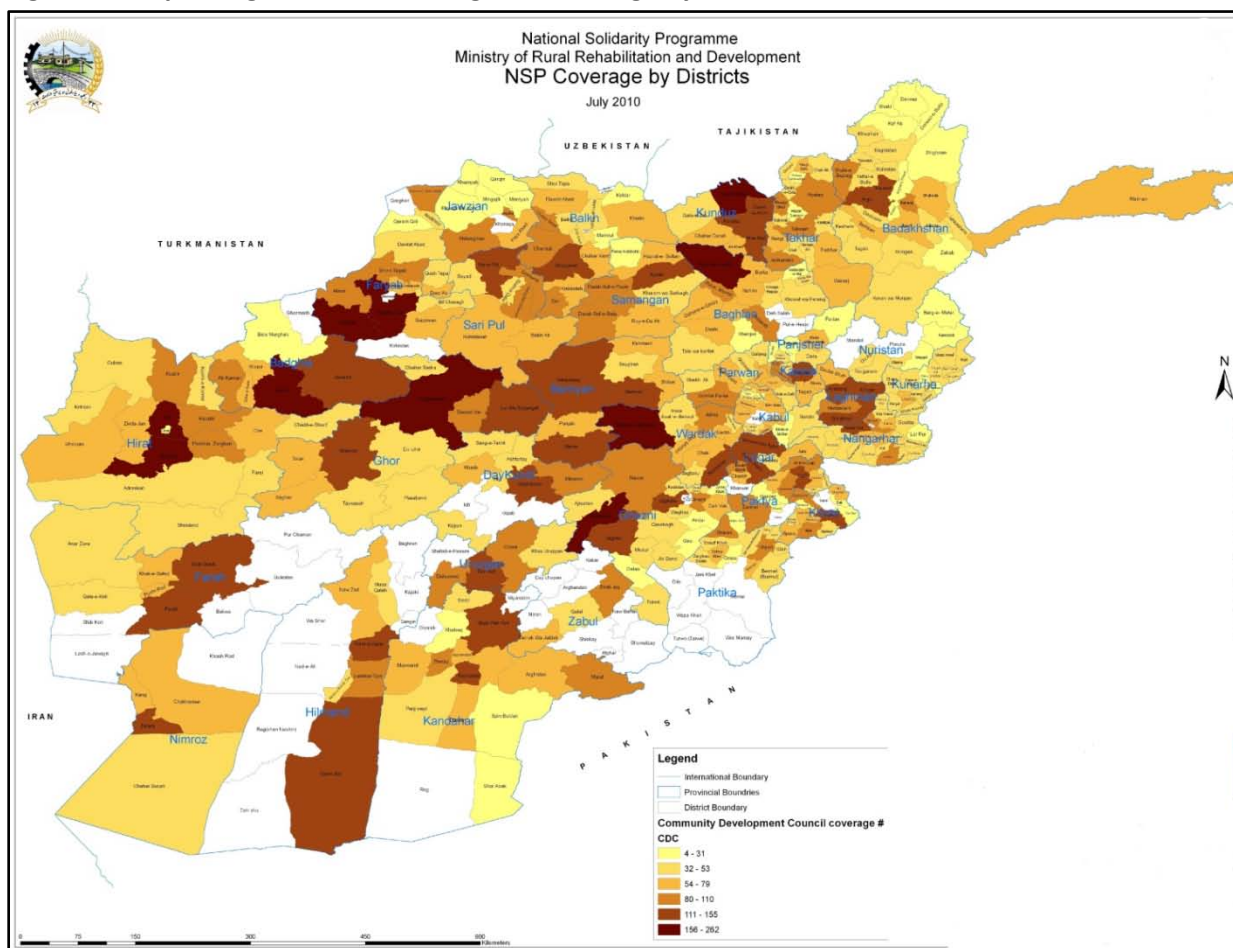
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<sup>24</sup> *Implementation Completion and Results Report on a Grant to the Islamic Government of Afghanistan for an Emergency National Solidarity Program* (Report No: ICR0000524), October 24, 2007, The World Bank.

By January 2011, NSP management reported that the program had resulted in a total of 44,972 projects completed, 25,875 villages with elected CDCs, and \$793 million in block grants disbursed to CDCs. However, final achievements against NSP II targets will not be known until the completion of NSP II activities in September 2011.

The NSP has “mobilized,” or begun working with, communities in all 34 provinces of Afghanistan. The NSP has projects in 361 (91 percent) of the country’s 398 districts and provincial centers. Figure 3 illustrates the extent to which the NSP has been implemented throughout the country. As indicated by the uncolored portions of the map, NSP has not yet reached a number of districts in insecure areas. However, NSP III is aiming for nationwide coverage by establishing CDCs in 15,800 new communities, many of which are located in these insecure districts.

**Figure 3: Map of Afghanistan, Showing NSP Coverage by District**



Source: MRRD/NSP website: [www.nspafghanistan.org](http://www.nspafghanistan.org)

Note: Uncolored districts indicate the lack of CDCs. As can be seen, most of these districts are in the southern (less-secure) areas of the country.

## Monitoring of Progress Toward Achieving NSP's Governance Objective Needs Strengthening

In its "Performance Monitoring Indicators Handbook," the World Bank defines performance indicators as measures of impacts, outcomes, outputs, and inputs that are monitored during project implementation to assess progress toward project objectives. According to the handbook, performance indicators are used to evaluate a project's success and should be integrated with the monitoring and evaluation procedures used by the World Bank and its clients. However, the NSP has only recently begun measuring progress toward achieving one of its primary objectives, the improvement of local governance due to NSP activities, and relies on external evaluations for a full assessment of the program's impact in that area.

The results framework for NSP III proposes using assessments, surveys, and samples, conducted at regular intervals, to measure changes in community-level governance. However, many of these methods were not used during the earlier phases of the program. Although the NSP has been implemented for more than seven years, the following program performance indicators were not established until 2010:

- Percentage of communities that recognize CDCs as legitimate bodies;
- Percentage of CDCs able to perform their functional mandates in community development, project implementation, and conflict resolution;
- Percentage of women representatives on CDCs involved in decision making; and
- Number of CDCs that attempt to form linkages with government or non-government actors.

The NSP's monitoring and evaluation department produces implementation and post implementation monitoring reports, but it does not routinely collect data and report on progress toward targets established for these indicators. Instead, the NSP relies on external evaluators to measure the impact the NSP is making with regard to these and other performance indicators.

A mid-term evaluation of NSP I undertaken for the MRRD in 2005-06 by the University of York<sup>25</sup> found that, while their composition and functions varied between communities, CDCs were emerging as legitimate local governance institutions. However, this conclusion was based on case studies of only 18 CDCs.

The World Bank is funding research to study changes in local governance as a result of the NSP, but this has been outside the NSP's regular data collection and reporting systems. In 2007, the World Bank commissioned a multi-year study to undertake an assessment of the NSP's economic, institutional, and social impacts.<sup>26</sup> While preliminary research shows that the NSP created functional village councils, improved villagers' access to services, and increased the engagement of women in several aspects of community life, the indicators used to obtain these findings have not been included in the NSP's weekly

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<sup>25</sup> Mid-term Evaluation of the National Solidarity Programme (NSP), Afghanistan, May 2006 by the Post-War Reconstruction & Development Unit, University of York.

<sup>26</sup> Information pertaining to this study, being conducted by researchers from Harvard University and the Massachusetts Institute of Technology, can be obtained from the evaluation website at <http://www.nsp-ie.org>.

and monthly reporting. Furthermore, the NSP does not routinely collect data or report on some indicators that could be used to track progress toward the important objective of improving local governance. For the example, the NSP does not report on the number of signboards posted and social audits undertaken. Nor does it report on the number of CDCs that have received and managed funds from other government ministries, nongovernmental organizations, or other sources, although facilitating partners report that this is occurring.

As a result of the NSP not establishing baseline indicators early in the program, and not measuring progress under newly established indicators through regular data collection and reporting on changes in local governance, it is difficult to determine the degree to which NSP activities have or will result in improvements in local governance in rural Afghan communities. Moreover, while the capability of CDCs to assume increased responsibilities in the role of village councils has reportedly improved, the body of data to support their increased capacity does not exist.

### **CDCs Are Expected to Fill the Role of Village Councils, but Have Not Yet Received Authority to Do So on a Permanent Basis**

Although the MRRD, the MoF, and international donors support the conversion of CDCs to village councils, the local government bodies described in the Afghan constitution, a new Afghan government sub-national governance policy does not envision CDCs filling that role and proposes holding elections for 38,000 local government bodies. The lack of available reporting on changes in local governance, as a result of CDC creation, means the MRRD and the international community lack data to strengthen their argument that such a conversion has merit. Moreover, if CDCs are not converted to local government bodies, then the investment in the establishment and capacity building of CDCs was primarily for the purposes of implementing small projects rather than to improve local governance, which was an original objective of the NSP.

Although the Afghanistan National Development Strategy states that the role between proposed village councils and the CDCs established under NSP would be clarified, the legal status and post-NSP future of CDCs has never been fully clarified or finalized by the Afghan government. CDCs are not specifically addressed in the Afghan constitution and they have no political history since they were created out of a development project. Early NSP I language laying out the vision of CDCs described them as future advocates for and monitors of services from sub-national government bodies. They were not described as future governance bodies or long-term conduits of funds for services at the local level. However, when NSP II was being planned in late 2006, the language was changed to reflect the MRRD's vision that CDCs would be recognized as the "lowest form of local governance, institutionalized at the village level, in line with the Constitution." The MRRD also proposed that CDCs be recognized as legal bodies to harness development resources from other ministries and sources.

In 2007, CDCs were provided a basic legal framework through the Community Development Council By-Law of SY 1385 (2007) that was approved by Presidential Order 3138. The CDC By-Law described the purpose and working procedures of CDCs. According to the By-Law, CDC objectives were to work within communities to improve and strengthen local governance, promote community welfare, and strengthen a sense of solidarity. However, the By-Law did not grant CDCs the status of village council, one of the local governing bodies specified in article 140 of the Afghan constitution. Article 140 calls for the

establishment and election of local governing bodies, but does not specify a timeframe by which this is to occur for Afghan villages, numbering about 38,000.

The MRRD, the NSP, and facilitating partners have considered CDCs organizations suited to assuming the role of village councils. World Bank NSP III documentation noted that MRRD; the Ministry of Finance; the Ministry of Agriculture, Irrigation and Livestock; and the Independent Directorate of Local Governance (IDLG) agreed that a sustainable role for CDCs with respect to rural development would be promoted. According to the documentation, a transformation of CDCs into village councils was envisioned. However, the IDLG appears to have another vision for the establishment of village councils.

The 2010 Sub-national Governance Policy developed by IDLG calls for elections in 2011 for village councils. The policy notes that village councils will, among a long list of responsibilities, design and implement development plans, manage funds, and coordinate with line ministries, tasks similar to those performed by CDCs. However, the policy does not call for the conversion of CDCs into village councils, nor does it establish procedures for training elected village council members in the responsibilities for which they will be tasked, a process that has taken about 6 months per CDC under NSP I and II. The policy suggests that after 2011, CDCs may continue as civil society organizations, although no mention is made of how these organizations would raise funds. Since NSP III is scheduled to run through September 2015, it is also unclear whether village councils—if elected—would assume the functions of NSP CDCs.

During the July 2010 Kabul Conference Communiqué, the Afghan government pledged to implement the Sub-national Governance Policy within 12 months. However, as of October 2010, no date for village council elections had been set, and no funding had been identified for such elections. A July 2010 Afghan Presidential Decree tasked an inter-ministerial committee, under the chairmanship of the IDLG, to study existing councils at the district and village level and recommend a strategy for establishing sub-national governance structures. In January 2011, the committee sent a letter to the Afghan President proposing that CDCs be recognized officially as village councils, but only until formal elections take place. Consequently, although it is clear that most stakeholders envision CDCs as filling the role of village councils, they have not yet been provided authority to do so on a permanent basis.

## **NSP FACES IMPLEMENTATION CHALLENGES THAT COULD LIMIT OUTCOMES**

The NSP faces implementation challenges from unresolved issues that were evident during the first two phases of the NSP, as well as new challenges from program modifications under NSP III. Although improvements have been made, delays in the receipt of block grants by CDCs and payments to facilitating partners, continue to result in increased implementation time and costs. A new challenge for NSP III is a plan to achieve full nationwide coverage by focusing on implementing the NSP in insecure areas that have not yet been reached by the program.

### **Difficulties in Ensuring the Timely Receipt of Block Grant Funds Have Not Been Fully Resolved**

According to an NSP implementation monitoring report issued in January 2011, almost 10 percent of projects were experiencing delays due primarily to late disbursement of block grants. Facilitating partners and senior MRRD/NSP officials confirmed that, although improvements have been made,



delays in CDCs receiving community block grant funds are a continuing problem for the NSP. Such delays increase the cost and time required for implementing the NSP.

Block grant transfers to communities from the MoF are normally made through Afghanistan's central bank, Da Afghanistan Bank (DAB). Although the DAB has expanded to all of Afghanistan's provinces, in part due to demand arising from the NSP, the Afghan government has not been able to guarantee that communities will be able to access funds promptly and during a season when project implementation can occur. Delays have resulted for several reasons. Contributions to NSP prior to 2007 were sometimes insufficient to meet the needs of the program. Consequently, insufficient funds were available during that period.<sup>27</sup> Also, several facilitating partners indicated that the MRRD/NSP and the MoF developed cumbersome bureaucratic procedures for the release of block grants. Furthermore, the DAB did not always have enough cash on hand, particularly during the summer months when work could take place, in branches in remote and insecure areas.

Facilitating partners and NSP officials reported recent improvements in and steps taken to address some of the causes of delay. A shortage of donor funding is no longer an issue. As the Afghan government's "flagship" program, the NSP has been able to attract increased donor contributions. The MRRD/NSP has reportedly streamlined its requirements to decrease block grant processing to 3 days, though this is still followed by additional processing by the MRRD and the MoF before block grant funds are transferred. According to the World Bank, the MoF has also instituted a procedure whereby ministries can seek approval to carry forward their unutilized budget amounts to the next year. With this approval, ministries can continue to make payments for activities at the beginning of a new fiscal year (which is when the working season starts) from that carry forward budget until the new fiscal year's budget is approved by the Parliament.

Despite these improvements, MRRD/NSP officials stated that "more improvements are required," since processing can still take 2 months in "exceptional" circumstances. Another problem is the unavailability of Afghani bank notes in DAB provincial branches. Facilitating partners and MRRD/NSP officials stated that branches of DAB in remote and insecure areas receive fewer airlifts of bank notes. This leaves branches with insufficient cash for withdrawals, even when accounts have been credited with block grant funds.

Due to delays experienced during NSP I and II in implementing projects in some parts of Afghanistan, MRRD contracts in 2010 provide an additional \$700 and \$252 respectively, per community, to facilitating partners working in areas affected by seasonality and remoteness. The inability to ensure that communities can access funds during the months in which work can be undertaken, such as communities in areas that receive snowfall, leads to delays in project implementation. This is recognized by the MRRD/NSP as a problem requiring resolution. The MRRD/NSP stated that they were considering piloting the use of a commercial bank, instead of the central bank, for block grant transfers in remote Uruzgan province.

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<sup>27</sup> To help ensure that sufficient funds were readily available, NSP has implemented the use of a "float" account, managed by its financial management agent (Deloitte), to maintain a balance of \$80 million in pre-positioned block grant funds.

## **Delays in Payments to Facilitating Partners Have Not Been Fully Resolved**

According to NSP records, between March 2009 and January 2011, about 14 percent of payments to facilitating partners occurred after they were due. Facilitating partner contracts with the NSP require that they receive payment within 60 days of submitting an invoice, provided that the milestone against which payment has been requested has been achieved and verified. Facilitating partners stated that the problems with lengthy bureaucratic procedures were being addressed by the MRRD/NSP, but the partners expressed concern about ongoing payment issues, including the difficulty in receiving payment for their work in less secure areas where MRRD/NSP staff refuses to travel to verify the completion of contractual milestones. Delayed payments to facilitating partners led to delays in implementing NSP projects and financial distress for some facilitating partners.

An NSP report that tracks payments to facilitating partners showed that 266 individual payments, totaling \$35.3 million, were made during the period March 2009 to January 2011. Of those 266 payments, 37, worth \$5.3 million, were paid 61-151 days after submission of an invoice.

Facilitating partners provided several reasons for the slow payments and their dissatisfaction with facilitating partner payment management. Facilitating partners blamed the NSP generally for slow payment processing, although some cited specific reasons for the delays: the MoF payment processing system was slow, donors contributed to the NSP late, and, on one occasion, long-awaited funds were transferred to the wrong account. Many facilitating partners stated that they address the problem by using funding from other programs to remain engaged with NSP communities and keep the NSP running while waiting for facilitation payments. One facilitating partner stated that in 2008 it was owed a total of \$2 million by the NSP and this shortfall “nearly destroyed the organization.” An Afghan facilitating partner stated in August 2010 that the NSP owed them \$600,000, which they depended on to pay their staff.

Facilitating partner contracts further require the payment of interest for payments made 60 days later than the original due date. An international facilitating partner reported asking the NSP to pay interest, as required by the contractual obligation, on late facilitation payments. At the time of our audit, the facilitating partner reported not receiving any interest payments and still being owed \$1 million. The 2009 facilitating partner evaluation conducted by the NSP calculated that facilitating partners were using up to \$26 million of their own funds or those of other donors while waiting for the NSP to pay their facilitation fees. Consequently, delayed payments to NSP facilitating partners can negatively affect the implementation of other development programs, as well as engender poor working relations between the facilitating partners and MRRD/NSP management.

## **Expansion of NSP into Insecure Areas Increases Risk, Implementation Time, and Costs**

Although NSP I and NSP II were implemented in some high risk areas of Afghanistan, increasing insecurity and the desire to expand NSP to all rural communities resulted in the development of an insecure areas strategy, now annex G of NSP Operational Manual V. This strategy provides flexibility to

facilitating partners and NSP management in implementing NSP in insecure areas<sup>28</sup> of Afghanistan. NSP III targets 15,800 new communities, many of which are in insecure areas. The new strategy allows facilitating partners and the MRRD flexibility in implementing certain requirements in the NSP operational manual, including those pertaining to CDC elections, women's participation, engineering review, and block grant transfer.

Under the strategy, facilitating partners as well as MRRD and NSP officials are expected to have less oversight of activities. Facilitating partners have the option of subcontracting their work to a local nongovernmental organization or having community members serve as facilitators, rather than requiring facilitating partners to travel to rural villages. Since facilitating partners state that long-term engagement in communities is a key ingredient for successfully facilitating the NSP, distance facilitation may reduce the effectiveness of NSP activities.

The insecure areas strategy also permits the use of hawalla dealers in areas where it is too difficult or dangerous for CDC members to travel to DAB branches in the provincial capitals. The use of hawalla dealers for delivery of block grants is a matter of concern because block grant funds misappropriated through this mechanism are difficult to recover, as demonstrated by the problem NSP has had in recovering about \$2.8 million from a hawalla dealer in Paktika Province. According to NSP III documentation, CDCs may, depending on the security situation, choose to use hawalla dealers to transfer NSP funds on an exceptional basis. However, the hawalla dealers must be chosen from a list of pre-qualified and registered hawalla dealers. Further, hawalla contracts must include risk mitigating measures such as multiple layers of confirmation and verification of receipt of funds by the designated representatives of the communities. To further mitigate the increased program risks in insecure areas, NSP's strategy introduces some new measures such as reducing the size of block grants, limiting the types of projects, and using third-party monitors. To help offset the additional risk of working in insecure areas, the NSP has agreed to compensate facilitating partners who agree to work in such areas by paying them an additional \$800 to \$1,500 per community, depending on the level of insecurity. However, it has been difficult to recruit facilitating partners for these areas and work proceeds slower than in more secure areas. The insecure areas strategy was piloted through a facilitating partner in Kandahar province in 2009-10, but work progressed slowly. Since the facilitating partner could not monitor project progress in all districts, they set up alternate mechanisms that included a verification committee outside the CDC and secret monitors who reported back on project progress. According to the facilitating partner, these sources reported serious issues in three of the five districts where they worked, including murder, kidnapping, Taliban intimidation of CDC members, and the cessation of all work due to the lack of security.

The lack of access by oversight bodies in insecure areas also increases risk. For example, due to security considerations the ARTF external auditors visited fewer than 20 percent of Afghan provinces in each of the last 2 years. While alternative means may be used to monitor operations, there is no real substitute for on-site review. The NSP's planned expansion into insecure areas increases risk to personnel and

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<sup>28</sup> NSP's Insecure Areas Strategy defines "insecure areas" as districts where a considerable number of villages cannot be accessed consistently by NSP provincial management unit and facilitating partner personnel due to threats from, or the presence of, hostile insurgent groups or other types of armed actors.

resources, and will likely increase the time and cost of implementing NSP activities. These risk factors could contribute to a failure to achieve program objectives in those areas.

## **CONCLUSION**

The NSP is an Afghan national priority development program funded almost entirely by international donors. The United States, as the single largest provider of NSP funding, has a vested interest in the successful implementation of the program. Having confidence in the NSP becomes particularly important as the United States looks for ways to increase direct assistance to the Afghan government. The proposed increase in funding under NSP III provides an opportunity for the United States and other international donors to use the NSP as a vehicle to meet their direct assistance goals. Numerous international and Afghan oversight mechanisms and internal controls help provide reasonable assurance that donated funds will be used as intended. While some NSP funds were fraudulently withheld by a hawalla dealer, this appears to be an isolated event.

The program has made progress in providing local governance training and development funding to thousands of rural communities in the more secure districts of Afghanistan. Less certain is how well the program will work in insecure areas. Expansion into less secure areas of the country increases the level of risk associated with NSP activities and could limit or dilute the NSP's ability to achieve intended outcomes.

We identified specific areas for operational improvements, such as ensuring the timely receipt of block grants and payments to facilitating partners, and strengthening the measuring and reporting of performance indicators to measure improvements in local governance. Documenting such changes could help in determining the future role of community development councils.

## **RECOMMENDATIONS**

To help ensure that about \$2.8 million of NSP funds retained by a hawalla dealer in Paktika Province, and \$84,648 in unearned transfer fees paid to the same hawalla dealer, are used for their intended purposes, we recommend that the U.S. Ambassador to Afghanistan:

1. Urge the Afghan government to continue its efforts to recover those funds from the hawalla dealer and either reprogram the recovered funds for NSP activities or return the funds to the ARTF.

To improve internal controls associated with monitoring and accounting for donor funds and help mitigate the potential effects of future challenges to NSP identified in this report, SIGAR recommends that the U.S. Ambassador to Afghanistan encourage the NSP, the MRRD, and the World Bank to:

2. Strengthen the existing monitoring system within the program and improve the quality of the internal monitoring reports to measure progress toward established performance indicators to show improvements in local governance and linkages over time between local communities and the Afghan government as a result of NSP activities.

3. Seek final determination by the Afghan government as to whether community development councils established by NSP should become village councils.
4. Continue to improve the block grant transfer system to ensure that community development councils receive and have access to funds in a timely and consistent manner—particularly during the seasons in which they can implement approved projects.
5. Strengthen and streamline the system for paying facilitating partners in accordance with NSP contractual obligations.
6. Closely monitor and evaluate NSP activities in insecure areas to determine whether the greater flexibility in applying internal controls results in losses of NSP funds or the failure to achieve program objectives.

## COMMENTS

U.S. Embassy Kabul, the World Bank, and MRRD provided written comments on a draft of this report. See appendices V through VII. Both the World Bank and the MRRD also provided technical comments, which we have incorporated, as appropriate.

In its response to a draft of this report, the Embassy generally concurred with the report's findings and provided some additional information regarding several of the recommendations as well as some technical changes that we have incorporated. (The Embassy did not specifically comment on recommendations four and five.) Regarding our recommendation to collect the NSP funds from the hawalla dealer, it noted that a number of efforts are underway, including measures taken by the NSP before our audit. We concur and have clarified the report section addressing the hawalla dealer to better highlight the sequence of events and reworded the recommendation. The Embassy also noted that steps have already been taken to strengthen the monitoring of NSP's progress towards its governance objective, and that the government of Afghanistan has begun taking action to recognize CDCs as interim village councils. We welcome these actions and believe that, if the Afghan government takes the steps it says it is going to take, they will substantially address our recommendations. Finally, the Embassy agreed that monitoring and evaluating NSP activities in more insecure areas will present a challenge, but questioned our assertion that "internal controls will be reduced." As we note in the report, MRRD and NSP officials are providing greater "flexibility" in implementing certain internal controls because of the difficulty in operating in more insecure areas. We characterized this as "reduced" in the draft report. We reworded the recommendation to reflect this.

The World Bank generally concurred with the report's findings, but noted with regard to the payment of block grants that during SY1389 (March 2010-March 2011) there were no delays in the release of payments. However, according to the MRRD's NSP implementation monitoring report (dated January 2011) for the quarter ending June 2010, 10 percent of the projects reviewed faced delays with the main cause being late disbursement of block grants. Further, the World Bank stated that standard procedures allow up to two months to process block grant payments and that the NSP maintains an \$80 million float account to ensure that adequate funds are available. We acknowledge improvements in the timeliness of block grant payments over time and that the majority of block grants are received in a timely manner.

However, the lack of cash in some remote branches of Da Afghanistan Bank, particularly during the summer months, has not been resolved.

The MRRD stated that the report will be an important document to influence stakeholder opinions of the program and potential future funding to the NSP. Nevertheless, MRRD expressed concern that various documents and related clarifications provided to us were not taken into account. In its comments, the MRRD provides specific explanations corresponding to each of our recommendations. Several comments were similar to the Embassy's and we have addressed them. Overall, however, we believe we have accurately reflected the matters the MRRD raises. Nevertheless, the MRRD's comments are reproduced in full in appendix VII.

## APPENDIX I: SCOPE AND METHODOLOGY

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In this review of the National Solidarity Program (NSP), we assessed (1) the extent and use of U.S. and other donor assistance to the NSP, (2) the level of oversight and internal controls over donor funds, (3) whether NSP was meeting its targets, and (4) key challenges facing NSP in its third and final phase.

To determine the extent and use of U.S. and other donor assistance to the NSP, we obtained funding data and documentation from Afghanistan's Ministry of Rural Rehabilitation and Development (MRRD), U.S. Agency for International Development (USAID), the World Bank, and other international donors. In particular, we reviewed the original award and 35 subsequent modifications to the Afghanistan Reconstruction Trust Fund (ARTF) grant agreement (EEE-G-00-02-0002S-00) between USAID and the World Bank. We also reviewed U.S. congressional appropriations containing language and earmarks pertaining specifically to NSP. We conducted interviews with officials from various organizations to verify the funding data and to determine how funds were used and compared funding data to annual audit reports of NSP's financial statements. We also reviewed a prior SIGAR audit of Afghanistan's Control and Audit Office and met with officials of that office who were responsible for conducting the annual financial audits of NSP.

To assess the level of oversight and internal controls over NSP donor funds, we obtained documentation and interviewed representatives from the World Bank, MRRD, NSP, facilitating partners, and other donors. We obtained an understanding of the fiduciary oversight mechanisms provided by the ARTF administrator by reviewing minutes of the ARTF management committee, as well as reports of World Bank-funded program evaluations and supervision missions. We also reviewed ARTF quarterly and annual reports to donors, and reports issued by the ARTF donor committee. We obtained an understanding of financial and programmatic internal controls over NSP activities by reviewing the NSP operational manual. To determine the level of compliance with those internal controls, we conducted a review of NSP files for 62 randomly selected NSP projects initiated after September 1, 2009 (the implementation date for the latest version of the operational manual) and completed prior to July 29, 2010 (to ensure that the projects had ended). The sample projects were randomly selected from a universe of 664 projects meeting the pre-selection criteria. The universe data were provided in an Excel spreadsheet by the head of NSP's Management Information System Department. We verified the accuracy of the data by reviewing scanned copies of the randomly selected project files and comparing the data to those files. The sample selection was drawn using the Excel random number generator after determining that a sample size of 62 projects was sufficient to obtain a 90-percent confidence level with an error rate of plus or minus 10 percent drawn from a universe of 664 projects. For each of the 62 projects, we reviewed administrative, accounting, and procurement files, located at NSP headquarters in Kabul, Afghanistan. We tested the files for existence and completeness, including appropriate approvals, stamps, and signatures. We interviewed the facilitating partners responsible for the 62 randomly selected projects. In all, we met with 9 separate facilitating partners covering NSP communities in 195 districts and 14,404 villages in 26 of Afghanistan's 34 provinces. Due to security reasons, the audit team was unable to visit any CDCs or inspect any NSP project sites, although we obtained completion and site visit reports for 10 randomly selected projects from NSP's Monitoring and

Evaluation Department. We were also unable to review any books and records at the village level, with the exception of files for 5 of the randomly selected projects which we reviewed in NSP Provincial Management Units in Kabul and Parwan provinces.

To determine whether NSP was achieving its intended results, we reviewed the program objectives included in NSP program documentation and compared them with results included in progress reports from NSP, MRRD, and the World Bank. We verified the comparative information by interviewing officials from those and other organizations, including USAID, and other international donors, including the Danish Embassy, the United Kingdom's Department for International Development, the Asian Development Bank, the Italian Cooperation Office, and the United Nations Assistance Mission to Afghanistan (UNAMA), as well as nine separate NSP facilitating partners. These facilitating partners included the Afghanistan Rehabilitation and Education Program, Bangladesh Rural Advancement Committee, Coordination of Humanitarian Assistance, Aga Khan Foundation, International Rescue Committee, Sanayee Development Organization, Mission d'Aide au Développement des Economies Rurales Programme Afghanistan, UN-Habitat, and Danish Committee for Aid to Afghan Refugees. We also reviewed program evaluations conducted by the World Bank, Harvard University, University of York, Integrity Watch Afghanistan, and the UN Development Programme.

To highlight key challenges facing NSP in its third and final phase, we interviewed key implementers and stakeholders of NSP, including the Minister of MRRD; the Deputy Minister, Programmes, MRRD; NSP Executive Director; and department heads of NSP's Finance, Operations, Management Information System, Monitoring and Evaluation, and Engineering Departments. We also met with the USAID official designated to oversee USAID's ARTF grant agreement with the World Bank and officials from the Danish Embassy, United Kingdom's Department for International Development, the Asian Development Bank, the Italian Cooperation Office, and UNAMA, as well as nine NSP facilitating partners. These facilitating partners included Afghanistan Rehabilitation and Education Program, Bangladesh Rural Advancement Committee, Coordination of Humanitarian Assistance, Aga Khan Foundation, International Rescue Committee, Sanayee Development Organization, Mission d'Aide au Développement des Economies Rurales Programme Afghanistan, UN-Habitat, and Danish Committee for Aid to Afghan Refugees. We also reviewed program evaluations conducted by the World Bank, Harvard University, University of York, and UNDP.

We relied on performance data reported by NSP's management information system. To verify the reliability of that data, we utilized the random sampling of individual projects that were reported to have been recently completed and matched the computerized data to documentation in NSP's paper files. We found hardcopy evidence for all 62 of the randomly selected projects. Since we could not visit the project sites, we randomly selected 10 of the 62 projects for a more thorough review and found documentary evidence that all 10 projects had received monitoring site visits by NSP staff and had been completed as intended.

Where possible, we traced reported funding data to at least two sources to confirm its reliability. We verified expenditure data with annual financial audit reports issued by Afghanistan's Control and Audit



Office, after confirming that those audits were conducted in accordance with international auditing standards promulgated by the International Organization of Supreme Audit Institutions.

We conducted work in Kabul and Parwan provinces in Afghanistan and in Washington, D.C., from April 2010 to January 2011 in accordance with generally accepted government auditing standards. These standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The audit was conducted by the Office of the Special Inspector General for Afghanistan Reconstruction under the authority of Public Law No. 110-181, as amended, the Inspector General Act of 1978, and the Inspector General Reform Act of 2008.

## APPENDIX II: NSP REPORTED OUTPUTS AGAINST TARGETS, 2002 - 2007

**Table I: NSP Reported Outputs Against Targets, 2002 – 2007**

<b>Output Indicators</b>	<b>ECEPWP<sup>a</sup> outputs Dec 31, 2004</b>	<b>NSP I Targets</b>	<b>NSP I Outputs by Mar 31, 2007</b>	<b>Total Outputs by Mar 31, 2007</b>
<b>Community Block Grants</b>				
Sub-projects meeting appraisal criteria and receiving funds	5,962	15,116	16,496	22,458 <sup>b</sup>
Sub-projects completed	53	10,539	10,357	10,410
Block grant disbursement (in millions of dollars)	\$59.3	\$210.0	\$224.4	\$283.7
Block grant commitment (in millions of dollars)	\$120.0	\$304.8	\$183.7	\$313.7
Percentage of communities contributing at least 10% of project cost	100%	90%	100%	100%
Number of beneficiary families (in communities that receive block grant funds)	496,833	1,260,000	1,720,084	2,216,917
Labor days created from NSP projects	3,827,604	9,700,000	10,590,432	14,418,036
<b>Community Facilitation and Project Preparation</b>				
Villages with elected CDCs	6,181	10,254	10,321	16,502
Villages with community development plans	6,181	9,432	10,082	16,263
Sub-project proposals submitted	7,472	16,000	20,083	27,555
Percentage of women voting in CDC elections	40-80%	>40%	>40%	>40%
Communities with representation of women in CDCs (joint or separate)	>90%	>40%	95%	95%
Districts	101	178	178	279
Provinces	33	34	34	34
Number of facilitating partners	21	NA	24	24
<b>Capacity Building and Implementation Support</b>				
Project Management Consultant	1	1	1	1
Community members trained in either procurement, financial management, or operations and maintenance	27,350	393,000	408,171	472,234
Facilitating partner field staff trained	2,607	5,000	1,811 <sup>c</sup>	4,418
MRRD staff trained	714	850	263	950
<b>External Monitoring and Evaluation</b>				
Assessment of facilitating partners	1	NA	NA	1
External project evaluation	NA	1	1	1

<b>Output Indicators</b>	<b>ECEPWP<sup>a</sup> outputs Dec 31, 2004</b>	<b>NSP I Targets</b>	<b>NSP I Outputs by Mar 31, 2007</b>	<b>Total Outputs by Mar 31, 2007</b>
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Source: World Bank.

Notes:

<sup>a</sup> Emergency Community Empowerment and Public Works Project, 2002-2004 (the foundation of NSP).

<sup>b</sup> The 22,458 projects were implemented by 12,270 communities (1.8 projects per community).

<sup>c</sup> Figures on facilitating partner and MRRD staff trained do not include staff that also attended training in the previous period.

## APPENDIX III: NSP FACILITATING PARTNERS

**Table II: NSP Facilitating Partners, as of August 2010**

NSP Facilitating Partners		
Facilitating Partner	Provinces in which Facilitating Partners Conducted NSP Activities in 2010	Interviewed by SIGAR
Agency for Technical Cooperation and Development	Baghlan, Badakhshan, Faryab, Kunduz, Takhar	
ActionAid International Afghanistan	Jawezjan, Kabul	
Afghan Aid	Badakhshan, Ghor, Nuristan, Samangan	
Aga Khan Foundation	Badakhshan, Baghlan, Bamyan, Parwan, Takhar	X
Afghanistan National Re-Construction Co-ordination	Uruzgan	
Afghanistan Rehabilitation and Education Program	Paktika	X
Bangladesh Rural Advancement Committee BRAC	Nangarhar, Hilmand, Paktika, Badghis, Samangan, Takhar	X
CARE	Baghlan, Balkh, Ghazni, Paktia, Parwan, Wardak	
Coordination for Humanitarian Assistance	Balkh, Faryab, Ghor, Herat	X
Concern Worldwide	Badakhshan, Takhar	
Danish Committee for Aid to Afghan Refugees	Badghis, Faryab, Ghazni, Herat, Laghman, Paktia, Parwan	X
Future Generation	Ghazni, Nangarhar	
Flag International	Ghazni, Badakhshan	
German Agro –Action	Faryab, Jawzjan, Nangarhar	
Ghazni Rural Support Programme	Baghlan, Kunduz	
Interco Operation	Herat - Chishti Sharif district	
International Rescue Committee	Herat, Khost, Logar, Nangarhar	X
Mission d’Aide au Développement des Economies Rurales Programme Afghanistan	Ghor, Kunar, Laghman, Nuristan	X
Norwegian Project Office /Rural Rehanilitation Assosiation for Afghanisntan	Badghis, Herat, Nangarhar, Kunar	
Oxford Committee for Famine Relief	Dai Kundi	
People in Need	Baghlan, Balkh, Nangarhar, Paktia	
Partners for Social Development	Dai Kundi	
Relief International	Kunar, Nimroz	
Swedish Committee for Afghanistan	Wardak	
Sanayee Development Organization	Kabul	X
Solidarites, Aide Humanitaire d'Urgence	Samangan	

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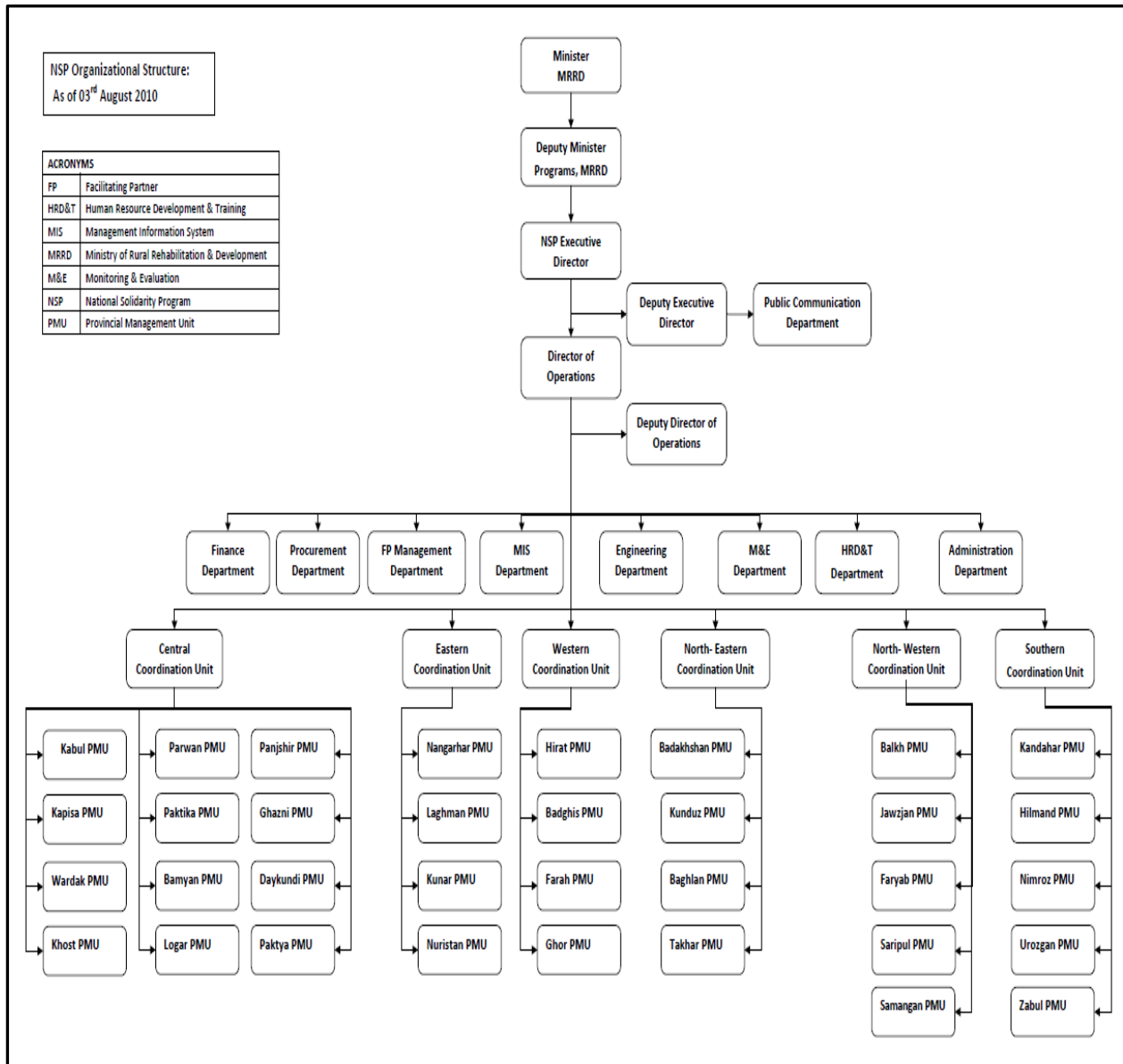
United Nations Human Settlements Program (UN-Habitat)	Balkh, Bamyan, Farah, Herat, Kandahar, Kapisa, Nangahar, Panjshir, Parwan	X
Refugee Care for Afghanistan	Jawzjan , Saripul	

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Source: NSP Facilitating Partner Management Department data.

## APPENDIX IV: NSP ORGANIZATIONAL STRUCTURE

Figure I: NSP Organizational Structure, as of August 2010



Source: NSP data.

**APPENDIX V: COMMENTS FROM U.S. EMBASSY**



*Embassy of the United States of America*  
Kabul, Afghanistan

UNCLASSIFIED  
**DECISION MEMORANDUM**

March 10, 2011

TO: Charge d'Affaires E. Anthony Wayne

FROM: CDDEA, Ambassador William Todd *WT*

SUBJECT: Follow-up Response to Draft SIGAR Audit 11-8, Afghanistan's National Solidarity Program Has Reached Thousands of Afghan Communities, but Faces Challenges that Could Limit Program Outcomes."

**CONTEXT**

Post concurs in general with Draft SIGAR audit 11-8, but offers the attached response to specific recommendations and sections of the report. It is to be noted that SIGAR made revisions to its previous draft as the result of our initial feedback, for which Post is greatly appreciative.

**RECOMMENDATION**

That you approve the response to SIGAR at Tab 1.

Approve     *WT*     Disapprove \_\_\_\_\_ Let's discuss \_\_\_\_\_

2 Attachments:

Tab 1 – Embassy Response to SIGAR Audit 11-8, National Solidarity Program

Tab 2 – Draft SIGAR Audit 11-8

**Embassy Kabul Response to the Office of the Special Inspector General for Afghanistan Reconstruction's (SIGAR) Draft audit report 11-8 entitled: "Afghanistan's National Solidarity Program Has Reached Thousands of Afghan Communities, but Faces Challenges that Could Limit Program Outcomes."**

Embassy Kabul appreciates the audit undertaken by SIGAR on the Afghanistan National Solidarity Program (NSP) and supports the overall positive assessment of the NSP that is provided in the draft SIGAR report.

The draft report contains six official recommendations. In summary, SIGAR recommends that the US Ambassador to Afghanistan urge NSP, MRRD, and the World Bank to:

1. Ensure that NSP block grant funds retained by the hawala dealer and not delivered to the intended CDCs are refunded by the Afghan government to the ARTF account and that MRRD and NSP pursue recovery of the funds from the hawala dealer;
2. Strengthen the existing monitoring system within the program and improve the quality of the internal monitoring reports to measure progress toward established performance indicators to show improvements in local governance and linkages over time between local communities and the Afghan government as a result of NSP activities;
3. Seek final determination by the Afghan government as to whether community development councils (CDCs) established by NSP should become village councils;
4. Continue to improve the block grant transfer system to ensure that CDCs receive and have access to funds in a timely and consistent manner;
5. Strengthen and streamline the system for paying facilitating partners in accordance with NSP contractual obligations; and
6. Closely monitor and evaluate NSP activities in insecure areas to determine whether the reduction in internal controls result in excessive losses of NSP funds or failure to achieve program objectives.

**Embassy comments on the SIGAR recommendations.**

Embassy Kabul offers the following comments on the draft report in response to the official recommendations and to the report in general. We base our comments on: participation in regular NSP donor program and financial reviews; quarterly NSP financial reports and weekly NSP program reports; ad hoc USAID program and financial consultations with the NSP leadership team; active participation in World Bank Supervisory Missions of the NSP program (Mirbacha Kot; Zabul; upcoming Helmand, Uruzgan, Herat, and Mazar); consultations with World Bank NSP country coordination team; review of the independent MIT/Harvard Randomized Impact Evaluation of Phase II of the NSP; and consultations with MIT/Harvard evaluation team member Fotini Cristina.



Comment on recommendation #1:

While the text of the draft SIGAR report accurately provides the facts of the case including acknowledging measures taken by NSP – before the SIGAR audit – to recover the funds and fully report the occurrence to both the Afghan authorities and to the donor community, this recommendation does not reflect the on-going actions of NSP/MRRD to recover the funds and could be misinterpreted to suggest a lack of action on the part of NSP. Actions undertaken by NSP include:

- NSP immediately took legal action – the hawala dealer is currently in the custody of the Attorney General and efforts to recover the funds are on-going;
- NSP hired legal counsel to follow-up with the Auditor-General and help retrieve the stolen funds;
- NSP withheld payments from the facilitating partner (US\$ 1million);
- NSP hired local monitors to individually, physically verify the reimbursements made to each of the affected communities; and
- NSP ceased making block transfers from the center to the provinces using hawala dealers.

Comment on recommendation #2:

In accordance with generally accepted principles of continuous improvement, Embassy agrees that monitoring progress toward NSP's governance objective needs strengthening. Embassy also notes that the NSP implementation and post-implementation monitoring reports regularly measure governance-related indicators such as inclusion, participation, transparency, accountability, and equity. Moreover, the on-going external impact evaluation of NSP II (conducted by a joint MIT/Harvard team) also shows that governance-related indicators have been measured.

Comment on recommendation #3:

As noted in the text of the draft report, an inter-ministerial committee was established to consider the future role of CDCs. In January 2011, this committee sent a letter to President Karzai proposing, among other things, that the CDCs be immediately recognized as interim village councils (VCs) until formal VC elections take place and that CDCs are the sole development gateways for their respective communities. This Afghan-led process is moving in the right direction with MRRD and NSP support. USG and the international community will continue to monitor and, as appropriate, assist in the process.

Comment on recommendation #6:

We agree with monitoring and evaluating NSP activities in insecure areas as elsewhere, but question the reference to reduced internal NSP controls. Embassy Kabul is not aware of a planned reduction in internal NSP controls. Rather, to address increased operating risks in insecure areas, NSP has introduced risk mitigation measures that are integral to the operating strategy of NSP III.

## APPENDIX VI: COMMENTS FROM THE WORLD BANK

The World Bank  
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT  
INTERNATIONAL DEVELOPMENT ASSOCIATION

19, Street 15  
Wazir Akbar Khan  
Kabul, Afghanistan

Tele: (0700) 27 6002  
WBGN: 5232 + Extension  
WBGN Fax: 5232-350

March 06, 2011

To: Special Inspector General for Afghanistan Reconstruction

### *SIGAR Audit on NSP: World Bank response*

We would like to express our gratitude and appreciation for the hard work and professionalism of the SIGAR team in carrying out the audit of NSP and especially for being willing to consider our comments as your review has progressed over time. The NSP program has been the focus of sustained Government of Afghanistan (GoA) and World Bank effort in Afghanistan over the last 8 years and continues to be a major part of the World Bank's overall program to support the country's development. We are proud to be associated with the program which, financed not only by IDA but more substantially by the multi-donor Afghanistan Reconstruction Trust Fund (ARTF), represents one of the most successful partnerships between donor nations and the Government in helping Afghanistan's rural poor.

We appreciate and concur with the report's finding that NSP has been an effective mechanism through which GoA has enabled communities to lead and implement local development projects. The achievements of the first two phases of NSP have been considerable. The program has reached national scale and presence (reaching some 26,000 communities already) not only delivering essential community infrastructure, but as importantly creating democratically elected bodies at the village level and increasing social accountability and transparency in project implementation. This remarkable achievement has been done without sacrificing a robust governance and oversight framework.

Of course, in any program of this scale, and particularly in a country wracked by violence and with some of the greatest development challenges in the world, it would be unrealistic to assume that everything will go perfectly. However, we believe that the multiple levels of oversight, starting with the communities themselves, provide a highly effective system. The case of the Paktaki hawalla dealer described in the report is a case in point. The communities' own sense of ownership of the program led to the discovery of the fraud. Cooperation between the provincial MRRD department and the facilitating partner brought the issue to the attention of NSP Management at the national level. The issue therefore came to light as part of the World Bank's regular supervision of the program and we are now tracking the resolution of the issue by the government through our ongoing supervision work.

The World Bank has enjoyed an excellent and open cooperation with the SIGAR review team. Many of our comments, corrections and suggestions to the initial draft have now been incorporated into the final draft. Indeed the final recommendations made by SIGAR in the report largely reflect the improvements in NSP that were already incorporated into the project design and implementation NSP III which was approved by the World Bank Board in June 2010 and became effective


in September 2010. The NSP III design incorporated many of the lessons emerging from NSP I and II and the program is already implementing many of the improvements that the SIGAR report now points out as recommendations. A clear case in point is the strengthened monitoring of governance indicators.

There is, however, one point where we do not concur with the findings of your report. This relates to the payments of block grants which the report states remains an unresolved issue. In fact, there are now standard operating procedures for processing payments which are closely monitored by NSP management and the Bank. Since NSP III started - and indeed during the whole of SY1389 (March 2010-March 2011) - there were no delays in the release of block grant payments to communities (where standard procedures, including proper oversight, allows for a maximum two month processing time) and the NSP float account has maintained a balance of \$80 million to ensure that funds are pre-positioned. We believe that SIGAR made its conclusion based on information that is out of date.

More broadly, we feel that the SIGAR report would benefit from presenting NSP in either a comparative or contextual perspective. There is no other program in Afghanistan which has NSP's reach and scale. In writing its report, SIGAR might have usefully compared the NSP, which is an on-budget program implemented and led by the Afghan government, with other efforts financed by the US to bring local governance in terms of impact, efficiency and accountability. Over 26,000 communities now have elected councils across the country. Councils are receiving financial management and other training and are widely recognized at the local and national level as de facto village-level governance structures. Moreover, little effort is made to explain the extraordinarily difficult environment in which NSP is implemented. The program is delivering in many areas in the country which are heavily impacted by the ongoing conflict. Furthermore, while the report highlights the risks associated with the program, it does not give GoA credit for anticipating and mitigating risk. The NSP high risk areas strategy is exactly that - a transparent effort to both highlight and agree a mitigation approach for the important but dangerous work that communities, NSP teams and facilitating partners are all engaged in.

We do hope that you will take these comments on board. In conclusion, I would like to thank you again for the hard work and professionalism of your team. We hope that the report serves to strengthen the US government's generous commitments to sponsor the further roll-out of the program, the Afghan government's commitment to deliver it, as well as our own work in supervising it.

Sincerely,



Nicholas J. Krafft  
Country Director for Afghanistan  
South Asia Region

**APPENDIX VII: COMMENTS FROM MINISTRY OF RURAL REHABILITATION AND DEVELOPMENT/NATIONAL SOLIDARITY PROGRAM**



د کليو د پياوړتيا وزارت  
وزارت ايجاد واکملاش دات

د افغانستان اسلامي جمهوريت  
جمهوری اسلامی افغانستان



Islamic Republic of Afghanistan  
Ministry of Rural Rehabilitation & Development

Ms Monica Brym  
Acting, Assistant IG for Afghanistan Operations  
Deputy Assistant IG for Audits  
SIGAR

6<sup>th</sup> March 2011

Dear Ms Brym

Subject : MRRD formal response to SIGAR's Draft Audit Report on NSP

The Ministry of Rural Rehabilitation and Development (MRRD) would like to express its appreciation to the United States Special Inspector General for Afghanistan Reconstruction (US SIGAR) for its audit of the National Solidarity Programme (NSP) undertaken from April 2010 to January 2011 (10 months) and, for sharing the draft audit report with us in February 2011. The MRRD is especially thankful to the US Government for its interest and its generous support and contributions to the NSP, and we believe that the SIGAR NSP Audit Report will be an important document to influence stakeholder opinions of the Programme and impact on potential future funding to the NSP.

I am happy to note that the report includes several positive findings on the outcomes and achievements of the NSP to-date. However, I am disappointed that the various documents and other related clarifications provided by the MRRD/NSP for the issues highlighted in the draft version of this report have not been taken into account when this was finalized. As such, the MRRD leadership and NSP would like to provide specific feedback on these issues.

Please note the following in this regard:

1. **Title and Headings:** While the contents of the report reflect the auditors' findings in a positive light, the title of the report and some of the sub-headings can be construed as negative, and do not reflect the tone and the findings in the subsequent sections.
2. **Paktika Hawalla Block Grant Theft Case:** The report implies that this was brought to the auditors attention through the World Bank. The fact is that when this case was first identified by the NSP itself (based on information received from some of the communities, FPs' and NSP PMU staff) in 2009, NSP pro-actively informed all our donors, the government and the CAO's office of this case. While the report accurately states the other facts of the case, it omits information on the various measures taken by the NSP as a response to this fraud, prior to the audit itself. The measures include:

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(IEC), to work on the modalities and the details for the future of the CDCs and the DDAs and outline the government's vision in regard to sub-national governance. This Committee has sent a letter to the President in January 2011 proposing 4 key decisions. Of these decisions, 2 deal directly with the CDCs. One proposes that the CDCs be immediately recognized as interim village councils (VCs) until formal VC elections take place, and that CDCs are recognized formally as the sole development gateways for their respective communities. While the MRRD acknowledges that considerable capacity-building is required for the CDCs to assume all the roles and responsibilities outlined for the VCs, it maintains that CDCs are the best-suited for this role and this change will best protect the investments in time, money and capacity built in the CDC institutions. The ongoing external evaluation of NSP II and various other documents that throw light on the various roles and functions handled by the CDCs, within and outside the NSP mandate, and how these can be utilized in the VCs, are available on request.

5. **Delayed Block Grant Payments to Communities:** The NSP Operational Manual allows 8 weeks from the subproject proposal submission to the disbursement of block grants. Since the decentralized data-entry system has been introduced in the NSP in September 2009, over 90% of all NSP subproject proposal related block grant disbursements happens within the stated timeframe. The few delayed cases have specific reasons for the delay such as temporary suspension of work by the FP, winter shut-down, inadequate block grant entitlement remaining until expenditure documents from earlier projects are submitted etc.
6. **Delayed Payments to the FPs:** Again, FP payments have been delayed when NSP experienced funding shortages between 2003 and 2009. Between 2003 and 2007, most NSP FP contracts were time-based contracts and payments were significantly delayed. Since 2009 when NSP funds became adequate, the only periods of real delay in FP payments is when the MoF is closed at the end of the fiscal/solar year and the start of the new fiscal/solar year and no financial transactions are possible as NSP does not have a float account to handle FP payments during this period. Since NSP II the NSP FP contracts are no longer time-based but lump-sum contracts, i.e. the payments are linked to predefined milestones that need to be met before payments are being made. Often FPs state "delays" in payment or significant sums of money owed to them by the NSP by interpreting their contracts as time-based, i.e. the money they have spent as being due. However, this is not feasible given their signed contract agreements wherein the payments may be made only after contractual milestones have been completed. Also, the FP contracts define payment delays as only after 60 days of invoice submission. With this definition, over 85% of all FP invoices from the start of 1388 have been made on time.
7. **Expansion into Insecure Areas:** From the start of NSP in mid-2003, NSP has been present in insecure areas and in all the then-existing 33 provinces. While the NSP III Sub-phase A is now expanding into the most insecure areas of the country, this is not a new decision. NSP was always conceived to be a national, priority programme which would cover all rural communities of the country, conditional only on funding availability and the acceptance of the programme by the communities. With funds now available, and the relatively safe areas of the country already covered during the first block grant under NSP Phases I and II, the NSP principle of equity also demands that the programme expands in the more insecure, as-yet-uncovered areas. Donors such as the US, UK, Netherlands and Canada are also keen for the NSP to cover these areas. NSP appreciates the

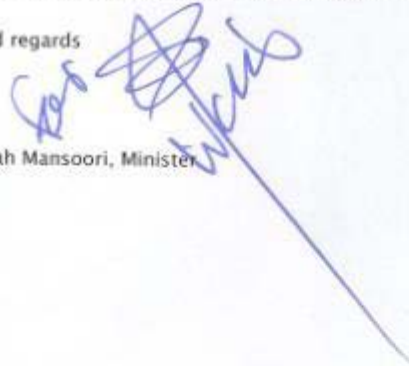
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increased risks for programme operations and funds when expanding into such areas. As such, NSP is introducing a number of risk-mitigating measures while allowing flexibility in the modus operandi for programme implementation in the high risk areas. In addition to the measures stated in the report, additional measures to be taken are stated below:

- a) A designated High Risk Area Implementation Unit (HRAIU) has been set-up in the NSP Operations Directorate to especially focus on such areas' implementation,
- b) The NSP Operational Manual's Annex on HRAI is continuously being updated and revised based on best-practices and lessons-learned from the field.
- c) A HRAI Working Group has been set up to advise the NSP senior management on the work progress, challenges and new measures needed for smooth operations in such areas.
- d) FP representatives have been added as signatories to the communities' bank accounts to ensure that NSP block grants may not be withdrawn independent of approval from the FP.
- e) Physical and financial (i.e. block grant utilization) progress for each subproject is now linked and is being monitored against block grant withdrawals from the bank accounts as well.
- f) Communities are encouraged to pay contractors and suppliers for works/supplies related to NSP approved subprojects using NSP block grants in the DaB provincial branches itself, this will avoid the physical transfer of cash between the provincial centres to the communities.

I would appreciate SIGAR's commitment to the MRRD/NSP to include this response, unabridged and unedited, in the final report. This will then allow the readers to further understand our position on these important issues and to show the MRRD/NSP's commitment to execute this national, priority programme in a transparent and accountable manner.

With kind regards



HE Jarullah Mansoori, Minister  
MRRD

(This report was conducted under the audit project code SIGAR-023A).



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- improve management and accountability over funds administered by U.S. and Afghan agencies and their contractors;
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- prevent fraud, waste, and abuse; and
- advance U.S. interests in reconstructing Afghanistan.

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