



USAID
FROM THE AMERICAN PEOPLE

OFFICE OF INSPECTOR GENERAL

**AUDIT OF USAID/AFGHANISTAN'S
RECONSTRUCTION OF THE
KANDAHAR-HERAT HIGHWAY
UNDER THE REHABILITATION
OF ECONOMIC FACILITIES AND
SERVICES (REFS) PROGRAM**

AUDIT REPORT NO. 5-306-06-005-P
May 18, 2006

Manila, Philippines



USAID
FROM THE AMERICAN PEOPLE

Office of Inspector General

May 18, 2006

MEMORANDUM

TO: USAID/Afghanistan Director, Alonzo L. Fulgham

FROM: RIG/Manila, Catherine M. Trujillo /s/

SUBJECT: Audit of USAID/Afghanistan's Reconstruction of the Kandahar-Herat Highway Under the Rehabilitation of Economic Facilities and Services (REFS) Program (Audit Report No. 5-306-06-005-P)

This memorandum transmits our final report on the subject audit. In finalizing the report, we considered your comments to the draft report and included the comments (without attachments) in Appendix II.

This report contains one recommendation to improve USAID/Afghanistan's Reconstruction of the Kandahar-Herat Highway under the REFS Program. Based on your comments, we consider that final action has been taken on the recommendation upon issuance of this report.

I want to thank you and your staff for the cooperation and courtesy extended to us during the audit.

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SUMMARY OF RESULTS

The Regional Inspector General/Manila conducted this audit to determine whether USAID/Afghanistan's Kandahar-Herat highway reconstruction activities were on schedule to achieve planned outputs. (See page 3.)

The audit found that USAID/Afghanistan's Kandahar-Herat highway reconstruction activities were on schedule to achieve planned outputs, except for 24 kilometers of road work. (See page 4.)

USAID/Afghanistan's goal was to have all 326 kilometers of the Kandahar-Herat highway paved with three layers of asphalt by December 31, 2005. As of the time of our fieldwork (September 26 to October 19, 2005), reconstruction activities were on schedule to have 302 of 326 kilometers (92.6 percent) paved with three layers of asphalt by the due date. (See pages 4-5.) Although the remaining 24 kilometers were also to have been completed by December 31, 2005, they were not finished on time because of funding shortages, which the Mission could have addressed sooner. (See page 6.)

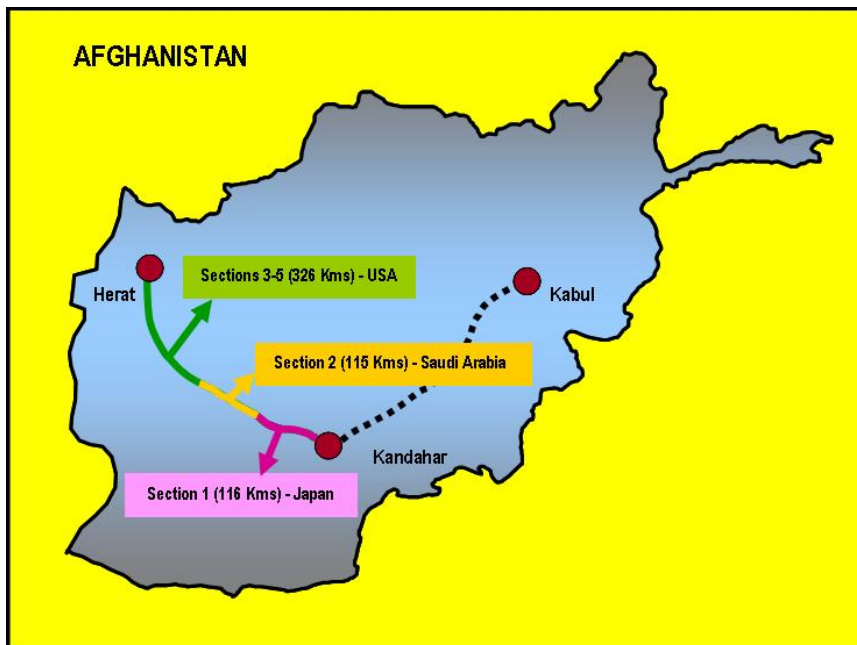
This report made one recommendation intended to improve USAID/Afghanistan's reconstruction efforts. (See page 8.) Based on USAID/Afghanistan's comments, we consider that final action has been taken on the recommendation upon the issuance of this report. (See page 9.) USAID/Afghanistan's comments are included (without attachments) as Appendix II to this report. (See page 12.)

BACKGROUND

The Rehabilitation of Economic Facilities and Services (REFS) program continues to be the largest and most visible program being implemented by USAID/Afghanistan. Its purpose is to promote economic recovery and political stability by repairing infrastructure in Afghanistan. In September 2002, USAID contracted The Louis Berger Group, Inc. (LBGI) to implement the program, including road reconstruction and other infrastructure activities. The contract's original completion date was December 31, 2005, and its estimated cost was \$155 million. At the time of this audit, the contract's completion date was December 31, 2006, and its estimated cost was \$665 million. However, during our audit fieldwork, USAID/Afghanistan submitted a request to extend the contract to July 31, 2007, and to increase its cost to \$730 million.

The signature infrastructure project under the REFS is the reconstruction of Afghanistan's major east-west highway, which runs from Kabul to Herat and is approximately 1,207 kilometers long. Under USAID/Afghanistan's oversight, LBGI substantially completed the Kabul-Kandahar portion of the highway in October 2004, except for one section that was completed in April 2005.

Like the Kabul-Kandahar portion, reconstruction of the Kandahar-Herat portion of the east-west highway is a multinational effort. The Kandahar-Herat highway—about 557 kilometers long—was divided into five sections for reconstruction purposes. The governments of Japan and Saudi Arabia are funding the reconstruction of Sections 1 and 2, respectively, which have a combined length of about 231 kilometers; the United States of America, through USAID, is funding the reconstruction of Sections 3, 4, and 5, which have a combined length of about 326 kilometers. This division of responsibilities is shown in the map below.



Map showing the five sections of the Kandahar-Herat highway and the countries funding their reconstruction.

As it did for USAID's portion of the Kabul-Kandahar highway, LBGI is reconstructing USAID's sections of the Kandahar-Herat highway. To accomplish its task, LBGI subcontracted three construction firms; each firm is responsible for reconstructing one of the three USAID sections of the highway.

At USAID/Afghanistan, the Office of Infrastructure, Engineering and Energy is responsible for overseeing the work of LBGI and its subcontractors. As of October 1, 2005, the reconstruction of the Kandahar-Herat highway was estimated to cost \$162 million.

AUDIT OBJECTIVE

The Regional Inspector General/Manila conducted this audit as part of its fiscal year 2005 annual audit plan to answer the following question:

- Were USAID/Afghanistan's Kandahar-Herat highway reconstruction activities on schedule to achieve planned outputs?

Appendix I contains a discussion of the audit's scope and methodology.

AUDIT FINDING

Except for 24 kilometers of road work, USAID/Afghanistan's Kandahar-Herat highway reconstruction activities were on schedule to achieve planned outputs.

USAID/Afghanistan manages a sizable program to advance Afghanistan's recovery to a stage where transformational development progress is possible. In doing so, it faces a number of challenges: deteriorating security, difficult living and working conditions, and frequent staff turnover. Despite these challenges, the Mission continues to make progress.

Reconstruction of USAID's sections of the Kandahar-Herat highway included a number of planned outputs such as:

- Demining the highway right-of-way.
- Removing the old road surface.
- Surveying and designing the highway.
- Mobilizing camp sites and asphalt-making plants.
- Constructing the new highway, including culverts, causeways, and bridges.

Most of the outputs had to be and were completed before construction of the new highway could begin. Of the remaining planned outputs, we considered the construction of the new road surface, which consisted principally of applying three layers of asphalt so that the highway could be open to traffic, to be the key output for answering the audit objective. It was the output most used by the Mission and its implementing partners to track progress.

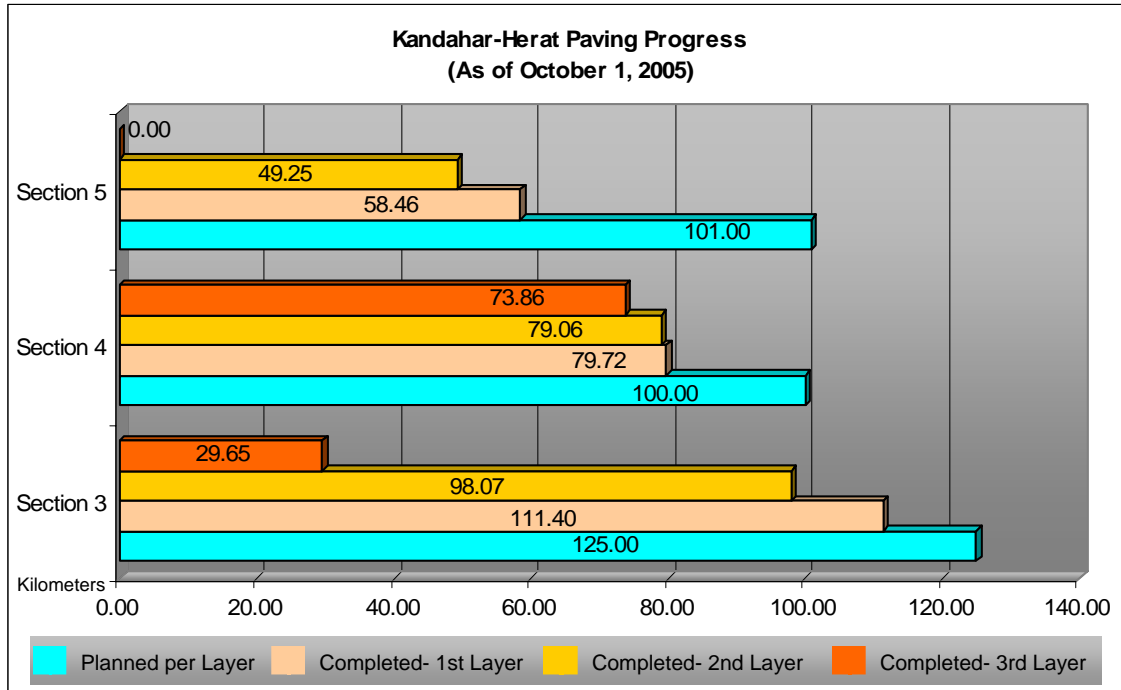


OIG photograph of a segment of Section 4 of the Kandahar-Herat highway in Herat, Afghanistan that had been paved with three layers of asphalt. (October 2005)

USAID/Afghanistan's goal was to have all 326 kilometers of the USAID-financed portion of the Kandahar-Herat highway paved with three layers of asphalt by December 31, 2005. As of the time of our fieldwork (September 26 to

October 19, 2005), reconstruction activities were on schedule to have 302 of the 326 kilometers (92.6 percent) paved with three layers of asphalt by December 31, 2005.

For each section of the Kandahar-Herat highway being reconstructed by USAID, the following chart compares the planned number of kilometers to be paved with three layers of asphalt to reported progress by layer of asphalt, as of October 1, 2005.



Our conclusion that the paving of the Kandahar-Herat highway was on schedule was made considering the physical progress noted during our 3-day site visit compared to completion dates in project agreements, the contractor’s implementation plan, and construction schedules. Assessing progress also included comparing reported progress in the chart above to what was noted in our site visit and to other supporting evidence, comparing contractor paving rates to the Mission’s estimated progress rates taking into account the time remaining to complete paving, and discussions with engineers and other personnel from USAID/Afghanistan and The Louis Berger Group, Inc. (LBGI).

Although 302 kilometers of the Kandahar-Herat highway were on schedule to be completed by December 31, 2005, USAID/Afghanistan did not promptly request additional funds to address funding shortages in the Rehabilitation of Economic Facilities and Services (REFS) program. The delay in requesting additional funds contributed to the suspension of work on the remaining 24 kilometers of highway, and the planned date to complete the work is now October 2006. This issue is discussed in more detail in the following section of this report.

Some Highway Reconstruction Activities Suspended

Summary: USAID guidance states that an operating unit and its strategic objective teams should prudently plan, monitor, and manage the financial aspects of a program throughout the life of the strategic objective. However, USAID/Afghanistan did not promptly request additional funds to address the funding shortages affecting completion of the Kandahar-Herat highway. The Mission's delay in requesting additional funds contributed to work on the last 24 kilometers of the Kandahar-Herat highway being suspended. Because constant staff turnover was a factor in this delay, the Mission needs to formally document, track, and promptly resolve significant issues uncovered in its own monitoring efforts that could affect the progress of its reconstruction activities.

USAID's Automated Directives System Chapter 202.3.7 states that an operating unit and its strategic objective teams are responsible for managing the resources made available to them so that planned outputs and results are achieved in a cost-effective and timely manner, in accordance with applicable regulatory requirements. These responsibilities include prudently planning, monitoring, and managing the financial aspects of a program throughout the life of the strategic objective because the financial position of a strategic objective and its activities is critically important to achieving desired results. Another responsibility is formulating resource requests. If pipelines are not adequate to finance projected expenditures, there is a risk that new funds will not be available on time to avoid a curtailing or even a shutdown of activity implementation. It is, therefore, critical that an operating unit and its strategic objective teams make careful projections and monitor them closely so adequate resources are available when needed.

USAID/Afghanistan did not promptly request additional funds to address funding shortages in the REFS program, thus affecting the completion of the Kandahar-Herat highway. According to e-mail correspondence, a Mission official responsible for the Kandahar-Herat highway reconstruction informed Mission management as early as December 2004 that the REFS contract's \$665 million ceiling would not allow for the completion of all the work that was ongoing or scheduled to be done. In May 2005, in response to the Mission official's e-mail reminder about the funding shortages, Mission management began considering such options as cutting back on work to address the funding problem. But, it was not until October 10, 2005, that USAID/Afghanistan issued an action memorandum requesting the Deputy Assistant Administrator for the Bureau for Asia and the Near East to approve increasing the ceiling of the REFS contract by \$65 million (from \$665 million to \$730 million) to address the need for more funding and to extend the contract completion date from December 31, 2006, to July 31, 2007.

The Mission's action memorandum explained that the request was not a proposal to increase the ceiling in order to award new work; rather, the additional \$65 million (a 9.8 percent increase over the contract ceiling of \$665 million) was needed to cover cost growth in the projects already subcontracted by LBGI. About 43 percent of the increase was attributable to cost growth in the Kandahar-Herat highway. According to the memorandum, a detailed assessment of the old road and bridges could not be done when LBGI's contract was awarded because demining had not yet occurred. Consequently, costs increased when changes or variations in conditions were found as road reconstruction progressed—conditions that were exacerbated by the extreme

winter of 2004-2005. The memorandum also disclosed that nearly \$8.7 million of the proposed ceiling increase was directly attributable to increased security costs necessitated by the deteriorating security situation in the country. Over 60 percent of this increase was specific to the Kandahar-Herat highway. Increasing fuel costs and the declining value of the dollar were also cited.

On October 4, 2005, work was suspended on the last 24 kilometers of Section 5 of the highway leading into Herat, including 4 bridges. Section 5's completion date was also extended from December 31, 2005, to October 17, 2006.¹ Although these actions were taken because of the funding shortages, in our opinion, the Mission's taking ten months to request additional funding also contributed to the need to suspend work on the Kandahar-Herat highway reconstruction activities.



U.S. Army Corps of Engineers' photograph of the segment of Section 5 of the Kandahar-Herat highway in Herat, Afghanistan on which work was suspended. (April 2005)

With respect to the impact on commerce, it should be pointed out that the suspension did not halt traffic into Herat. Traffic continued to flow along the last 24 kilometers of Section 5, but at a slow pace due to the deteriorated condition of the old highway. We do not know if other REFS program activities were suspended because of funding shortages as our audit covered only the Kandahar-Herat highway reconstruction activities.

USAID/Afghanistan's program manager for road reconstruction cited staff turnover as the reason for the Mission's delayed response to the funding shortages. He explained that the Mission suffered from constant turnover at all levels. For example, in the summer of 2005, the following personnel joined the U.S. mission in Afghanistan: a new ambassador; deputy chief of mission; USAID mission director; program officer; director for the Office of Infrastructure, Engineering and Energy (OIEE); and other OIEE staff. These officials and staff were involved in the decision-making process regarding raising the ceiling of the REFS contract, and had to be briefed on the contract's history, the options considered, and the necessity for the additional amount requested. He added that another contributing factor to the Mission's delayed response was the time it took USAID/Washington to approve the contract's previous ceiling increase, which was initiated in May 2004 and signed in April 2005.

¹ Paving of the last 24 kilometers of Section 5 and rehabilitation of three bridges are scheduled to be completed by May 2006; work on the fourth bridge is scheduled to be completed in October 2006.

USAID/Afghanistan operates in a challenging environment. It manages a large, ever-increasing portfolio with limited staffing. Terrorist attacks are a daily threat to all its activities throughout the country. Living conditions are harsh and staff turnover is frequent because tours of duty are limited to one year.²

The above factors, particularly the constant staff turnover, make it important that USAID/Afghanistan have formal procedures to document and track significant issues it uncovers that could affect the progress of its reconstruction efforts. Such procedures would ensure that the issues are resolved promptly. The REFS program is USAID's largest in Afghanistan, and it carries out many activities important to the rebuilding of the country. Given its size, visibility and importance, USAID/Afghanistan should have requested additional funding early enough to avoid having to suspend work on the last 24 kilometers of the Kandahar-Herat highway. Consequently, we are making the following recommendation:

Recommendation No. 1: We recommend that USAID/Afghanistan develop and implement procedures with milestones to document, track and promptly resolve significant issues uncovered in its own monitoring efforts that could affect the progress of its reconstruction activities.

² As in the previous year, these are issues that the Mission reported as material weaknesses in its Federal Managers' Financial Integrity Act report for fiscal year 2005.

EVALUATION OF MANAGEMENT COMMENTS

USAID/Afghanistan concurred with the contents of this report and the recommendation. In its comments, the Mission provided evidence that it had developed and is implementing procedures to document, track and promptly resolve significant issues uncovered in its own monitoring efforts that could affect the progress of its reconstruction activities. Based on our review of the evidence provided by the Mission, we considered that final action has been taken on the recommendation upon the issuance of this report.

The Mission's written comments are included (without attachments) as Appendix II to this report.

SCOPE AND METHODOLOGY

Scope

The Regional Inspector General/Manila conducted this audit in accordance with generally accepted government auditing standards. The audit was designed to determine whether USAID/Afghanistan's Kandahar-Herat highway reconstruction activities were on schedule to achieve planned outputs.

The audit was performed at USAID/Afghanistan and at the offices of The Louis Berger Group, Inc.—the primary contractor reconstructing the Kandahar-Herat highway—and it covered reconstruction activities from June 6, 2004, through October 1, 2005. Fieldwork was conducted from September 26 to October 19, 2005, and included site visits to various points between Kandahar and Herat to observe reconstruction activities. As of September 30, 2005, USAID records showed payments of \$69.2 million for work on the Kandahar-Herat highway.

As part of the audit, we assessed the significant internal controls used by USAID/Afghanistan to monitor reconstruction of the Kandahar-Herat highway. The assessment included controls related to whether the Mission (1) conducted and documented site visits to evaluate progress and monitor quality, (2) required and approved an implementation plan, (3) reviewed and approved the primary contractor's proposed changes to its scope of work, (4) reviewed progress reports submitted by the primary contractor, and (5) compared the primary contractor's reported progress to planned progress and the Mission's own evaluations of progress. We also reviewed the Mission's Federal Managers' Financial Integrity Act report for fiscal year 2005 for any issues affecting the reconstruction of the Kandahar-Herat highway. Finally, we obtained and reviewed any relevant prior audit reports.

Methodology

To answer the audit objective, we interviewed officials and staff from USAID/Afghanistan, the primary contractor, and the U.S. Army Corps of Engineers. In addition, we reviewed:

- Documentation such as, but not limited to, the primary contractor's implementation plan, progress reports, site visit and other monitoring reports, and financial reports.
- Contracts and subcontracts and their modifications.
- Job orders and their modifications.
- Laws, regulations, and USAID policy and guidance related to the audit objective.

We did not set a materiality threshold for this audit as the nature of the audit did not lend itself to the establishment of such a threshold. However, we designed our audit to

address potential concerns such as inadequate oversight over reconstruction activities and lack of awareness of existing problems along the Kandahar-Herat highway.

MANAGEMENT COMMENTS



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FROM THE AMERICAN PEOPLE

May 16, 2006

MEMORANDUM

To: Catherine M. Trujillo, RIG/Manila

From: Alonzo Fulgham/s/, Mission Director

Subject: USAID/Afghanistan – Response to Draft Audit Report – Reconstruction of the Kandahar–Herat Highway under the Rehabilitation of Economic Facilities and Services (REFS) Program, Audit Report dated April 6, 2006. (Report No. 5-306-06-XXX-P)

We appreciate the opportunity to respond to the subject draft report. The Mission concurs with the draft report and has accordingly taken corrective action to address the recommendation below:

Recommendation No. 1: We recommend that USAID/Afghanistan develop and implement procedures with milestones to document, track and promptly resolve significant issues uncovered in its own monitoring efforts that could affect the progress of its reconstruction activities.

USAID/Afghanistan Response: USAID's Automated Directives System (ADS) Chapter 202.3.7 states that an operating unit and its strategic objective teams are responsible for managing the resources made available to them so that planned outputs and results are achieved in a cost-effective and timely manner, in accordance with applicable regulatory requirements. To better meet this ADS section and address the audit recommendation above USAID/Afghanistan developed procedures and issued a Mission Notice that implements those procedures with milestones to document, track and promptly resolve significant issues uncovered in our monitoring efforts that could affect the

progress of our reconstruction activities. The Mission Notice complements the ADS by defining the frequency of reporting of any significant issues uncovered in our monitoring.

RECOMMENDATION:

Based on the above, USAID/Afghanistan requests closure of the recommendation upon issuance of the report since corrective action has being taken.

Thank you.

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