UNITED NATIONS DEVELOPMENT PROGRAMME
Office of Audit and Investigations

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AUDIT

OF

UNDP COUNTRY OFFICE

IN

MALAYSIA

Report No. 1462

Issue Date: 17 September 2015

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Report on the Audit of UNDP Malaysia
Executive Summary

The UNDP Office of Audit and Investigations (OAI) conducted an audit of UNDP Malaysia (the Office) from 1 to 16 June 2015. The audit aimed to assess the adequacy and effectiveness of the governance, risk management and control processes relating to the following areas and sub-areas:

(a) governance and strategic management (organizational structure and delegations of authority, leadership/ethics and values, risk management, planning, monitoring and reporting, financial sustainability);

(b) United Nations system coordination (development activities and Resident Coordinator Office);

(c) programme activities (programme management, partnerships and resource mobilization, project management); and

(d) operations (human resources, finance, procurement, and general administration).

The audit covered the activities of the Office from 1 January 2014 to 31 March 2015. The Office recorded programme and management expenditures totalling $7.5 million. The last audit of the Office was conducted by OAI in 2007.

The audit was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*

Overall audit rating

OAI assessed the Office as **satisfactory,** which means, "Internal controls, governance and risk management processes were adequately established and functioning well. No issues were identified that would significantly affect the achievement of the objectives of the audited entity."

Key recommendations: Total = **4**, high priority = **1**

The four recommendations aim to ensure the following: (a) achievement of the organization's strategic objectives (Recommendations 2 and 3); (c) effectiveness and efficiency of operations (Recommendations 1 and 4).

For high (critical) priority recommendations, prompt action is required to ensure that UNDP is not exposed to high risks. Failure to take action could result in major negative consequences for UNDP. The high (critical) priority recommendation is presented below:

Accountability over NIM reimbursement of funds not adequate (Issue 2)	Under project management arrangements for Atlas Project No. 82252, the accountability over the reimbursement of funds to the responsible parties and the corresponding accounting treatment were not adequately defined. Reimbursements were recorded in grant accounts instead of expense accounts. In addition, the supporting documentation to justify the reimbursements was not sufficient.

Recommendation: In future project documents, the Office should clearly define the accounting procedures to be used for advances and reimbursements of funds to responsible parties. In the case of reimbursements, the Office should include verification procedures to ensure correct use of the funds, and propriety of the expenses reported.

In addition, reimbursement claims should only be based on verified supporting documents and recorded in the appropriate expenditure accounts. This will enable the proper accounting, tracking, and auditing of expenditures.

Management comments and action plan

The Resident Representative accepted all of the recommendations and is in the process of implementing them. Comments and/or additional information provided has been incorporated in the report where appropriate.

Issues with less significance (not included in this report) have been discussed directly with management and actions have been initiated to address them.

Helge S. Osttveiten
Director
Office of Audit and Investigations

I. About the Office

The Office is located in Kuala Lumpur, Malaysia (the Country). At the time of the audit, the Office had 22 staff members with a programme portfolio of 30 projects. The Country was ranked among the upper-middle income countries and was politically stable.

II. Audit results

Satisfactory performance was noted in the following areas:

(a) Development activities. Programme management arrangements and preparations for a new cycle were on track.

(b) Resident Coordinator Office. Systems in the Resident Coordinator Office for planning, budgeting and reporting of activities by the United Nations Country Team were found to be adequate.

(c) Human resources management. Recruitment of staff and service contractors was generally in line with organizational procedures. Leave procedures were managed through Atlas (enterprise resource planning system of UNDP).

(d) Procurement. The process for the selection of goods and services was competitive and ensured that value for money was obtained.

(e) General administration. The administration of common services was adequately managed. Assets were recorded, safeguarded and reported in line with policies and procedures.

Low priority issues/recommendations were discussed directly and agreed with the Office and are not included in this report.

OAI made one recommendation ranked high (critical) and three recommendations ranked medium (important) priority.

High priority recommendation:

(a) In future project documents, the Office should clearly define the accounting procedures to be used for advances and reimbursements of funds to responsible parties (Recommendation 2).

Medium priority recommendations, arranged according to significance:

(a) Under the guidance of the OFRM, the Office and the GSSC should develop and agree on a framework for the provision of administrative support and services to the GSSC (Recommendation 1).
(b) The Office should optimize the utilization of available programme resources by closely reviewing the selection and design of projects (Recommendation 3).
(c) For the upcoming cycle, the Office should document a medium to long-term resource mobilization strategy (Recommendation 4).

A. Governance and strategic planning

1. Financial sustainability

Issue 1 Corporate Issue: Arrangements for support to GSSC not fully defined

The Office of Financial Resources Management (OFRM), as the headquarters department in charge of overseeing the Global Shared Service Centre (GSSC), is responsible for agreeing with the Office in developing a framework for the provision of administrative and support services to the Centre.

The Office had been providing operations support to the GSSC since 2011. In turn, the GSSC had been funding two of the Office's general administrative support posts from 2012 up until the time of the audit. The number of GSSC personnel had increased from 33 to 55 between 2012 and 2015, with a possibility of further significant increases by 2017, according to the Office. In addition, in 2014, the Office received reimbursement of $60,000 from OFRM mainly for compensation for human resources administration support (recruitment) and other support to the GSSC, however, it was not clear how this amount was determined and calculated. Provisions for human resources/administration support (recruitment) and other support to the GSSC had not been made for 2015 at the time of the audit.

According to the OFRM, short-term arrangements to cover the Office's support to the GSSC during its expansion were made up to 2015 with the further understanding that beyond 2015, the Office, together with the GSSC would review those arrangements and possibly move to a Universal Price List – based on a cost recovery scheme. However, those new arrangements and the corresponding cost recovery scheme were yet to be agreed upon and formalized at the time of the audit. In addition, the existing arrangements were not legally framed or properly documented.

If arrangements for administrative and support services are not adequately defined, budgeted for, or agreed upon, there is a risk that the Office may not be able to provide the optimal services required. In addition, there is a risk that the Office may not be adequately compensated for services rendered.

Priority	Medium (Important)
Recommendation 1: Under the guidance of the OFRM, the Office and the GSSC should develop and agree on a framework for the provision of administrative support and services to the GSSC. This framework should include details on resource planning and cost recovery mechanisms. **Responsible units:** OFRM	
Management action plan: The OFRM agrees that the existing framework for Office support between the Office and the GSSC should be reviewed by all parties involved, and updated as necessary. The Office will accelerate the dialogue with the OFRM to implement full cost recovery for services provided during 2015 by negotiating a cost recovery framework to cover the next programme cycle. **Estimated completion date:** November 2015	

B. Programme activities

1. Project management

Issue 2 Accountability over NIM reimbursement of funds not adequate

UNDP NIM (national implementation modality) guidelines provide that funds advanced and reimbursed to the implementing partner require close monitoring from the Country Offices in order to verify the correct use of the funds, and ascertain the accuracy and propriety of the expenses reported.

Under project management arrangements for Project No. 82252, the accountability over the reimbursements of funds to the responsible parties and the corresponding accounting treatment were not adequately defined. The arrangement was for the Office to provide financial resources to the implementing partner for implementing project activities.

In addition, the implementing partner signed agreements with responsible parties, who at the same time were beneficiaries of implemented activities, through the reimbursement modality. According to the agreements, the Office was committed to making payments to responsible parties based on claims channeled through the implementing partner. When payments to the responsible parties were made by the Office, these were based on Direct Requests for Payments for the completion of agreed upon milestones. However, these were endorsed by the implementing partner without the requirement to substantiate the claims with receipts and other supporting documents. Furthermore, payments were recorded by the Office through the grants account rather than the expense account in Atlas. Total project expenditure from 2013 to 2015 was approximately $6.2 million. The project was audited by an audit firm in 2013 and it received an unqualified opinion. However, the audit scope did not include a review of supporting receipts and invoices.

Without proper supporting documentation and underlying receipts/invoices, there is a risk that the Office will not be able to ensure that cash transferred to responsible parties is used for the intended purposes.

Priority High (Critical)

Recommendation 2:

In future project documents, the Office should clearly define the accounting procedures to be used for advances and reimbursements of funds to responsible parties. In the case of reimbursements, the Office should include verification procedures for supporting documentation to ensure correct use of funds, and propriety of the expenses reported.

In addition, reimbursement claims should only be recorded in the appropriate expenditure accounts. This will enable the proper accounting, tracking, and auditing of expenditures.

Management action plan:

In the future, the Office will:

(a) pay reimbursement claims based on receipts and supporting documents and will use Atlas expense account codes (instead of grant codes) as suggested;
(b) provide additional training for programme and operations staff related to relevant policies and

procedures and ensure that all staff have completed mandatory courses on project and programme management related to their profiles; and

(c) ensure refresher training for implementing partners on documentation requirements as we agree on new projects for the new programme cycle and train new implementing partners accordingly.

Estimated completion date: January 2016

2. Programme management

Issue 3 Sub-optimal use of programme resources

The UNDP Strategic Business Plan 2014-2017 requires offices to optimize the allocation of programme resources to achieve development results. Country Offices are responsible for the efficient and effective use of programme resources.

The Office recorded satisfactory programme delivery rates over budgeted resources, with 98 percent (or $7 million) in 2013 and 92 percent (or $6 million) in 2014. However, as shown in Table 1 below, it had a trend of low budget and low delivery over available resources. For the current programme cycle, delivery rates over available resources were 66 percent (or $7.1 million) in 2013 and 56 percent (or $6 million) in 2014. Delivery rates in the last two years of the previous cycle were 58 percent (or $3.3 million) in 2011 and 48 percent (or $4.4 million) in 2012. From 2011 to 2014, an average of 34 percent of available resources remained unbudgeted every year. Similarly, in 2015, the Office had not budgeted 30 percent of available resources.

Table 1: Delivery trend from 2011 to June 2015

Year	Total available resources $ '000	Total Budgeted Resources $ '000	Under budget $ '000	Under budget %	Delivery $ '000	Delivery on available resources	Delivery over budget	Resource balance $ '000
2011	5,672	4,570	1,102	19%	3,298	58%	72%	2,374
2012	9,140	5,082	4,058	44%	4,410	48%	87%	4,730
2013	10,800	7,279	3,521	32%	7,098	66%	98%	3,722
2014	10,808	6,545	4,263	39%	6,040	56%	92%	4,768

Source: Atlas system

The Office attributed the low delivery rate to the fact that the Government Agency leads and oversees the processes of project selection and budgeting funded from government cost sharing resources. Fund allocations for such projects are done on a project-by-project basis to ensure clear and substantive contributions to national development priorities and to avoid overlapping budget allocations among government ministries. The Office further indicated that the absence of projects implemented by NGOs was another factor affecting delivery rates.

Low programme resource allocations and delivery rates may adversely affect the achievement of overall objectives and outcomes of the Country Programme.

Priority	Medium (Important)

Recommendation 3:

The Office should optimize the utilization of available programme and ensure optimum budget limits are set against available resources.

Management action plan:

The Office will undertake steps to address the optimal utilization of the allocated resources, such as:

(a) including non-state development actors in the draft Country Programme Document 2016-2020 as implementing partners;
(b) providing briefings to the Government Agency on the utilization of the government cost sharing funds;
(c) initiating a joint UNDP-Government Agency briefing to ministries and potential implementing partners on the draft Country Programme Document on thematic priorities and available resources for the entire cycle; and
(d) providing further technical support to potential implementing partners in developing project documents to fully utilize the available resources.

Estimated completion date: December 2015

3. Partnerships and resource mobilization

Issue 4 Lack of resource mobilization strategy

Country Office strategic planning processes require the establishment of management strategies, including resource mobilization and partnership strategies.

The Office planned to mobilize $24.7 million for the current cycle (2013-2015). Out of that, $23 million was to be earned from non-core resources. Resources mobilized as of June 2015 were $21.4 million (or 87 percent of resource target), of which $19.1 million (or 89 percent of resources mobilized) were non-core resources. About 92 percent of these funds (or $17.5 million) were mainly resourced from the Global Environment Facility only, and the rest from government cost sharing ($900,000 or 5 percent) and regional programme initiatives ($980,000 or 5 percent).

The Office lacked a documented and a robust medium to long-term resource mobilization strategy. Its resource mobilization plans were based on the annual targets, as opposed to longer term planning that could have explored opportunities for establishing wider and additional partnerships that could create new, broader and more sustainable funding streams for the programme cycle and beyond.

The Office's explanation for not having a strategy was that Country Offices in the Regional Bureau for Asia and the Pacific region would set and review their resource mobilization targets with the Bureau annually, which guided their resource mobilization efforts.

Having only one significant source of funding for the cycle puts the financial sustainability of the Office at risk, particularly in cases where resources are significantly reduced or partnerships are terminated. In addition, there is a risk that the Office might miss out on opportunities for identifying more and longer-term partnerships and new revenue streams.

Priority	Medium (Important)
Recommendation 4: For the upcoming cycle, the Office should document a medium to long-term resource mobilization strategy with the view to leverage the Country's funding environment, establish new partnerships and create additional and predictable funding streams.	
Management action plan: The Office will develop a medium and long-term resource mobilization strategy for the Country Programme Document 2016-2020. **Estimated completion date:** December 2015	

Definitions of audit terms - ratings and priorities

A. AUDIT RATINGS

- **Satisfactory** Internal controls, governance and risk management processes were adequately established and functioning well. No issues were identified that would significantly affect the achievement of the objectives of the audited entity.

- **Partially Satisfactory** Internal controls, governance and risk management processes were generally established and functioning, but needed improvement. One or several issues were identified that may negatively affect the achievement of the objectives of the audited entity.

- **Unsatisfactory** Internal controls, governance and risk management processes were either not established or not functioning well. The issues were such that the achievement of the overall objectives of the audited entity could be seriously compromised.

B. PRIORITIES OF AUDIT RECOMMENDATIONS

- **High (Critical)** Prompt action is required to ensure that UNDP is not exposed to high risks. Failure to take action could result in major negative consequences for UNDP.

- **Medium (Important)** Action is required to ensure that UNDP is not exposed to risks that are considered moderate. Failure to take action could contribute to negative consequences for UNDP.

- **Low** Action is desirable and should result in enhanced control or better value for money. Low priority recommendations, if any, are dealt with by the audit team directly with the Office management, either during the exit meeting or through a separate memo subsequent to the fieldwork. Therefore, low priority recommendations are <u>not included in this report</u>.