UNITED NATIONS DEVELOPMENT PROGRAMME
Office of Audit and Investigations

AUDIT

OF

UNDP COUNTRY OFFICE

IN

UZBEKISTAN

Report No. 1453

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(REDACTED)

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Report on the Audit of UNDP Uzbekistan
Executive Summary

The UNDP Office of Audit and Investigations (OAI) conducted an audit of UNDP Uzbekistan (the Office) from 25 May to 5 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, Resident Coordinator Office, role of UNDP – "One UN", Harmonized Approach to Cash Transfers);

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

(d) operations (human resources, finance, procurement, information and communication technology, general administration, and safety and security).

The audit covered the activities of the Office from 1 January 2014 to 28 February 2015. The Office recorded programme and management expenditures totalling $21 million. The last audit of the Office was conducted by OAI in 2010.

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 **unsatisfactory**, which means, "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." This rating was mainly due to the improper use of the service contract modality, weaknesses with vendor approval, ███████████████████████ ██████████████ and weaknesses in submissions to procurement review committees.

Even though good practices and satisfactory performance were identified, the issues identified with vendor approval, █████████████████████████████ and procurement are critical, and could put the achievement of overall objectives at risk.

Good practice

Programme management

The Office developed and implemented several tools to facilitate monitoring of programme and project activities, such as the (a) Internal Project Monitoring Calendar introduced on the Office's intranet; (b) internal projects dashboard on key indicators on project performance, (c) peer-to-peer review group on quality of programming; (d) guidance note on integrated results-based programme and (e) checklists for budget revision.

Key recommendations: Total = **5**, high priority = **4**

The five recommendations aim to ensure the following: (a) achievement of the organization's strategic objectives (Recommendations 1); (b) reliability and integrity of financial and operational information (Recommendation 3, 4, and 5); and (c) compliance with legislative mandates, regulations and rules, policies and procedures (Recommendation 2).

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. All high (critical) priority recommendations are presented below:

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Improper use of service contract modality (Issue 2)	The Office engaged 18 individuals under the service contract modality and all of them were performing core functions in various units of the Office, covering both programme and operations functions. Recommendation 2: The Office should avoid using the service contract modality as a cost-saving measure when filling vacant positions that require performing core functions.
Weaknesses in vendor approval (Issue 3)	The review of the vendors' database disclosed that 12 vendors had the same address with other vendors in the system. The Office issued purchase orders totalling $0.8 million for these vendors during the period 2010-2014. Furthermore, the performance evaluation of one vendor was unsatisfactory; however, it continued to receive orders during the audit period. Recommendation 3: The Office should strengthen controls in approving vendors in Atlas by conducting comprehensive research to identify established companies that will be contacted to bid on relevant procurements; requiring bidders to provide information to ensure that the vendor is authentic, including a declaration of owners' interest in other companies and the experience of vendors and capacity to provide goods and services; and conducting regular reviews of existing vendors and deactivating all vendors with duplicate profiles.
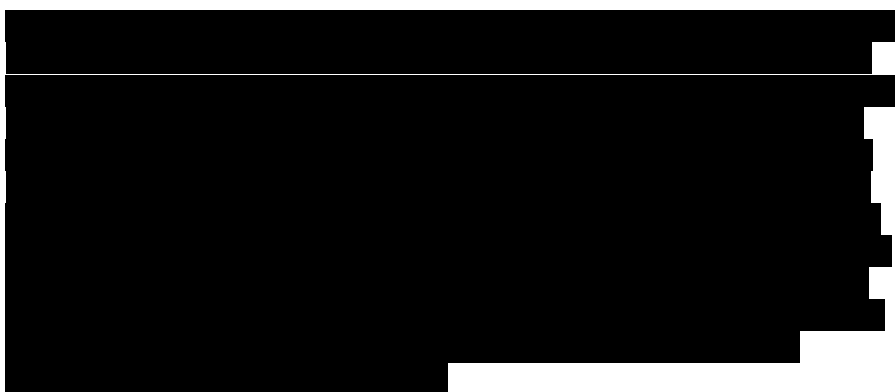
Procurement cases not submitted to procurement review committees (Issue 5)	The Office had eight vendors with cumulative contract values totalling $0.5 million in 2013 and 2014. Each vendor had exceeded the threshold of $50,000, but their contracts were not submitted to the Contracts, Assets and Procurement Committee for review. During the audit, OAI identified three additional vendors that exceeded the thresholds and were not submitted to the Contracts, Assets and Procurement Committee for review.

Recommendation 5: The Office should strengthen controls in procurement management and monitoring by submitting all procurement cases (including the 11 vendor contracts) that meet the procurement threshold to the procurement review committee for review.

Management comments and action plan

The Resident Representative accepted all five recommendations and is in the process of implementing them. Comments and/or additional information provided have 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, located in Tashkent, Uzbekistan (the Country) was established in 1993. At the time of the audit, the Office was implementing the 'United Nations Development Assistance Framework', covering the period from 2010 through 2015 in the areas of economic well-being, social services, environment, and governance. Most of the projects were nationally implemented with direct support services by the Office. The new 'United Nations Development Assistance Framework' document, covering the period from 2016 through 2020, was signed by the Government in June 2015.

The Office had 29 staff members, 215 service contract holders and 5 United Nations Volunteers.

II.   Good practice

OAI identified good practices, as follows:

Programme management

The Office developed several tools to facilitate monitoring of programme and project activities, such as (a) the Internal Project Monitoring Calendar introduced on the Office's intranet; (b) internal projects dashboard on key indicators on projects' performance, including delivery status, evaluation pending response/actions; (c) peer-to-peer review group on quality of programming; (d) guidance note on integrated results-based programme implementation, including quality programming, monitoring, planning and reporting requirements for the Office; and (e) checklists for budget revision.

III.   Audit results

Satisfactory performance was noted in the following areas:

(a)   Governance and strategic management. The governance and strategic management function was adequate and reliable and ensured the achievement of the Office's delivery. Organizational structure, reporting lines, and business processes were also adequate. No issues were identified in the areas of leadership and financial sustainability.

(b)   United Nations system coordination. Staffing, planning, budgeting and reporting of activities by the United Nations Country Team were found to be adequate. The records of meetings among United Nations agencies, donors and government representatives disclosed that UNDP was performing its coordination functions well. The Regional Director of the Europe and Central Asia United Nations Development Group approved the Office's request to defer HACT (Harmonized Approach to Cash Transfers) implementation until the end of the current programmatic cycle.

(c)   Programme management. The Office had made important progress in the implementation of the 2010-2015 programme, and had instituted a strong results-based management structure throughout its programming. OAI met with government counterparts and donors, and they expressed their appreciation for the work undertaken by the Office.

(d)   Partnerships and resource mobilization. The Office had an adequate resource mobilization approach and was able to engage in new partnerships during the current programme cycle. The Office was perceived by donors as a good and reliable partner, and it had established a good a relationship with the Government.

(e) <u>General administration</u>. The review of general administration activities, including common services, fuel management, vehicle management, and processing travel expense claims disclosed that controls were generally well established and functioning adequately. The review of asset records and the physical verification conducted disclosed that controls were functioning effectively.

(f) <u>Information and communication technology</u>. The systems managed by the Office, including hardware, software, systems security, and disaster recovery mechanisms, were operating adequately.

(g) <u>Safety and security</u>. The Office provided records of Security Management Team meetings and the risk assessment was conducted in 2014. The Office was compliant with safety and security requirements in the Country.

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

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

High priority recommendations, arranged according to significance:
(a) Strengthen controls in approving vendors in Atlas (Recommendation 3).
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(c) Avoid using the service contract modality as a cost-saving measure when filling vacant positions that require performing core functions (Recommendation 2).
(d) Strengthen controls in procurement management and monitoring (Recommendation 5).

Medium priority recommendations:
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The detailed assessment is presented below, per audit area:

A. Programme activities

1. Project management

[**NOTE**: Part of this section has been redacted as it is deemed to contain sensitive information.]

Issue 1   <u>Weak controls in nationally implemented project</u>

According to the 'Programme and Operations Policies and Procedures', as part of the project appraisal process, appropriate UNDP representatives and stakeholders shall ensure that a project has been designed with a realistic project scope with regard to the outputs and the specified time frame. All projects and substantive revisions should be reviewed and approved through a Project Appraisal Committee meeting to ensure that outputs are aligned with the desired results of the Country Programme. The role of Project Manager is defined as the one that has the authority to run the project on a day-to-day basis on behalf of the implementing partner within the constraints laid down by the Project Board. The implementing partner appoints the Project Manager.

In addition, the 'Programme and Operations Policies and Procedures' require that a progress report be submitted to the Project Board for review at least once a year for each project to undertake their project oversight and steering functions. Furthermore, a final project review should be conducted during the final quarter of a project's duration. Like the annual review, the final project review is driven by the Project Board and may involve other stakeholders, as required.

A sample of six projects (five nationally implemented by the Government and one directly implemented by the Office) was reviewed and the following weaknesses were noted:

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B.   Operations

1.   Human resources

Issue 2   <u>Improper use of service contract modality</u>

The service contract modality is intended to engage individuals for development projects or to perform UNDP's non-core support services, which would normally be outsourced to an external company (e.g., custodial, security and information technology services). The 'Service Contract Guidelines' state that service contract holders should not perform core functions, specifically functions that are of a continuing nature and are part of the central work of UNDP.

The Office engaged 18 individuals under the service contract modality and all of them were performing core functions in various units of the Office, covering both programme and operations functions. The Office explained that this was driven by the higher costs associated with the use of fixed-term contracts, which would have exceeded the budget available to fund these posts.

Since service contract holders are not granted approving rights in Atlas (enterprise resource planning system of UNDP), there is an increased risk of duties not being adequately segregated due to the limited number of staff members that can perform certain functions. In addition, the different levels of remuneration and benefits between service contract holders and staff under fixed-term appointments may create tension among personnel in the Office performing the same or similar tasks.

Priority	High (Critical)
Recommendation 2: The Office should avoid using the service contract modality as a cost-saving measure when filling vacant positions that require performing core functions.	
Management action plan: The Office agreed with the recommendation. The service contract modality is used to provide full operational support to nationally implemented projects in a complex business environment. The Office is consulting UNDP headquarters on the implementation of the new policy on direct project costing, which is important in making a determination on which contract modality to use. **Estimated completion date:** January 2016	

2. Finance

Issue 3   Weaknesses in vendor approval

The 'Operational Guide of the Internal Control Framework for UNDP' states that the vendor approver must ensure the vendor is authentic. For example, the Country Office should conduct background checks of all vendors to ensure they are bona fide companies. This may include reference checking with other entities who have conducted business with the vendor, along with a physical inspection of the vendor's business premises.

Vendor records in Atlas should be reviewed prior to creating a new vendor profile to ensure there are no duplicate records. When a vendor has not fulfilled the conditions of previous contracts, this should be documented and assessed as part of the evaluation of future bids. The Office's vendor verification procedures included a process to confirm that a company registration document was in place and the company was not on the United Nations ineligible vendors list.

In response to the draft report, the Office explained that it had comprehensive consultations with the Legal Support Office, the Procurement Support Office, and the Chair of the Regional Advisory Committee on Procurement on due diligence of vendors, which also included the documents sought from the vendors. Documentary evidence was provided to show that due diligence practices were established in the Office. OAI reviewed the documents and confirmed that the Office performed due diligence.

Notwithstanding the due diligence performed by the Office, a number of issues were identified following the review of the vendors' database:

- Twelve vendors had the same address with other vendors in the system, and all payments to these 12 vendors were made to two bank branches in another country. The Office issued purchase orders totalling $0.8 million for these vendors during the period 2010-2014.

- The performance evaluation of one vendor was unsatisfactory in 2012 and 2013 due to its failure to deliver the required products and due to the fact that the vendor was not responsive in subsequent communications. However, this vendor continued to receive orders during the audit period.

In response to the draft report, the Office explained that procurement is a compliance-based function and should be conducted in strict compliance with the established policies. Suspending vendors based on negative past performance is not in line with the 'Programme and Operations Policies and Procedures', in particular the vendor sanction procedures. A vendor can only be suspended by authorized corporate bodies if found to be involved in proscribed practices. Past performance evaluations provide useful input into contract award decision-making processes, but are not a legitimate reason to reject otherwise responsive offers. Such a practice would expose UNDP to the risk of protest/legal action by the bidders.

- The vendor database had 11 duplicate vendor names, including 4 that were active. The Office deactivated the duplicate records subsequent to the audit fieldwork.

By not having sufficient vendor information, the Office might not be able to (a) determine whether the vendor has the capacity to fulfill its contractual obligations, (b) monitor if vendor contracts reached the cumulative procurement thresholds, and (c) confirm whether the vendor is included in the United Nations ineligible vendors list. There is also a risk for irregularities and fraud in the procurement process.

Priority	High (Critical)

Recommendation 3:

The Office should strengthen controls in approving vendors in Atlas by

(a) conducting comprehensive research to identify established companies that will be contacted to bid on relevant procurements;

(b) requiring bidders to provide information to ensure that the vendor is authentic, including a declaration of owners' interest in other companies and the experience of vendors and capacity to provide goods and services;

(c) conducting regular reviews of existing vendors and deactivating all vendors with duplicate profiles.

Management action plan:

Management commented that:

(a) Current practices are compliant with this recommendation. Preliminary market research activities are practiced in the Office for all purchases over $5,000. Apart from that, all cases with estimated value over $5,000 are at least, posted online and disseminated via email as demonstrated to the auditors. Large purchases are announced in a nationwide circulated newspaper media, on UNDP procurement website, United Nations Global Marketplace and United Nations Development Business pages in line with corporate requirements.

(b) Current practices are compliant with this recommendation: evaluation of experience and capacity to provide goods and services are part of standard evaluation processes and reflected in evaluation reports. The Office might not have requested to provide specifically a "declaration of owners interest in other companies", but it certainly looks into business registration documents, company charter and similar to obtain information on owners and profile of the vendor.

(c) Current practices are compliant with this recommendation: value for money is one of the underlying principles of UNDP procurement and no purchase is cleared without a documented value-for-money analysis and justification.

(d) The Office promptly deactivated four duplicate vendors and will perform the review regularly.

Estimated completion date: Done

OAI response:

OAI acknowledges the actions taken by management; these will be reviewed at a later stage as part of the standard desk follow-up process of OAI. Due to a specific business environment the Office is expected to implement all elements in the recommendation to further strengthen controls over approving vendors.

[**NOTE**: This section has been redacted as it is deemed to contain sensitive information.]

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3. Procurement

Issue 5   Procurement cases not submitted to procurement review committees

The 'Programme and Operations Policies and Procedures' provide that contracts or series of contracts with a cumulative value above $50,000 within a calendar year must be submitted to the Contracts, Assets and Procurement Committee. A "post facto" situation arises when a contract is finalized that exceeds the delegated authority, without submission to the procurement review committee. The 'Programme and Operations Policies and Procedures' define "post facto" actions as a serious deviation and officials that approve such contracts are solely accountable for the consequences resulting from these actions.

OAI noted that during 2013 and 2014, eight vendors with cumulative contract values totalling $473,852 ($195,838 in 2013 and $278,014 in 2014), exceeded the threshold of $50,000, but their contracts were not submitted to the Contracts, Assets and Procurement Committee for review before the contracts were awarded. The Office indicated there had been an oversight in the tracking of cumulative procurement values for vendors. The Office identified the control weakness in April 2015 and proposed to develop a checklist for new contract requests; however, during the audit, OAI identified three additional vendors that exceeded the thresholds and were not submitted to the Contracts, Assets and Procurement Committee for review.

Not submitting high value procurement cases to the relevant procurement committee may prevent the organization from achieving best value for money.

Priority	High (Critical)
Recommendation 5: The Office should strengthen controls in procurement management and monitoring by submitting all procurement cases (including the 11 vendor contracts) that meet the procurement threshold to the procurement review committee.	
Management action plan: This issue has been identified prior to the audit. The information on per vendor cumulative values for 2014 was provided to the Contracts, Assets and Procurement Committee and corrective measures were proposed in the submission. The Office further stated that values were checked for each procurement case regardless of purchase order/contract value before clearance for approval. A checklist for this purpose has been introduced. As of September 2015, three cumulative value cases for the calendar year 2015 had been submitted and reviewed by the Contracts, Assets and Procurement Committee in a timely manner. **Estimated completion date:** September 2015	
OAI response: OAI acknowledges the action taken by management; these will be reviewed at a later stage as part of the standard desk follow-up process of OAI.	

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 not included in this report.