UNITED NATIONS DEVELOPMENT PROGRAMME
Office of Audit and Investigations

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CONSOLIDATED REPORT
ON THE AUDITS
OF SUB-RECIPIENTS OF GRANTS FROM
THE GLOBAL FUND TO FIGHT AIDS, TUBERCULOSIS AND MALARIA
MANAGED BY UNDP
(FISCAL YEAR 2011)

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Executive Summary

Background

In December 2012, the Office of Audit and Investigations (OAI) analysed audit reports of projects implemented by non-governmental organizations or government institutions that were Sub-recipients of grants from the Global Fund to Fight AIDS, Tuberculosis and Malaria (Global Fund). As of December 2012, UNDP was the Principal Recipient of 55 Global Fund grants in 25 countries totalling $1.4 billion. Except for United Nations entities, organizations engaged as Sub-recipients of those grants are required to be audited by external audit firms pursuant to the UNDP procedures for audits of projects under the non-governmental organization/national implementation modality and to submit those audit reports to UNDP. The main objective of those audits is to provide UNDP with assurance that resources have been used properly.

Purpose and scope of the review

The OAI desk review aimed to: (a) analyse the distribution of external audit firms' audit opinions; (b) identify common audit issues reported by them and (c) determine the implementation status of the audit recommendations made. The review covered 50 audit reports for fiscal year 2011 that had been uploaded by country offices in the Comprehensive Audit and Recommendations Database System (CARDS) of OAI.

These 50 audit reports pertained to 47 awards funded by the Global Fund in 22 countries where UNDP was the Principal Recipient and which met the required audit threshold. The reports covered fiscal year 2011 project expenditures totaling $99.8 million, equivalent to 31 percent of the overall UNDP/Global Fund expenditures of $324.3 million incurred in 2011. In terms of distribution, $61.7 million (62 percent) of the expenditures audited related to grants managed under the Additional Safeguard Policy.[1] The audit report of Global Fund Sub-recipients in Yemen, with total expenditures of $0.4 million planned for audit, had not been submitted at the time this report was drafted.

Results of the review

Of the $99.8 million in expenditures audited, $6.8 million (7 percent) had qualified audit opinions with a net financial impact of about $0.1 million representing 0.1 percent of the total audited expenditures. By comparison, in 2010, $5 million (3 percent) of expenditures had qualified audit opinions with a net financial impact of about $0.6 million, equivalent to 0.3 percent of the audited expenditure. The overall decrease in the net financial impact of qualified audit opinion denotes an improvement over 2010. Of concern in 2011, is the programme in Niger, which received qualified audit opinions in three of the last four years (2008, 2010, and 2011). In 2011, the net financial impact of the qualification in Niger was $182,000. Similarly, the programme in the Democratic Republic of the Congo has received qualified audit opinions in the last four consecutive years (2008, 2009, 2010, and 2011) but the grants were ultimately closed.

The external audit firms raised a total of 488 audit observations in fiscal year 2011, categorized by risk severity and by audit area, as follows:

- Risk severity: The 488 audit observations were comprised of 67 (14 percent) categorized as high priority; 233 (48 percent) medium priority and 188 (38 percent) low priority.

[1] The Additional Safeguard Policy is a range of tools established by the Global Fund as a result of its risk management processes.

- Audit areas: There were three core audit areas, namely: financial management; project progress and rate of delivery and; human resources management and administration, which together, accounted for 361 (74 percent) of the total 488 audit observations.

The frequent absence of or inadequacy of documents in support of the expenditures audited, errors in recording of transactions, as well as the lack of reconciliation of bank statements and cash in hand with accounting records can be attributed to the sub-optimal financial management capacity of many of the Sub-recipients.

Implementation of audit recommendations

OAI focused its assessment on the implementation status of the high priority recommendations. Of the audit recommendations for fiscal year 2010, all 201 observations categorized as high priority had "action plans" (intended management action to address the observation) uploaded in CARDS. Of the 201 audit recommendations, 75 (37 percent) had been implemented and 107 (53 percent) withdrawn (the grant or project had closed, or UNDP had ceased working with the Sub-recipient). The implementation of four (2 percent) recommendations were still in progress, while only 15 (7 percent) had not been implemented in 2012. The closure of grants in the Democratic Republic of the Congo and Mauritania, which accounted for the majority of the outstanding recommendations in fiscal year 2010, contributed to the improved implementation rate for fiscal year 2011.

Conclusion

More effort is required in following up on the implementation of recommendations to ensure that the identified root causes of the audit observations are adequately addressed in a timely manner. However, an improvement was noted in financial management, as the net financial impact of qualified opinions was only about $0.1 million in 2011, as compared to $0.6 million in 2010, and $1.7 million in 2009.

As the Principal Recipient of Global Fund grants, UNDP is more often than not partnering with Sub-recipients, whose financial management capacities are sub-optimal, and who are operating within a difficult country context. Recognizing the need for close monitoring and oversight of Sub-recipient financial management, the Terms of Reference for the non-governmental organization/national implementation modality audits had been strengthened for financial management and expanded to also include review of controls and processes. In 2012, the Bureau for Development Policy Global Fund Partnership Team had also engaged in long term agreements with external audit firms for future audits of Sub-recipients to improve the consistency and quality of the Sub-recipient audit reports.

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Director
Office of Audit and Investigations

1. Introduction

The Global Fund is a global public/private partnership dedicated to attracting and disbursing resources to prevent and treat HIV/AIDS, tuberculosis, and malaria. As of December 2012, UNDP was the Principal Recipient of 55 Global Fund grants in 25 countries totaling $1.4 billion. As Principal Recipient, UNDP is accountable for the proper use of grant funds and the implementation of projects in recipient countries. UNDP may appoint a Sub-recipient to implement part of the project activities that would otherwise be carried out by UNDP. A Sub-recipient can be a governmental entity, a United Nations entity, or a non-governmental organization. Sub-recipients that are a governmental entity or a non-governmental organization are required to be audited by external audit firms pursuant to the UNDP procedures for audits of projects under the non-governmental organization/national implementation modality.

During the last three years, the total UNDP/Global Fund expenditures have been steadily increasing: $254 million in 2009, $286 million in 2010 and $324 million in 2011. During the same period, project expenditures incurred by Sub-recipients that were audited under the non-governmental organization/national implementation modality audit process were $112 million in 2009, $192 million in 2010 and $100 million in 2011. Expenditures for Additional Safeguard Policy countries showed the same pattern of variation over the period with expenditures of $47 million in 2009, $140 million in 2010 and $62 million in 2011.

2. OAI role in the non-governmental organization/national implementation modality audits

The main objective of a non-governmental organization/national implementation modality audit is to provide UNDP with assurance that resources have been used properly. Each year, UNDP country offices that are Principal Recipients advise OAI of the Sub-recipients to be audited as part of their annual non-governmental organization/national implementation modality audit plans. Each Sub-recipient selected is required to undergo an audit of its expenditure, cash and assets statements. The audit of the Sub-recipient's expenditures must be completed by the deadline established by OAI. UNDP country offices are responsible for selecting and engaging these external auditors by using the standard terms of reference, established by OAI for the audit of non-governmental organization/national implementation modality projects. The final reports on the audit of Sub-recipients are to be submitted to OAI for review. When requested by the Global Fund, the country office may provide the final audit report of the Sub-recipients to the Global Fund or its representative (the Local Fund Agent).

The submission, tracking and analysis of non-governmental organization/national implementation modality audit reports and action plans, is supported by a dedicated module in CARDS.

3. Review of audits of Global Fund Sub-recipients in fiscal year 2011

In December 2012, OAI conducted a desk review to:

(a) analyse the distribution of external audit firms' audit opinions;
(b) identify common issues reported by the audit firms; and
(c) determine the implementation status of the audit recommendations made.

The desk review encompassed 50 audit reports for fiscal year 2011 that had been uploaded by country offices to CARDS and covered 47 awards funded by the Global Fund in 22 countries where UNDP was the Principal Recipient and which met the required audit threshold. The reports covered fiscal year 2011 project expenditures totaling $99.8 million, equivalent to 31 percent of the overall UNDP/Global Fund expenditures of $324 million incurred in 2011. In terms of distribution, $61.7 million (62 percent) of the expenditures audited were related to grants managed under the Additional Safeguard Policy, whereas $38.1 million (38 percent) were not.

In line with OAI criteria for the selection of Sub-recipients for audit, audits were not required for seven countries where UNDP was directly implementing projects without partnering with Sub-recipients (Chad, Mauritania, Maldives, Sudan), where the Sub-recipients were United Nations entities (Iraq), or where the expenditures incurred by the Sub-recipients did not meet the audit threshold (Central African Republic, Togo).

The analysis of the audit opinions and audit observations of the 50 Sub-recipient audit reports showed the following:

Distribution of audit opinions

The external auditor of each Sub-recipient was required to certify, express an opinion, and quantify the net financial impact on three types of financial statements, namely:

(a) The Certification on UNDP Statement of Expenditure - Combined Delivery Report for the period 1 January to 31 December 2011;

(b) The Certification on Statement of Cash Position as at 31 December 2011; and

(c) The Certification on Statement of Assets and Equipment as at 31 December 2011.

The distribution of audit opinions by country as well as the definition of the type of external audit opinions are detailed in Annex 1 and 2, respectively.

In fiscal year 2011, of the $99.8 million audited expenditures, $93 million (93 percent) had unqualified audit opinions and $6.8 million (7 percent) had qualified audit opinions (Bosnia and Herzegovina, Haiti, Liberia, Niger and Democratic Republic of the Congo). The net financial impact of the qualified opinions was about $0.1 million, representing 0.1 percent of the total audited expenditure, as shown in Figure 1.

Figure 1: Net Financial Impact of the Qualified Opinion on Audited Expenditures

Country Office	Audited Expenditure (GFATM)	Total CDR	Qualified Opinion			
			# Awards	Amount Audited	Amount of Qualification of Audit Opinion	Net Financial Impact
Democratic Republic of Congo	5,182,924	24,875,026	1	331,383	2,168	-268
Liberia	1,753,951	6,018,774	1	1,001,865	328,012	-328,012
Niger	655,754	2,457,782	1	531,632	192,770	-181,842
Bosnia and Herzegovina	4,527,126	7,793,072	1	4,527,126	224,126	224,126
Haiti	3,980,822	12,287,004	1	366,716	366,716	230,874
Total	**16,100,577**	**53,431,658**	**5**	**6,758,722**	**1,113,792**	**-55,122**

Audit observations

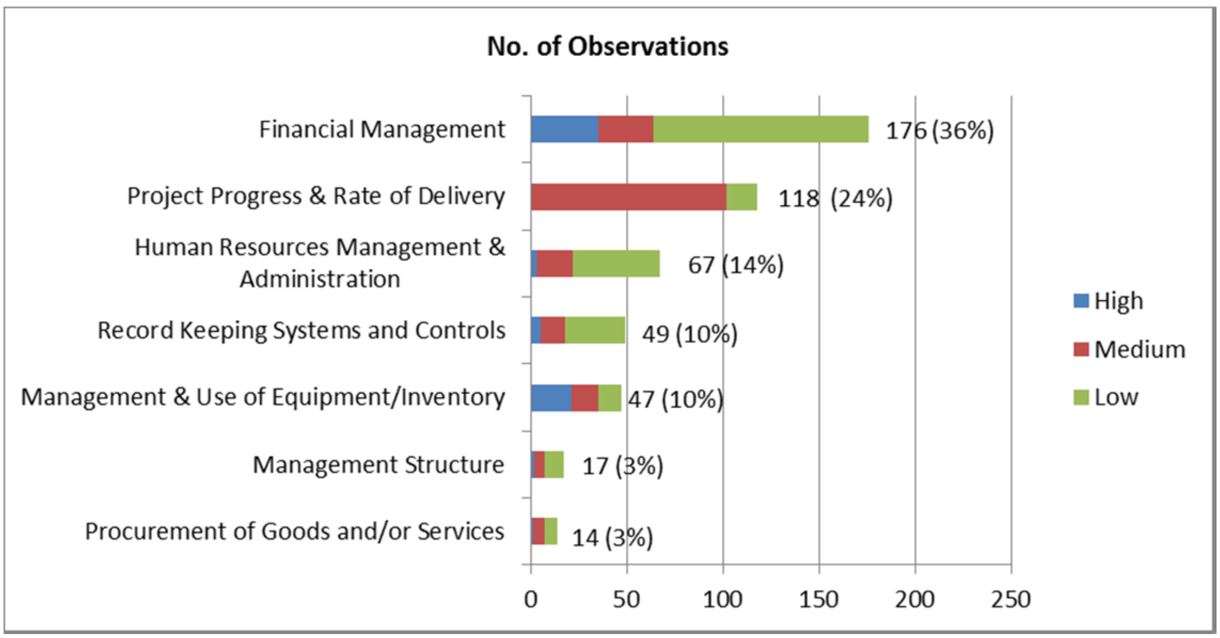
For each Sub-recipient audit, the Sub-recipient external auditors were required to describe internal control weaknesses in a management letter. The management letter described the audit observations and recommendations; categorized the nature of audit observations by risk severity; classified the audit observations by audit areas and inferred the possible causes of the reported internal control weakness. The external audit firms raised 488 observations in the 50 Sub-recipient audit reports for fiscal year 2011. The reports were examined by OAI and the distribution of the audit observations by risk severity, by audit area and by cause were as follows:

Risk severity:
In terms of risk severity, the external audit firms classified the risk severity of the audit observations in three categories, namely high, medium, or low. The 488 audit observations comprised of 67 (14 percent) categorized as high priority; 233 (48 percent) categorized as medium priority and 188 (38 percent) categorized as low priority.

Audit areas:
The external audit firms classified the nature of audit observations according to seven audit areas, namely: (a) financial management; (b) project progress and rate of delivery; (c) human resources management and administration; (d) record keeping systems and controls; (e) management and use of equipment/inventory; (f) management structure and (g) procurement of goods and/or services.

The distribution by audit area and risk severity for the 488 audit observations is shown in Figure 2.

Figure 2: Classification of Audit Observations by Audit Area



Three core audit areas, namely financial management; project progress and rate of delivery; and human resources selection and administration, accounted for 361 audit observations or about 74 percent. In respect to financial management, the most common issues related to inadequate documentation in support of expenditures, errors in recording transactions, the lack of adequate accounting or project management software and the lack of reconciliation between accounting records/bank statements to cash in hand. Project management issues principally concerned delivery delays. Human resources issues mainly encompassed a lack of transparency in the hiring process, and poor management of contracts and personnel performance assessments.

4. Implementation of audit recommendations

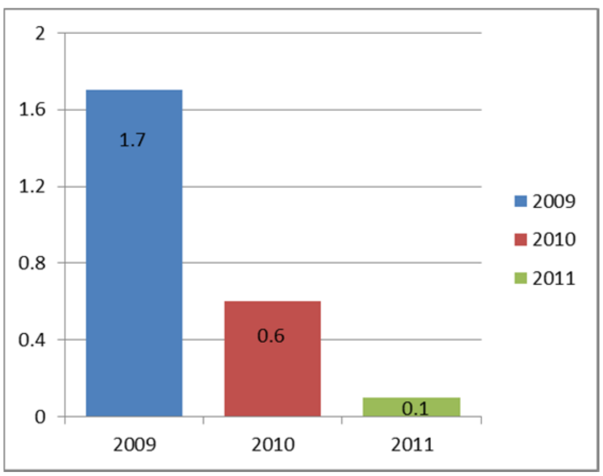
As part of the project audits, the auditors were required to review the progress achieved by the Sub-recipients in implementing the prior year's audit recommendations (fiscal year 2010) and to report on the updated "action plans" (intended management action to address the observation) for those recommendations. The country offices are required to upload and monitor the implementation status of the recommendations in CARDS.

OAI focused its assessment of the implementation status on the high priority recommendations. Of the 201 audit recommendations ranked high priority in fiscal year 2010, all had "action plans" uploaded in CARDS. Of the 201, 75 (37 percent) had been implemented, and 107 (53 percent) were withdrawn (the grant or project had closed, or UNDP had ceased working with the Sub-recipient). Fifteen (7 percent) recommendations had not been implemented in 2012, while four (2 percent) were still in progress. This marks a significant improvement over the past three years. In 2010, only 24 out of 135 (18 percent) high priority audit recommendations had been implemented. However, the closure of grants in the Democratic Republic of the Congo and Mauritania, which accounted for most of the outstanding recommendations for fiscal year 2010, contributed to the improved implementation rate for fiscal year 2011, as shown by the number of withdrawn recommendations above.

5. Conclusion

More effort is required in the follow up of the implementation of recommendations to ensure that the identified root causes of the audit observations are adequately addressed in a timely manner and that the implementation status is kept up-to-date in CARDS. An improvement was noted in financial management, as the net financial impact of qualified opinions was only about $0.1 million in 2011, representing 0.1 percent of the total audited expenditures, as compared to $0.6 million in 2010, equivalent to 0.3 percent of the audited expenditure, and $1.7 million in 2009, or 1.5 per cent of the audited expenditure (see Figure 5).

Figure 5: Comparison of Net Financial Impact of Qualified Opinions ($ million) from 2009 to 2011



As Principal Recipient of Global Fund grants, UNDP is more often than not partnering with Sub-recipients, whose financial management capacities are sub-optimal, and who are operating within a difficult country context. Recognizing the need for close monitoring and oversight of Sub-recipient financial management, the Terms of Reference for the non-governmental organization/national implementation modality audits had been strengthened for financial management and expanded to also include review of controls and processes. In 2012, the Bureau for Development Policy Global Fund Partnership Team had also engaged in long term agreements with external audit firms for future audits of Sub-recipients to improve the consistency and quality of the Sub-recipient audit reports.

Annex 1: Distribution of audit opinions on the fiscal year 2011 non-governmental organization/national implementation modality audit reports of the Global Fund Sub-recipients

Country Office	Audited Expenditure	Total CDR	Qualified		Unqualified		NFI Current Year
			# Awards	Amount Audited	# Awards	Amount Audited	
Angola	169,817	7,247,112			1	169,817	
Belarus	3,359,533	16,729,734			3	3,359,533	
Bolivia	3,414,740	3,414,740			1	3,414,740	
Bosnia and Herzegovina	4,527,126	7,793,072	1	4,527,126			224,126
Cuba	8,598,263	9,917,034			3	8,598,263	
Democratic Republic of the Congo	5,182,924	24,875,026	1	331,383	4	4,851,541	-268
El Salvador	1,461,425	3,647,742			2	1,461,425	
Haiti	3,980,822	12,287,004	1	366,716	1	3,614,106	230,874
Iran	1,875,245	10,647,563			1	1,875,245	
Kyrgyzstan	311,612	5,647,418			3	311,612	
Liberia	1,753,951	6,018,774	1	1,001,865	1	752,086	-328,012
Montenegro	1,547,416	3,697,236			2	1,547,416	
Nepal	6,354,463	6,354,463			1	6,354,463	
Niger	655,754	2,457,782	1	531,632	1	124,122	-181,842
Programme of Assistance for the Palestinian People	111,789	287,164			1	111,789	
Sao Tome and Principe	485,396	485,396			2	485,396	
Sudan-South	3,079,573	$4,763,315			3	$3,079,573	
Syria	293,629	830,989			1	293,629	
Tajikistan	4,105,526	25,111,568			3	4,105,526	
Turkmenistan	72,041	2,819,356			1	72,041	
Zambia	1,252,594	6,999,968			2	1,252,594	
Zimbabwe	47,205,277	64,288,652			5	47,205,277	
Total	**99,798,916**	**226,321,108**	**5**	**6,758,722**	**42**	**93,040,194**	**-55,122**

Annex 2: Definition of External Audit Opinions

Unqualified (Clean or positive) Opinion

An unqualified opinion should be expressed when the auditor concludes that the financial statements give a true and fair view or are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.

Qualified Opinion – a modified (negative) audit opinion

A qualified opinion should be expressed when the auditor concludes that an unqualified opinion cannot be expressed but that the effect of any disagreement with management, or limitation on scope is not so material and pervasive as to require an adverse opinion or a disclaimer of opinion. A qualified opinion should be expressed as being 'except for' the effects of the matter to which the qualification relates.

Disclaimer of opinion – a modified (negative) audit opinion

A *disclaimer of opinion* should be expressed when the possible effect of a limitation on scope is so material and pervasive that the auditor has not been able to obtain sufficient appropriate audit evidence and accordingly is unable to express an opinion on the financial statements.

Adverse – a modified (negative) audit opinion

An *adverse opinion* is expressed by an auditor when the financial statements are significantly misrepresented, misstated, and do not accurately reflect the expenses incurred and reported in the financial statements (**UNDP CDR**, statement of cash, statement of assets and equipment).

An adverse opinion is expressed when the effect of a disagreement is so material and pervasive to the financial statements that the auditor concludes that a qualification of the report is not adequate to disclose the misleading or incomplete nature of the financial statements.