UNITED NATIONS DEVELOPMENT PROGRAMME
Office of Audit and Investigations

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AUDIT

OF

UNDP COUNTRY OFFICE

IN

URUGUAY

Report No. 1324

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Report on the audit of UNDP Uruguay
Executive Summary

The UNDP Office of Audit and Investigations (OAI) conducted an audit of UNDP Uruguay (the Office) from 21 April to 2 May 2014. 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, safety and security, asset management, leave management, Global Environment Facility).

The audit covered the activities of the Office from 1 January 2013 to 31 March 2014. The Office recorded programme and management expenditures totalling $17.4 million in 2013, and $3.2 million in 2014 (as at 31 March). The last audit of the Office was conducted by OAI in 2008.

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 = **5**, high priority = **1**

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:

Financial sustainability of Office at risk (Issue 1)	The Office faced challenges similar to those faced by other high income countries, and consisted of increased operational costs, and reduced inflow of core resources. Over the past four years the Office had spent more than its actual income by approximately $350,000 per year. The Office had engaged UNDP's Management Consulting Team to conduct an evaluation of its Operations, which resulted in a Transformation Plan that included a restructuring of the Office. Although the Office had begun implementing the plan, the financial situation of the Office continued to be a matter of concern due to the decline in income and the Office's inability to secure funding from the Government to support its

operational costs.

Recommendation: Continue implementing actions contained in the Transformation Plan by: (a) expanding partnership base; (b) enhancing resource mobilization; (c) accelerating delivery to increase income; (d) reducing transaction cost and overall operational cost; and (e) negotiating with the Government to reduce rental costs.

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 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 Montevideo, Uruguay (the Country) had 20 staff members, 12 service contract holders and 8 individual contracts. The Office was implementing its Country Programme for the period 2011-2015 as part of the Delivering as One 'United Nations Development Assistance Framework Action Plan', with four priority areas aligned to national development priorities. The priority areas of the 'United Nations Development Assistance Framework Action Plan' were: (a) productive diversification and international integration; (b) environment; (c) social development; and (d) democratic governance and human rights. Since the Country was considered a high income country, the presence of donors had gradually decreased. As a result, the Office had difficulties in securing larger budgets for project implementation. This was despite the fact that the Country still faced human development needs.

II. Audit results

Satisfactory performance was noted in the following areas:

(a) Governance and strategic management. Organizational structure and delegations of authority were adequate. Project risk management, planning and reporting in Atlas were well managed. In addition, a major reorganization of the Office was undertaken in 2013 to address operational challenges and requests from the host Government. In meetings with them, government officials indicated that they were appreciative of the reorganization efforts undertaken by the Office.

(b) United Nations system coordination. Key controls were in place and adequate. The United Nations Country Team shared the common goal of improving coordination within the United Nations system. In addition, joint programming was successful.

(c) Programme activities. Resource mobilization and partnership strategies contained in the 'United Nations Development Assistance Framework Action Plan' were adequate. OAI met with government counterparts and implementing partners and donors, who expressed their appreciation of the Office as a development partner.

(d) Operations. No reportable issues were identified concerning finance, procurement, general administration and safety and security. Supporting documentation on financial and operational matters were properly kept and classified in an orderly manner to facilitate the Office's day to day work as well as the tests carried out throughout the audit. Information and communication technology managed by the Office, including hardware, software, systems security, and disaster recovery mechanisms were adequately operating.

OAI made five recommendations ranked high (critical) and medium (important) priority.

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

High priority recommendation:

(a) Continue implementing actions contained in the Transformation Plan (Recommendation 1).

Medium priority recommendations, arranged according to significance:

(a) Conduct audits and evaluations of implementing partners in a timely manner (Recommendation 2).
(b) Adhere to prescribed procedures for project appraisal and substantive revisions (Recommendation 3).
(c) Revise and update the internship cooperation agreement with the academic institution in order to align it to UNDP policies (Recommendation 4).
(d) Implement and correctly manage the use of contract modalities and individual contracts (Recommendation 5).

The detailed assessment is presented below, per audit area:

A. Governance and strategic management

1. Financial sustainability

Issue 1 Financial sustainability of Office at risk

The Office faced challenges similar to those faced by other high income countries, and consisted of increased operational costs, and reduced inflow of core resources. The situation was further exacerbated by recent changes in national legislation in regard to public funding, which limited the Office's ability to implement projects or provide services.

While the financial situation of the Office remained within the corporate limits of operational reserve (12 months or higher), over the past four years the Office had spent more (e.g. approx. $350,000 in excess per year) than its actual income (e.g. core funds plus extrabudgetary resources) thus impacting the financial position of the Office. In order to ensure that it had the necessary resources to achieve its overall mandate, in 2012, the Office engaged UNDP's Management Consulting Team to conduct an overall evaluation of its operations. The evaluation was meant to: (a) identify gaps and review business processes; (b) realign operations and programme areas to focus on the provision of high quality advisory services; (c) seek out new partnerships to reduce government cost-sharing; and (d) support negotiations with the host Government in an effort to reduce rental and operational costs.

The evaluation resulted in a Transformation Plan that included a restructuring of the Office, as well as a focus on programme activities and related costs. The implementation of that Plan began in early 2013 and was still ongoing at the time of the audit. Despite the changes in structure resulting from the abolishment of four core posts and the introduction of a cost savings approach, which resulted in savings of some $250,000 in 2013, the financial situation of the Office continued to be a matter of concern due to the decline in income over the past months and Office's inability to secure funding from the Government to support its operational costs (mainly rental costs).

Priority	High (Critical)

Recommendation 1:

Continue implementing actions contained in the Transformation Plan by:

(a) expanding partnership base;
(b) enhancing resource mobilization;

(c) accelerating delivery to increase income;
(d) reducing transaction cost and overall operational cost; and
(e) negotiating with the Government to reduce rental costs.

Management action plan:

On the resource mobilization initiatives identified in the Transformation Plan, the Office will continue its efforts to expand its partner base and diversify funding sources, and will also explore non-traditional partnerships.

The main lines of action are:

- Government Resources Programme - Monitoring the design and implementation of policies and programmes financed from the Government will require a tight follow up of the pipeline and delivery, particularly considering the circumstances of national elections in 2014 and a new Government taking office in March, 2015.

- Follow up of the major donor partners - (i) Inter-American Development Bank (IDB): the objective is to consolidate a solid relationship developed since 2012 with IDB and aimed at further opportunities for resource mobilization, (ii) Global Environment Facility (GEF): the relationship with the donor and the national environmental authority (MVOTMA, Ministry of Housing, Land Planning and Environment) will be consolidated, particularly considering the upcoming GEF VI.

- CAF and EU - the Office will continue its efforts in presenting and evaluating possible funding initiatives in the following areas: transport policy and development programme providers.

- Allocation of government funds additional to GLOC - In alignment with the Executive Board decision 2013/30 – Funding of differentiated physical presence, an agreement is being signed in which the Government, without prejudice to the regular financial contribution (GLOC) will make an additional annual contribution to UNDP to support the operating costs of the office into a sum of $350,000. That commitment will be governed by that agreement during the first two years -2013 and 2014, and is expected that it will also be included from 2015 in the National Budget. This is a key initiative in order to cover the annual deficit of the current structure of the office.

- On reducing transaction and overall operational costs - The office has made efforts to reduce operational and transactional costs. In April 2014, the Office reduced the cost of rent and utilities by 35 percent (about $120,000 per year). In December 2014, one of the drivers will retire and the position will be cancelled. This measure will also reduce operational costs.

  The Office has systematized internal processes simplifying and eliminating duplication of tasks without affecting the quality of UNDP operations in Uruguay. In this regard, the Office will continue taking actions to create synergies with other UN agencies and diversify the services provided (e.g. ICT, purchase of supplies, etc.) to increase the distribution of operational costs that are currently fully covered with extrabudgetary funds.

Estimated completion date: June 2015

B. United Nations system coordination

Issue 2 Harmonized Approach to Cash Transfers assurance plan incomplete

The Harmonized Approach to Cash Transfers aims to: (a) reduce transaction costs pertaining to the Country Programmes of the ExCom agencies by simplifying and harmonizing rules and procedures; (b) strengthen the capacity of implementing partners to effectively manage resources; and (c) help manage risks related to the management of funds, and increase overall effectiveness.

A country is considered as being in compliance with this approach when the following four steps have been completed: (a) a macro-assessment of the public financial system has been undertaken; (b) micro-assessments of implementing partners have taken place; (c) agreement has been reached with the Government on implementing the Harmonized Approach to Cash Transfers; and (d) an assurance and audit plan concerning implementing partners has been developed and implemented.

At the time of the audit, the harmonized approach had been implemented and was working well in the Country under the lead role of UNDP, except for the assurance and audit plan, which was still a matter in progress. According to the 'Framework for Cash Transfers', when more than one agency is involved in project implementation, assurance activities (including audits and evaluations) should be coordinated and carried out so as to ensure that funds transferred to implementing partners have been properly managed. The Office had not yet undertaken the required audits of implementing partners due to insufficient planning.

Not undertaking assurance activities in regard to the Harmonized Approach to Cash Transfers may result in the inadequate transfer of funds.

Priority Medium (Important)
Recommendation 2: Conduct audits and evaluations of implementing partners in a timely manner.
Management action plan: The Office is planning to implement the mandatory audits in 2014 in accordance with the implementation of the "Harmonized Approach to Cash Transfer Framework" approved in February 2014. **Estimated completion date:** December 2014

C. Programme activities

Issue 3 Project Appraisal Committee not following prescribed procedures

According to the 'Programme and Operations Policies and Procedures', as part of the project appraisal process, UNDP representatives and stakeholders shall ensure that a project is designed with a clear focus on agreed upon results, and that the Project Document conforms to the standard template. All projects and substantive revisions should be reviewed by a Project Appraisal Committee to ensure that outputs are aligned with the desired results of the Country Programme and that a proper project management structure is in place to monitor and evaluate results. In addition, those projects with a budget of $500,000 or more are also subject to an environmental and social screening as part of the appraisal.

OAI sampled eight development projects and identified the following weaknesses:

- seven Project Documents were reviewed by the Project Appraisal Committee, however, the meeting minutes included limited information or no information at all regarding the discussions on matters such as monitoring and evaluation, baselines and indicators, and were not signed by the participating Committee members;
- one Project Document was not reviewed by the Project Appraisal Committee;
- the template with the results of the environmental and social screening was not requested by the Project Appraisal Committee for those projects with a budget of $500,000 or more; and
- the local Project Appraisal Committee did not review any of the substantive revisions made to the sampled projects.

A thorough review by a Project Appraisal Committee adhering to the standard checklist may have spotted these weaknesses, which could have been addressed in a timely manner during project review and prior to the approval of such projects.

Weaknesses in the review and approval of projects increase the risk of not achieving expected results. Failure to meet expected results can negatively affect UNDP's reputation and could reduce donor interest in funding future projects.

Priority	Medium (Important)

Recommendation 3:

Adhere to prescribed procedures for project appraisal and substantive revisions by:

(a) ensuring that each project is reviewed with respect to its Project Document structure;
(b) including all relevant areas of discussion in line with the 'Programme and Operations Policies and Procedures' in the minutes of Committee meetings;
(c) requesting projects with a budget of $500,000 or more to perform the environmental and social screening and submitting the template with the results to the Committee together with the Project Document as required; and
(d) ensuring that all substantive revisions are reviewed by the Project Appraisal Committee.

Management action plan:

(a) & (b) The Office will ensure that the items enclosed in the 'Checklist for Review of Project Documents' in the 'Programme and Operations Policies and Procedures' will be taken into account when reviewing Project Documents and will be reflected in the minutes of the Project Appraisal Committee meetings to be endorsed by participants.

(c) The environmental and screening procedure will be applied to Projects of more than $500,000, and its results will be presented at a Project Appraisal Committee meeting.

(d) The Office will ensure that substantial revisions are reviewed by a Project Appraisal Committee.

Estimated completion date: August 2014

D. Operations

1. Human resources

Issue 4 Internship programme not compliant with UNDP policies

The ‘UNDP Internship Policy’ provides the framework by which students from diverse academic backgrounds may be assigned to UNDP offices. The policy clearly stipulates the criteria under which UNDP can engage in an agreement with a higher education institution. Specifically, it states that an internship programme is for graduate students, is non-remunerated, limited to a six-month period, and exceptionally may be extended up to nine months.

Furthermore, the ‘UNDP Internship Policy’ states that all costs related to interns working at UNDP must be borne by the nominating academic institution or the Government. The selection of a candidate must be on a competitive basis. Under the existing agreement, the university selected the candidates, and the Office was only involved in the final interview phase of the selection process.

A framework agreement between the Office and a local university was signed in December 2001 by the then Resident Representative. A cooperation agreement was drawn up to address the specific criteria to this agreement and also signed in December 2001. The cooperation agreement was revised and signed once again in 2008 by the Resident Representative at the time.

Even though having a cooperation agreement was noteworthy, it did not comply with the ‘UNDP Internship Policy.’ This was due to the fact that the agreement stipulated that students selected would be:

- engaged in a “work scholarship” for a one year period
- first year undergraduate students
- remunerated by UNDP under a service contract modality
- possibly extended to a second year based on a performance evaluation

The possibility of extending internships for a second year limits the number internship opportunities available for other university students, which defeats the purpose of having a cooperation agreement in the first place.

In addition, OAI noted that the agreement with the local university stipulated that the Office should authorize the use of information managed by the interns for academic purposes, as long as it was not confidential or restricted information. This clause of the agreement is contrary to UNDP communication guidelines on the use of information by a third party. There was no evidence that the agreement itself had been subject to a legal review.

Agreements with academic institutions that are not line with UNDP policies and guidelines may present financial and reputational risks for the Office.

Priority	Medium (Important)
Recommendation 4: Revise and update the internship cooperation agreement with the academic institution in order to align it to UNDP policies, and submit the revised agreement to the Legal Support Office for review.	
Management action plan: The Office has requested advice from the Office of Human Resources. A new procedure for contracting interns to act as Programme Assistants will be implemented in compliance with guidance from the Office of Human Resources. **Estimated completion date:** December 2014	

Issue 5 Incorrect use of contract modality

The 'Programme and Operations Policies and Procedures' cover the various contractual modalities of individuals hired as non-staff and the management of these modalities. The service contract modality is used for hiring individuals under a non-staff contract. The Human Resources Unit within the Office manages this contractual modality, even though this task should be under the purview of the Procurement Unit. The individual contract modality is used for hiring consultants and contractors. An individual contract is a procurement action solely intended for carrying out immediate and temporary services.

A review of a sample of service contracts for nationally implemented projects revealed that the Office did not use this contract modality correctly. For example:

- Service contracts were issued to local consultants when in fact an individual contracts should have been issued.
- Both service contracts and individual contracts were managed by the Human Resources Unit.
- In most cases, the Office did not participate in the selection process.
- The service contracts were remunerated on a percentage basis for output. Under this remuneration scheme, the correct contract modality would have been as individual contracts.
- In the cases of projects implemented with International Development Bank funding, service contracts were substantiated with a "No Objection" issued by the International Development Bank on the Terms of Reference of the post, yet subsequently a competitive process was not carried out.

The Office indicated that the service contract modality was only used for "contract for works" situations. However, the "contracts for works" can only be adopted when a government entity is the signatory. In this case, the Office was the signatory. Other discrepancies were encountered in the management of service contracts, specifically:

- Some of the service contracts were awarded as direct contracts.
- Terms of Reference were not included in the request for approval of a service contract extension.

- Service contracts issued and signed by the Office did not have a numerical sequence for audit trail purposes.
- Leave management of service contract holders was controlled manually because the migration of service contracts to the Atlas Human Resources module was pending.

The incorrect use of contract modalities and human resource management of individual contracts presents financial risks for the Office.

Priority	Medium (Important)
Recommendation 5: Implement and correctly manage the use of contract modalities and individual contracts.	
Management action plan: The service contracts will be reviewed to correct the situations. Regarding the participation of UNDP in the selection process, the Office is negotiating for the Government to carry out the selection process and sign the contracts for nationally implemented projects. In the cases of service contracts and individual contracts under directly implemented projects, the Office adjusted its recruitment process to be in accordance with the 'Programme and Operations Policies and Procedures.' **Estimated completion date:** July 2014	

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>.