



AUDIT

OF

UNDP COUNTRY OFFICE

IN

THE DEMOCRATIC PEOPLE'S REPUBLIC OF KOREA

Report No. 1744

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Report on the Audit of UNDP Democratic People's Republic of Korea Executive Summary

The UNDP Office of Audit and Investigations (OAI) conducted an audit of UNDP Democratic People's Republic of Korea (the Office) from 9 to 16 November 2016. 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, business continuity, monitoring and reporting, financial sustainability);
- (b) United Nations system coordination (development activities, Resident Coordinator Office);
- (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).

The audit covered the activities of the Office from 1 January 2015 to 31 October 2016. The Office recorded programme and management expenditures of approximately \$6.6 million during this period. The last audit of the Office was conducted by OAI in 2015 and was done remotely from OAI's Regional Audit Centre in Kuala Lumpur, Malaysia. The audit team was not able to travel to the Office due to travel restrictions in response to the Ebola outbreak at the time.

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

The Office operates in a complex and difficult environment and the challenges include difficulties in recruiting qualified staff, limited procurement opportunities and restrictive banking services.

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."

The audit did not result in any recommendations.

Implementation status of previous OAI audit recommendations: Report No. 1421 (7 April 2015).

Total recommendations: 4

Implemented: 4

Management comments and action plan

The draft report was shared with the Resident Representative and with senior management of the Regional Bureau for Asia and the Pacific (RBAP). Their 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.



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I. About the Office

The Office, located in Pyongyang, the Democratic People's Republic of Korea (the Country) operates in a complex, constrained and difficult environment. Following the discontinuation of UNDP's operations in the Country in March 2007, the UNDP Executive Board approved the resumption of operations in the Country in January 2009. Since the reopening, the Office has had to work within a limited programmatic space and under a special Internal Control Framework governing its administration, human resources, finance, procurement and monitoring and evaluation. The Office indicated that there were difficulties in recruiting qualified staff members (both national and international), limited procurement opportunities, relatively restrictive banking services, and delays in obtaining necessary clearances from countries exporting goods procured for projects. The Office is required to comply with the sanctions issued by the United Nations Security Council, and several other countries. These have indirectly impacted the Office's programme delivery and operating costs, which are very high in relation to programme expenditure.

The Regional Bureau for Asia and the Pacific (RBAP) mitigated the above challenges by assigning a relatively higher number of international staff to the Office. It also monitored the Office closely and engaged the Office's senior management in all critical matters.

II. Audit results

Satisfactory performance was noted in the following areas:

- (a) Governance and strategic management. Management structures, roles and responsibilities, together with delegation of authorities were established and operating effectively.
- (b) United Nations coordination. Adequate controls were established to manage and lead the United Nations coordination work in the Country.
- (c) Programme activities. Programme and project management were found to be effective and no reportable issues were noted.
- (d) Human resource management. Adequate controls were established and no reportable audit issues were noted.
- (e) Financial management. The review included bank reconciliations, paycycle processes, cancelled cheques, controls over the use of cash cheques and non-cash cheques as well as verifying inventory records to the contents of two safes. Adequate controls were established and no reportable audit issues were noted.
- (f) General administration. Adequate controls were established and functioning effectively.
- (g) Safety and security. The review of the Office's security plan and security risk assessment did not identify any reportable issues.
- (h) Information and communication technology. The audit team reviewed software and hardware management, conducted an ocular visit to the Office's servers, and reviewed the disaster recovery plan. No reportable issues were noted.

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

The detailed assessment is presented below:

A. Programme Activities

The Country Programme Document (CPD) 2011-2015, which was extended to 31 December 2016, focused on three priority areas: (a) nutrition and food security; (b) socio-economic development; and (c) environment and climate change. The estimated programme delivery target for the programme cycle from 2011 to 2015 was \$43.3 million. This target was not met due to various external factors that resulted in revisions of budgets in recent years. The total programme expenses decreased progressively, from \$3.8 million in 2012 to \$2.1 million in 2014 and \$1.4 million in 2015. The project expenses for the period from January to November 2016 amounted to \$2.8 million.

The progressive decrease in programme delivery was due to various challenges, such as the limited programmatic space that the Office was permitted to work in, financial and export restrictions and economic sanctions, as well as the Country's mandatory quarantine measures in response to the Ebola outbreak in November 2014. Further, the imposition of the sanctions as a result of resolution 2270 (2016) of the Security Council adopted in March 2016, resulted in the closure of banking channels during the majority of 2016. The unavailability of banking channels forced the Office to function in a "cash conservation mode" and to initiate contingency plans for possible limited operations due to cash flow suspension.

UNDP had not yet approved the new CPD for 2017 onwards. The Office indicated that the CPD 2011-2015 that had been initially extended up to 31 December 2016 is expected to be extended up to 31 December 2017.

The Office, in consultation with RBAP, commissioned a Strategic Review Mission to make recommendations for improving the effectiveness of the Country Programme and Office efficiency and its long-term sustainability. The review was undertaken in May 2015 and the report issued in July 2015 outlined the key constraints and challenges affecting the Office's operations. The Strategic Review made short- and long-term recommendations for the Office and RBAP. The Office and RBAP indicated that they had considered the recommendations, which were practical and relevant, and had taken actions to implement them.

The audit did not identify any reportable issues in this area.

B. Operations

1. Procurement

The 'UNDP Programme and Operations Policies and Procedures' mandate the rational use of resources to respond effectively to the needs of programmes and operations by ensuring the timely availability of high quality goods and services. The Office is also required to comply with the United Nations Security Council sanctions imposed on the Country, which include a list of equipment and supplies that can be used for dual use or military purposes.

RBAP, in consultation with the Office and the Procurement Services Unit, had decided to obtain clearance from the Security Council Sanctions Committee, established pursuant to resolution 1718 (2006), to mitigate risks from sanctions, and the clearance only refers to sensitive items.

However, seeking clearance for procurement items delayed the procurement process, as the Sanctions Committee needed to refer the procurement list to the panel of experts for review, as discussed below:

- Given the risks involved, the Office had taken additional precautions to seek approval for items it intended to procure for three development projects valued at \$2.3 million to the Sanctions Committee.
- In September 2015, the Office through RBAP contracted an individual consultant to vet items that the Office planned to procure for three development projects against the United Nations Security Council sanctions list. Subsequently, upon consultation with the Procurement Services Unit, the procurement list was submitted to the Sanctions Committee in December 2015.
- In June 2016, the Sanctions Committee wrote back to UNDP seeking confirmation as to whether these items were in compliance with the new resolution 2270 (2016) adopted in March 2016. After internal consultations, a revised procurement list was provided to the Sanctions Committee in September 2016.
- The Sanctions Committee, in October 2016, stated that the items in the resubmitted procurement list did not contravene the applicable sanctions regime. The procurement of these items was in progress as of the date of audit.

Realizing the significant amount of time to obtain confirmation from the Sanctions Committee, the Office and RBAP adopted a revised approach for the procurement of items required for the emergency response to the floods in the northern part of the Country in August 2016. The Office and RBAP provided a procurement list (mainly comprising corrugated galvanized iron sheets) to the consultant for review. After the consultant confirmed that the list did not contravene the United Nations Security Council sanctions list, the Office proceeded to initiate the procurement of items through the Procurement Services Unit. Simultaneously, the Office, through the Procurement Services Unit, submitted the procurement list to the Sanctions Committee for information and provided them an opportunity to comment if necessary.

Protracted procurement processes, because of the nature of the market and its restrictions upon the Country, may have an adverse impact on programme implementation and progress.

The Office's management indicated they had already communicated with RBAP. For future procurements, when there are doubts about whether procurement items contravene applicable United Nations sanctions regimes, they will submit the procurement list to the Sanctions Committee for clearance, through the Procurement Services Unit.

For items that are clearly not included in the sanctions regime, RBAP will request the contracted consultant to vet these items against the sanctions list. RBAP will subsequently notify the Sanctions Committee that based on UNDP's review and assessment, the items to be procured do not contravene any applicable United Nations sanctions regime and the Committee is requested to express its disagreement should its opinion diverge from UNDP.

The audit did not identify any reportable issues in this area.

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.