

UNITED NATIONS DEVELOPMENT PROGRAMME
Office of Audit and Investigations



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AUDIT

OF

UNDP COUNTRY OFFICE

IN

UKRAINE

Report No. 1987
Issue Date: 16 August 2018

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Report on the Audit of UNDP Ukraine Executive Summary

The UNDP Office of Audit and Investigations (OAI) conducted an audit of UNDP Ukraine (the Office) from 29 May to 8 June 2018. 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 (leadership, corporate direction, corporate oversight and assurance, corporate external relations and partnership);
- (b) programme (quality assurance process, programme/project design and implementation, knowledge management);
- (c) operations (financial resources management, ICT and general administrative management, procurement, human resources management, and staff and premises security); and
- (d) United Nations leadership and coordination.

The audit covered the activities of the Office from 1 January 2017 to 31 March 2018. The Office recorded programme and management expenses of approximately \$179 million. Of which, \$115.9 million was incurred against the Procurement Support Services to the Ministry of Health of Ukraine Project (Project No. 90474) and directly implemented by the Office. The last audit of the Office was conducted by OAI in 2015.

The audit fieldwork also included the audit of the above-mentioned Project No. 90474. The project areas of governance and strategic management, programme management, procurement, asset management and financial management were covered by the project audit. The results of the project audit are covered under a separate OAI report (Report No. 1988, issued on 16 August 2018).

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 “The assessed governance arrangements, risk management practices and controls were adequately established and functioning well. Issues identified by the audit, if any, are unlikely to affect the achievement of the objectives of the audited entity/area.”

Good practices

Operations/Paperless office initiative: The Office initiated the implementation of a “green office concept” in 2016 and developed a Policy on Paperless Office. The Policy included transitioning towards paperless working, performing daily tasks electronically and making use of systems to support electronic processing, storage and retrieval, signing and sharing/circulation.

Human resources/Work-life balance: The Office and the staff association had been active in promoting the work-life balance of staff. For example, the Office ensured that meetings were organized, and emails were answered only during office hours.

Key recommendations: Total = 3, high priority = 0

The audit did not result in any high (critical) priority recommendations. There are three medium (important) priority recommendations, which means "Action is required to ensure that UNDP is not exposed to risks. Failure to take action could result in negative consequences for UNDP." These recommendations include actions to address weaknesses in programme, operations, and United Nations leadership and coordination.

The three recommendations aim to ensure the following: (a) achievement of the organization's strategic objectives (Recommendation 1); and (b) compliance with legislative mandates, regulations and rules, policies and procedures (Recommendations 2 and 3).

Implementation status of previous OAI audit recommendations: Report No. 1493, 18 December 2015.

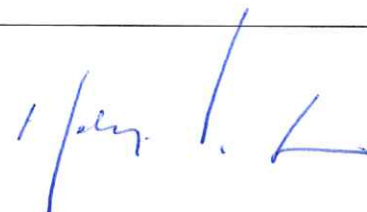
Total recommendations: 7

Implemented: 7

Management comments and action plan

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

Low risk issues (not included in this report) have been discussed directly with management and actions have been initiated to address them.

A handwritten signature in blue ink, appearing to read 'H. Osttveiten', is positioned above the printed name and title.

Helge S. Osttveiten
Director
Office of Audit and Investigations

I. About the Office

The Office, located in Kyiv, Ukraine has five field offices located in the Kharkiv, Kramatorsk, Severodonetsk, Donetsk and Luhansk regions. At the time of the audit, the Office had 55 staff members, 160 service contract holders, and 14 United Nations Volunteers. The Office's programme was focused on the following areas: inclusive and effective democratic governance, inclusive and gender responsive sustainable development, and recovery and peacebuilding in conflict-affected areas.

II. Good practices

OAI identified good practices, as follows:

Operations/Paperless office initiative: The Office initiated the implementation of a "green office concept" in 2016 and developed a Policy on Paperless Office. The Policy included transitioning towards paperless office work, performing daily tasks electronically and making use of systems to support electronic processing, storage and retrieval, signing and sharing/circulation of documents. The paperless policy reduced time needed for processing signatures on contracts and agreements from two working days in 2017 to 0.5 day in 2018. The utilization of printing paper in 2018 has decreased by 1.6 times when compared to 2017. Introduction of electronic signature (DocuSign), as part of the paperless office, enhanced assurance of document integrity.

Human resources/Work-life balance: The Office and the Staff Association had been active in promoting the work-life balance of staff. For example, the Office ensured that meetings were organized, and emails were answered only during office hours.

III. Audit results

Satisfactory performance was noted in the following areas:

- (a) Governance/Leadership. There was an adequate organizational structure, and a delegation of authority and implementation of an action plan to follow up on the results of the Global Staff Survey (GSS) were established.
- (b) ICT/General administrative management. ICT systems managed by the Office including hardware, software and security systems were operating effectively. General administration controls were well established and functioning adequately. The management of assets was found to be in line with UNDP policies and procedures.
- (c) Human resources. Adequate and effective controls were in place for recruitment, separations, learning processes as well as other human resources activities.
- (d) Procurement. Management had established adequate risk management, compliance, and control functions related to the procurement process.
- (e) Staff and premises security. The Office was compliant with the Minimum Operating Security Standards.

OAI made three recommendations ranked medium (important) priority.

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

Medium priority recommendations:

- (a) Strengthen programme management (Recommendation 1).
- (b) Strengthen the management of grants (Recommendation 2).
- (c) Enhance implementation of the United Nations Partnership Framework (Recommendation 3).

The detailed assessment is presented below, per audit area:

A. Programme

1. Project design and implementation

Issue 1 Strategy for transition toward national implementation not developed

Capacity development enables national institutions to better plan, manage and deliver on national development priorities, while ensuring strong national ownership of development plans and resource management.

At the time of the audit all 21 projects were being implemented through the direct implementation modality. Throughout the audit period, the Office had been operating under “fast track” procedures, which allowed for direct implementation as the default modality for all projects. However, the fast track procedures expired in April 2018, and capacity assessments had not been completed on the corresponding government counterparts of the sampled projects to identify capacity gaps and corresponding areas for support.

The Country Programme Document stipulates that during 2018-2022, the programme would transition from direct implementation to national implementation. The Office explained that due to continuing political instability, corruption, risk, and frequent changes in government leadership, it continued to use direct implementation. This coupled with the upcoming elections created a challenge in moving to national implementation in 2018.

A strategy had yet to be developed on how the programme would transition towards national implementation, although the Office confirmed the possibility of moving towards national implementation with certain government ministries. In addition, there were plans to establish a procurement agency within the relevant government ministry to support the procurement of health products.

Without a gradual transition towards national implementation to support capacity development, long-term programme results may not be achieved.

Priority	Medium (Important)
Recommendation 1:	
The Office should strengthen programme management by:	
<ul style="list-style-type: none"> (a) assessing the capacity of the designated government counterpart during the project design phase to identify capacity gaps, and corresponding areas for support; (b) establishing the conditions that need to be in place to move towards national implementation of projects, and develop a corresponding transition plan; and (c) monitoring and reporting on the progress on the transition plan during the annual programme results review meetings with the national counterpart. 	
Management action plan:	
The Office will develop a strategy for graduate transition to national implementation. This will be developed and discussed in the framework of the HACT macro-assessment.	
Estimated completion date: June 2019	

Issue 2 Weaknesses in grants management

The 'UNDP Programme and Operations Policies and Procedures' provide guidance on Micro-Capital Grant Agreements for non-credit related activities and include a template to be used for these purposes. The agreements define responsibilities for the recipient institution including performance targets, reporting and monitoring obligations and the project budget of the recipient institution. Any amendments to the template should be approved by an independent mechanism, such as a Steering Committee.

During the audit, OAI reviewed five grant agreements valued \$2.8 million out of a total value of \$10.4 million. In three Micro-Capital Grant Agreements reviewed, OAI noted that the following standard clauses were omitted: (a) provision of the grantee to provide annual audited statements (two cases); (b) clause covering the purpose and use of assets supplied by UNDP to the recipient institution (two cases); and (c) the disbursement clause, in which the meeting of performance targets is linked to payments (one case). The Office was unclear as to the reasons for these omissions, but for the assets clause the Office stated it was removed because that specific grant did not foresee or include any assets transfer.

If standard clauses are not in place, the Office may not have sufficient legal protection in the event of any disputes with the recipient organization.

Priority	Medium (Important)
Recommendation 2:	
The Office should strengthen the management of grants by ensuring any changes made to standard agreements are approved by an independent mechanism such as a Steering Committee and, if needed, cleared by the Legal Office.	

Management action plan:

The Office will ensure that any changes to the standard Micro-Capital Grant Agreement are reviewed and approved by the Steering Committee. The Steering Committee will convene to approve such changes.

Estimated completion date: September 2018

B. Operations**1. Financial resource management****Issue 3** Accrued VAT amounts since 2015

UNDP, as a subsidiary organ of the United Nations, is exempt from direct taxes such as income tax, and is entitled to reimbursement of indirect taxes, such as sales tax and valued added tax (VAT), on important purchases. This is derived from the 'Convention on the Privileges and Immunities of the United Nations', adopted by the General Assembly in 1946 (General Convention), Sections 7 and 8, respectively.

While in some countries, governments have provided an outright exemption to indirect taxes, in most countries, business units may be required to pay taxes and subsequently seek reimbursement. Governments are required, under the General Convention, to provide a mode of reimbursement on important purchases. The policy of the United Nations, including UNDP, is that all purchases are "important", as they are recurring and necessary for UNDP to carry out its official activities. Offices should liaise with the relevant government ministry to ensure reimbursement.

The Office was required to pay VAT and claim reimbursement afterwards. Since February 2015, the Government stopped reimbursing the VAT claimed for certain goods and services and the Office was not aware of the reasons for rejecting the VAT refund. Furthermore, the items for which the VAT was not refunded had not been officially communicated by the Government and the application had not been consistent. As of 31 March 2018, the accrued balance of the VAT account was approximately \$0.95 million, and most of it composed of VAT amounts rejected and not reimbursed by the Government. During the audit period, the Office had also reversed \$0.54 million from the VAT account and charged this as project expenditures due to the need to clear non-refunded amounts before the closure of projects.

The audit team also noted that:

- The Office, along with other United Nations agencies, reached out to the Government in an effort to resolve the VAT issue. It also reached out to the UNDP Legal Office and the United Nations Office of Legal Affairs, which communicated with the Country's Permanent Representatives at the United Nations. However, as of the date of the audit, the VAT was still not fully recovered.
- Donors were informed and consulted on how to proceed with non-recovered VAT since there was uncertainty on the recovery of the accrued amounts.
- The Office was using a detailed tracking tool to control the non-refunded VAT amounts. The VAT issue was included in the Office's risk log.

- In December 2017, the Office requested approval from Treasury to record the VAT in any expenditure accounts until the VAT issue was resolved. The Office was advised to continue recording the VAT in the VAT account until 31 March 2018 while awaiting a conclusive written response from the Government, and to review this recommendation on 1 April 2018. Subsequent to the audit, the Office indicated that it would communicate with Treasury again to revisit this recommendation. The Office had requested a new meeting with the Government authorities, but no response had been obtained.

Not recovering the full VAT amounts from its transactions may weaken partnership management and put the Office at risk of having liabilities with donors and other stakeholders, thus negatively impacting the achievement of UNDP's mandate in the Country.

Comment

OAI acknowledged the continuous efforts made by the Office to solve this issue as well as the mitigation actions adopted. OAI also noted that the resolution on the VAT refund issue is not entirely under the control of the Office. Therefore, no recommendation is being made.

C. United Nations leadership and coordination

Issue 4 Weakness in the United Nations Partnership Framework

The United Nations Partnership Framework represents the common strategic partnership framework between the Government of and the United Nations System for the period of 2018-2022. It affirms the commitment of all partners in support of the Sustainable Development Agenda 2030 in areas that coincide with national development priorities.

The implementation of the United Nations Partnership Framework 2018-2022 (UNPF) stipulates that the United Nations Country Team and the Government will hold annual review meetings to assess the progress of UNPF implementation and make any required adjustments to achieve the specified outcomes. In addition, the standard legal clauses must be attached to the UNPF for it to serve as the legal agreement with the Government.

The following weaknesses were noted:

- (a) In 2017, an annual review with the Government of the UNPF (2012-2017) was not carried out, although an independent evaluation was completed in 2016 to assist in the development of the new UNPF. The Resident Coordinator Office confirmed that it would develop a United Nations Annual Results report for 2018, which would be shared and discussed with the Government in early 2019.
- (b) The UNPF (2018-2022) signed with the Government did not include the required legal clauses relating to a resource mobilization strategy and certain clauses regarding the commitments of the Government. The Office was following up with the United Nations Development Group to determine whether an amendment was needed to include the annexes, which had been omitted.

Failure to address weaknesses in UNPF implementation could negatively impact the achievement of development outcomes.

Priority	Medium (Important)
Recommendation 3: The Office should follow up with the Resident Coordinator Office to enhance implementation of the United Nations Partnership Framework by: <ul style="list-style-type: none"> (a) developing a United Nations Annual Results report to be shared and discussed with the Government on an annual basis; and (b) through consultation with the relevant United nations agencies and the United Nations Development Group, reaching an agreement on the inclusion of legal clauses covering resource mobilization and the commitment of the Government within the United Nations Partnership Framework. 	
Management action plan: <ul style="list-style-type: none"> (a) Under the guidance of Resident Coordinator Office, the United Nations Country Team will develop an Annual Results Report for the United Nations Partnership Framework, this will be presented to the Joint Government/United Nations Steering Committee following the closure of the calendar year. (b) A process has already been initiated to correct the legal clauses and a dialogue has been initiated with agencies to determine the most appropriate process. 	
Estimated completion date: February 2019	

Definitions of audit terms - ratings and priorities

A. AUDIT RATINGS

- **Satisfactory** The assessed governance arrangements, risk management practices and controls were adequately established and functioning well. Issues identified by the audit, if any, are unlikely to affect the achievement of the objectives of the audited entity/area.
- **Partially Satisfactory / Some Improvement Needed** The assessed governance arrangements, risk management practices and controls were generally established and functioning, but need some improvement. Issues identified by the audit do not significantly affect the achievement of the objectives of the audited entity/area.
- **Partially Satisfactory / Major Improvement Needed** The assessed governance arrangements, risk management practices and controls were established and functioning, but need major improvement. Issues identified by the audit could significantly affect the achievement of the objectives of the audited entity/area.
- **Unsatisfactory** The assessed governance arrangements, risk management practices and controls were either not adequately established or not functioning well. Issues identified by the audit could seriously compromise the achievement of the objectives of the audited entity/area.

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. Failure to take action could result in 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.