AUDIT

OF

UNDP COUNTRY OFFICE

IN

LAO PEOPLE’S DEMOCRATIC REPUBLIC

Report No. 2000
Issue Date: 13 December 2018
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Report on the Audit of UNDP Lao People’s Democratic Republic
Executive Summary

The UNDP Office of Audit and Investigations (OAI) conducted an audit of UNDP in Lao People’s Democratic Republic (the Office) from 22 October 2018 to 2 November 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 30 September 2018. The Office recorded programme and management expenses of approximately $24 million. The last audit of the Office was conducted by United Nations Board of Auditors in 2016.

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 partially satisfactory/some improvement needed, which means “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.” This rating was mainly due to the improper use of grant agreements.

Key recommendations: Total = 6, high priority = 1

The six recommendations aim to ensure the following:

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<thead>
<tr>
<th>Objectives</th>
<th>Recommendation No.</th>
<th>Priority Rating</th>
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<tbody>
<tr>
<td>Reliability and integrity of financial and operational information</td>
<td>3, 4</td>
<td>Medium</td>
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<tr>
<td>Effectiveness and efficiency of operations</td>
<td>5, 6</td>
<td>Medium</td>
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<tr>
<td>Compliance with legislative mandates, regulations and rules, policies and procedures</td>
<td>1</td>
<td>High</td>
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<tr>
<td></td>
<td>2</td>
<td>Medium</td>
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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:
Improper use of grant agreement (Issue 1)

In December 2017, the Office signed a memorandum of understanding jointly with the government entities, resulting in the transfer of $1.2 million in Global Environment Facility funding to the one government entity through project 94709. These funds were recorded as grants and expensed in Atlas instead of using the regular procedure of a cash advance through the Harmonized Approach to Cash Transfer modality. Funds that were directly expensed in 2017 had not been spent for implementation activities at the time of this audit, in November 2018. Also, at the time of disbursement, the Office had not conducted a micro-assessment on the beneficiary to determine its capacity. Lastly, a non-standard memorandum of understanding, which had not been cleared by the Legal Office, was used.

Recommendation: The Office should ensure the proper use of the grant agreement by: (a) following the procedure for a cash advance through the Harmonized Approach to Cash Transfer modality when transferring funds for project implementation; (b) obtaining clearance from the Legal Office when a non-standard memorandum of understanding is used; and (c) developing and implementing a clear plan for the utilization of the $1.2 million transferred to the government entity through project 94709 within a specified timeframe, including recovering any unused funds.

Management comments and action plan

The Resident Representative accepted all 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.

Helge S.
Osttveiten
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Helge S. Osttveiten
Director
Office of Audit and Investigations
1. About the Office

The Office, located in Vientiane, Lao People’s Democratic Republic (the Country), comprised of 7 international staff, 7 national officers, 12 General Service staff, 4 service contract holders and 4 United Nations Volunteers/Junior Professional Officers at the time of the audit. The programme portfolio was made up of 15 projects focusing on the following three main Country Programme Document outcomes: all women and men have increased opportunities for decent livelihoods and jobs; forests and other ecosystems are protected and enhanced, and people are less vulnerable to climate-related events and disasters; and institutions and policies at national and local levels support the delivery of quality services that better respond to people’s needs. The Office underwent a change management process in 2016, resulting in a structure that was deemed to be more efficient and fit for purpose.

2. Audit results

Satisfactory performance was noted in the following areas:

(a) **Governance.** The Office exercised proper oversight and appropriate risk management to steer towards achieving its intended objectives. Adequate control was noted in managing the Office.

(b) **Operations/Human resources.** The review of processes relating to recruitment, separation, and leave management indicated that controls were adequate and working effectively.

(c) **Operations/Information and communication technology.** The Office’s business continuity and disaster recovery plan had been tested satisfactorily.

(d) **Operations/Safety and security.** The review of the Office security plan, security risk assessment, security management team meeting minutes did not identify any reportable issues.

(e) **UN coordination and leadership.** The review indicated that adequate and effective controls were established.

OAI made one recommendation ranked high (critical) and five recommendations 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 recommendation:**

(a) Ensure the proper use of the grant agreement (Recommendation 1).

**Medium priority recommendations,** arranged according to significance:

(a) Enhance project implementation (Recommendation 2).

(b) Enhance the accuracy of charging direct project costs (Recommendation 3).

(c) Improve the management of nationally implemented project cash advances (Recommendation 4).

(d) Enhance controls over direct contracting (Recommendation 5).

(e) Review and renegotiate the UN House common services costs (Recommendation 6).

The detailed assessment is presented below, per audit area:
A. Programme

1. Project Design and Implementation

**Issue 1**  Improper use of grant agreement

The ‘UNDP Programme and Operations policies and Procedures’ require that individual grant recipient shall not exceed $150,000 per individual grant and $300,000 on a cumulative basis within the same programme period. Further, according to Harmonized Approach to Cash Transfers framework, any implementing partner or responsible party who is expected to receive cash transfers of more than $300,000 in a programme cycle, will require a micro-assessment by a qualified third-party service provider. The result of the micro-assessment will determine the applicable cash transfer modality (e.g. cash advance, direct payment, or reimbursement) to use. Cash advances are recorded against advance account 16005 in Atlas (enterprise resource planning system of UNDP).

The audit team reviewed processes, related policies and procedures and information based on a sample of six projects, representing 70 percent of expenditures for the audit period.

In December 2017, the Office signed a memorandum of understanding jointly with the government entities. The Office transferred $1.2 million from the Global Environment Facility to the one government entity through project 94709. However, funds were recorded as grants and expensed in Atlas instead of using the regular procedure of a cash advance through the Harmonized Approach to Cash Transfer modality. Funds that were directly expensed in 2017 had not been spent for implementation activities at the time of this audit in November 2018. Also, at the time of disbursement, the Office had not conducted a micro-assessment on the beneficiary to determine its capacity.

Further, the memorandum of understanding was non-standard as amendments had been made to the template. However, the Office had not submitted it to the Legal Office for review and approval as required.

There is a risk that the Office may face unnecessary financial liabilities and reputational damage by not obtaining clearance from the Legal Office on non-standard memorandums of understanding. There is also a risk that the Office may not secure additional funding should expected outputs not be achieved within the planned timeframes.

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<th>Priority</th>
<th>High (Critical)</th>
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**Recommendation 1:**

The Office should ensure the proper use of the grant agreement by:

(a) following the procedure for a cash advance through the Harmonized Approach to Cash Transfer modality when transferring funds for project implementation;
(b) obtaining clearance from the Legal Office when a non-standard memorandum of understanding is used; and
(c) developing and implementing a clear plan for the utilization of the $1.2 million transferred to the government entity through project 94709 within a specified timeframe, including recovering any unused funds.

**Management action plan:**

(a) The Office will ensure that fund transfers/nationally implemented project advances for project implementation will adhere to regular Harmonized Approach to Cash Transfer mechanisms.
(b) Non-standard agreements will be referred to the UNDP Legal Office even when using a previously cleared agreement.
(c) A plan for utilization and a timetable have been developed with the implementing partner and the Environment Protection Fund. Implementation will be closely monitored by the Office.

**Estimated completion date:** (a) 30 November 2019; (b) 31 July 2019; (c) 30 November 2019

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**Issue 2**  Weaknesses in project implementation

In accordance with the UNDP Programme and Operations Policies and Procedures, offices are required to adhere to relevant policies and procedures for the proper implementation and management of programmes and projects in order to achieve organizational objectives.

A review of the project management practices identified the following weaknesses:

(a) **Weak/ad hoc programme assurance monitoring**

According to the Office’s Harmonized Approach to Cash Transfers assurance plans for 2017 and 2018, programme monitoring, including field visits, are to be undertaken.

Based on the reports provided, the field visits were organized on an ad hoc basis and they were not considered as part of the Harmonized Approach to Cash Transfers programme assurance visits. Also, field visit reports did not specify the specific activities/outputs or indicators to be monitored. For example, project 94709 reported conducting monthly meetings with the implementing partners in Vientiane. However, field missions were carried out for project personnel to attend events such as ground-breakings or to attend the project steering committee meetings. Similarly, project 101607 conducted four field visits in 2017 and one in 2018, but only to accompany the donor delegations. Additionally, the field visit reports did not articulate any challenges encountered, and therefore no follow-up actions were identified.

When projects are not adequately monitored by the Office, issues affecting implementation may not be identified in a timely manner to allow for corrective actions.

(b) **Letters of Agreement not signed**

In accordance with national implementation guidelines, the implementing partner assumes full responsibility for the related outputs. However, UNDP, at the request of the government can implement activities on behalf of the government. In this instance, a standard Letter of Agreement for support to national implementation is signed by both parties, and clearly articulates the responsibilities and accountabilities for both parties.

All six projects reviewed were nationally implemented, with Country Office support provided by the Office. However, only three projects had Letters of Agreement signed and the Office indicated that these were signed only in 2018. For the remaining three projects, the Office explained that Letters of Agreement had been submitted to the government ministries for endorsement and were yet to be received. The Office did not establish the Letter of Agreement for Country Office support when the project documents were initially signed, as required.

In the absence of a signed Letter of Agreement for Country Office support, roles and responsibilities are not clearly defined, which may result in unclear accountabilities between the Office and government ministries.
Priority: Medium (Important)

Recommendation 2:
The Office should enhance project implementation by ensuring that:

(a) Harmonized Approach to Cash Transfers programme monitoring missions are undertaken according to the assurance plan, with clear monitoring objectives articulated, including what will be monitored, by whom, findings, challenges identified, and follow-up actions documented if any; and
(b) Letters of Agreement are signed for all existing and newly approved projects.

Management action plan:

(a) The project will be tasked to prepare the 2019 Harmonized Approach to Cash Transfers assurance plan and subsequent programme visit/spot check reports with all necessary information.
(b) The Office already took action to sign Letters of Agreement for almost all projects in the Country Office portfolio, with two still outstanding. In these two cases the draft agreements were shared with the implementing partners on 24 October 2018. Going forward, Letters of Agreement for Country Office support will be signed for all new projects at the time of signing the project document.

Estimated completion date:
(a) 31 July 2019
(b) 31 January 2019 for the two remaining ongoing projects.

B. Operations

1. Finance

Issue 3 Direct project costs not adequately supported

Direct project costs are organizational costs incurred in the implementation of a development activity or service provided by UNDP Country Offices and Headquarters units that can be directly traced and attributed to that development activity (projects and programmes) or service. Regardless of the methodology used in the implementation of Direct Project Costing, the underlying principle is that the apportionment of direct project costs should be transparent and consistent for costing purposes.

The Office based their Direct Project Costing implementation methodology on a combination of using the results of a workload study (for programme staff costs) and the application of the Universal Price List or Local Price List (for transactional costs of operations support services). The total direct project costs for 2017 and 2018 were $1.2 million and $0.8 million, respectively. However, the apportionment of programme staff costs as direct project costs was not supported by adequate and transparent information that could be used as a sound basis for such apportionment. Although the Office explained that the apportionment of programme staff costs was based on actual time/support spent by programme staff on projects, this was not supported by the workload study undertaken by the Office.

In the absence of an appropriate basis for the apportionment of costs, the resulting direct project costs may not be accurate, and representative of the actual time/effort spent on projects. Furthermore, the lack of a transparent process for Direct Project Costing may result in reputational risks for the Office.
**Priority** Medium (Important)

**Recommendation 3:**

The Office should enhance the accuracy of charging direct project costs to projects by:

(a) ensuring that the basis of apportionment of costs is justified and fully supported; and

(b) performing periodic assessments (at least quarterly) of the estimates conducted at the beginning of each year to ensure that the basis for charging direct project costs remains valid through each financial year.

**Management action plan:**

(a) The apportionment of costs as direct project costs starting in January 2019 will be done in line with the results of the 2018 workload survey, which is currently ongoing.

(b) The Office will undertake quarterly reconciliations to ensure that actual direct project costs are in line with the actual work performed on behalf of the respective projects.

**Estimated completion date:** (a) 28 February 2019; (b) 31 July 2019

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**Issue 4** Inadequate management of nationally implemented project cash advances

The UNDP Programme and Operations Policies and Procedures’ on direct cash transfers, such as cash advances to implementing partners under nationally implemented projects, and reimbursements state that funding requests should be based on Funding Authorization and Certificate of Expenditure (FACE) forms. The requests should include a copy of the bank statement showing the closing cash balance for the relevant quarter and, as necessary, include a reconciliation to the balance of cash funds available as shown in the FACE form. Similarly, the direct cash transfer modality involves UNDP advancing funds to an implementing partner, and the partner in turn reporting back on the expenditure.

In a sample of 25 nationally implemented project cash advances made to implementing partners, the audit team noted that none of the FACE forms used for the funding requests included copies of the relevant bank statements and reconciliations.

In a sample of 20 payment vouchers reviewed, the audit team noted seven instances where the Office made payments totalling $700,494 to implementing partners and recorded them as expenses. However, the supporting documents attached to these payments indicated that they were advances to the implementing partners.

When FACE forms are not reviewed in line with the bank statement, there is no assurance that the balance of funds as reported on the FACE forms matches with the bank balance. Similarly, advances made to implementing partners, when recorded as expenditures, may result in an overstatement of the actual delivery.

**Priority** Medium (Important)

**Recommendation 4:**

The Office should improve the management of nationally implemented project cash advances by ensuring that:
(a) FACE forms include copies of bank statements and reconciliation of funds, and
(b) advances made to implementing partners are recorded as such until a report of expenditures is received from the implementing partner.

Management action plan:

(a) The Office will work with its implementing partners to ensure that FACE forms are consistently submitted along with copies of bank statements showing the closing cash balance for the relevant quarter and, as necessary, a reconciliation of funds. Only complete forms will be accepted by the Country Office.
(b) All nationally implemented project cash advances are recorded as such until the settlement forms are received and approved. No new advance will be approved until 80 percent of the previous advance is settled.

Estimated completion date: 30 April 2019

2. Procurement

Issue 5  Direct contracting not properly justified

Direct contracting, also known as sole-source or single source procurement, is a procurement method that allows the award of a contract without competition. The ‘UNDP Programme and Operations Policies and Procedures’ provide that this method is used when it is not feasible to undertake a competitive bidding process, and when proper justifications exist. UNDP Financial Rule No. 121.05 specifies nine instances when direct contracting is justified, including the need for standardization, which refers to the compatibility and consistency with existing equipment, systems or technologies. Furthermore, the ‘UNDP Programme and Operations Policies and Procedures’ elaborate on when the application of the direct contracting procurement method is allowable under certain circumstances.

The audit team reviewed a sample of 26 procurement cases with a total value of $1.31 million. Of the 26 procurement cases, 11 were carried out through direct contracting, with a total value of $0.3 million. The audit team noted that 5 of the 11 procurement cases totalling $159,000 did not have sufficient justification for the use of direct contracting.

In all five cases, the Office indicated that the selected individual consultants had the relevant knowledge and experience and had previously worked with the projects. Therefore, the Office indicated that there was no competitive market for this purpose. However, this justification is only applicable to instances where there is a monopoly, nationally legislated pricing, or a requirement of proprietary services, which is often not the case for services such as the facilitation of training, meetings, workshops or report writing, as identified in these five cases.

The Office stated that in one out of the five cases, the individual consultant was recommended by the Bangkok Regional Hub. For two cases, time criticality necessitated the direct contracting.

Failure to comply with UNDP requirements on direct contracting may impact the Office’s reputation and may lead to financial losses.
Priority: Medium (Important)

**Recommendation 5:**

The Office should enhance controls over procurement by ensuring that direct contracting is undertaken only in accordance with the ‘UNDP Programme and Operations Policies and Procedures’.

**Management action plan:**

The Office will ensure that direct contracting is undertaken in accordance with the ‘UNDP Programme and Operations Policies and Procedures’.

**Estimated completion date:** 31 May 2019

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### 3. General Administration

**Issue 6: Weaknesses in common services cost management**

According to the ‘UNDP Programme Operations Policies and Procedures’, offices need to negotiate and agree with participating resident agencies on the estimated cost of common/shared services for the upcoming year.

During the audit period, the Office reduced its occupancy of the UN House from three floors to one floor after the Office’s restructuring exercise in 2017. However, the space used for calculating the rental costs and the Office’s operations and IT related costs increased. Specifically, the Office’s annual costs increased from $220,000 in 2017 to $240,000 in 2018.

The audit team noted that the corresponding increase in operations and IT related costs did not tally with the unit rates charged. The increased unit costs were supposed to be applicable to all agencies housed within the UN House. In comparison, one UN agency, where unit rates were expected to proportionately increase, had the same costs for operations and IT for both 2017 and 2018. This could indicate that the cost adjustment based on the revised rates were not applied to this UN agency. Its annual costs in 2017 and 2018 remained the same at $84,061.

The Office had not undertaken a review of UNDP’s common premises cost sharing structure after the occupancy change to ensure a reasonable and fair cost-sharing methodology was applied to all agencies occupying the UN House.

Subsequently, the Office stated that due to the closure of office space for one UN agency, the cost of the resulting vacant 20 square metres was erroneously added to UNDP’s cost when it should have been evenly distributed among the UN agencies occupying the UN House.

Failure to review and renegotiate the UN House common premises costs may result in the Office overpaying for its share of costs.
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<th>Priority</th>
<th>Medium (Important)</th>
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**Recommendation 6:**

The Office should review and renegotiate the UN House common premises costs with other resident UN agencies, taking into account the occupancy and per unit rates.

**Management action plan:**

Necessary adjustments will be made during the 2018 closure and in 2019.

**Estimated completion date:** 31 March 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**.