

**UNITED NATIONS DEVELOPMENT PROGRAMME**  
**Office of Audit and Investigations**



*Empowered lives.  
Resilient nations.*

**AUDIT**

**OF**

**UNDP COUNTRY OFFICE**

**IN**

**AZERBAIJAN**

**Report No. 2057**  
**Issue Date: 3 July 2019**

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## Report on the Audit of UNDP Azerbaijan Executive Summary

The UNDP Office of Audit and Investigations (OAI) conducted an audit of UNDP Azerbaijan (the Office) from 29 April to 10 May 2019. 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 2018 to 31 January 2019. The Office recorded programme and management expenses of approximately \$11.9 million. The last audit of the Office was conducted by OAI in 2013.

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 weaknesses within grant, financial and vendor management.

### Good practice

The Office established a Project Management Implementation Unit working on the implementation of two or more projects funded by the same or different donors at the same time. This strategy allowed the Office to benefit from the economy of scale and saving project management costs. For example, in a call for proposal for vocational education organized by a donor, the Office presented two proposals that shared the total management cost, including project staff cost. This way, the proposals became more economical and the project was awarded two out of the four grants advertised. Also, under the gender and youth portfolio, two project managers were covering four projects funded by different donors.

### 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.”

The three recommendations aim to ensure the following:

Objectives	Recommendation No.	Priority Rating
Reliability and integrity of financial and operational information	2, 3	Medium
Compliance with legislative mandates, regulations and rules, policies and procedures	1	Medium

### 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.



Helge  
Osttveiten  
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Helge S. Osttveiten  
Director  
Office of Audit and Investigations

## I. About the Office

The Office, located in Baku, Azerbaijan (the Country) was comprised of 12 staff members, 8 service contractors, 1 international United Nations Volunteer (UNV), and 5 interns at the time of the audit. The Office's Country Programme for 2016–2020 focused on three development areas: i) human capital development and inclusiveness; ii) enhanced institutional capacities for equitable development policy; and iii) improving environmental management and resilience to climate-induced hazards. These areas contributed to three out of the five outcomes of the 2016–2020 United Nations Azerbaijan Partnership Framework (UNAPF).

## II. Good practice

OAI identified a good practice, as follows:

### Programme/Project design and implementation

The Office established a Project Management Implementation Unit working on the implementation of two or more projects funded by the same or different donors at the same time. This strategy allowed the Office to benefit from the economy of scale and saving project management costs. For example, in a call for proposal for vocational education organized by a donor, the Office presented two proposals that shared the total management cost, including project staff cost. This way, the proposals became more economical and the project was awarded two out of the four grants advertised. Also, under the gender and youth portfolio, two project managers were covering four projects funded by different donors.

## III. Audit results

Satisfactory performance was noted in the following areas:

- (a) Governance. No reportable issues were identified in relation to organizational structure, delegation of authority, risk management, business continuity and financial sustainability. Adequate controls were established and functioning well.
- (b) ICT and general administration. The audit team reviewed the disaster recovery plan and business continuity plan and found that adequate controls were in place. Within the area of general administration, adequate controls were in place.
- (c) Human resources. Adequate and effective controls were in place for recruitment, separations, learning processes as well as other human resources activities.
- (d) Staff and premises security. Staff and premises security area management was found to be adequate and all security measures were found to be in place. No reportable issues were identified.
- (e) United Nations leadership and coordination. Adequate controls were established to manage and lead the United Nations coordination in the Country.

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**, arranged according to significance:

- (a) Strengthen controls within vendor management (Recommendation 3).
- (a) Improve grant management by using the correct legal instrument (Recommendation 1).
- (b) Improve financial management (Recommendation 2).

The detailed assessment is presented below, per audit area:

## A. Programme

### 1. Programme/Project design and implementation

#### Issue 1 Incorrect contracting modality when awarding low value grants

The 'UNDP Programme and Operations Policies and Procedures' prescribe that the legal instrument used by UNDP to provide low-value grants (those not exceeding \$150,000), when the grant recipient is a civil society or non-governmental organization, is the Low Value Grant agreement (former Micro Capital Grant Agreement).

One of the outcomes of a project included the design and implementation of a grant programme to support civil society organizations (CSO) with gender-sensitive Sustainable Development Goal (SDG) initiatives. In line with the project document and following a programmatic selection process, in December 2018, the Evaluation Committee recommended to fund nine CSOs for an approximate total amount of \$853,000 (equivalent to 719,998 euros). After consultation with the selected CSOs, 4 out of 9 of them opted to sign grant agreements; the remaining 5 signed procurement contracts under the modalities of individual contract and Reimbursable Loan Agreement. The CSOs were also registered in the Country as private companies. The procurement contracts amounted to approximately \$477,449 (equivalent to 403,013 euros).

The Office explained that it did not sign grant agreements because the national legislation required grants to be registered and approved by the national authorities, prior to being implemented. The registration process was not only lengthy and uncertain, but also restrictive as there were cases of NGOs not being able to register grants funded by other UN agencies. As a result, grantees were given the choice of selecting the contracting modality for their individual projects. The project implementation modality was cleared by the Regional Bureau. In addition, other development partners had been working with CSOs through individual contracts or Reimbursable Loan Agreements.

The Office was not able to provide the audit team with evidence that the CSOs has tried but failed in their attempts to register the grants and have them approved by national authorities. This was because grants that had not been granted an approval did not receive any communication from the Government.

By not using the correct legal instrument when engaging programmatic partners, the Office may be exposed to legal and reputational risks.

Priority	Medium (Important)
<b>Recommendation 1:</b>	
The Office should improve grant management by:	
<ul style="list-style-type: none"> <li>(a) using the correct legal instrument to engage civil society organizations in development activities; and</li> <li>(b) obtaining advice and clearance from the UNDP Legal Office prior to choosing and signing any other alternate contract modality for awarding grants.</li> </ul>	

**Management action plan:**

- (a) The Office will use the correct legal instrument to engage civil society organizations in development activities in line with regulations for the Selection of Responsible Parties and Grantees, effective 6 May 2018.
- (b) The Office will seek advice and clearance from the UNDP Legal Office prior to implementing any other alternate contract modality for awarding grants.

**Estimated completion date:** September 2019

**B. Operations**

**1. Financial resources management**

**Issue 2**      Weaknesses within financial management

The audit team found the following weaknesses while reviewing the financial management function:

- (a) Contracts signed with suppliers prior to project funds becoming available

According to UNDP financial rules and regulations, offices do not have authority to enter into commitments in the absence of available cash. The Atlas (enterprise resource planning system of UNDP) commitment control module helps to enforce this rule by ensuring that only those purchase orders and vouchers that are linked to available funds and pass a budget check can be finalized. Special circumstances may justify short-term deficits, and the head of office is responsible for defining a budget override policy approved by the UNDP Controller, outlining the circumstances under which budget overrides would be applicable. Where an override has been exercised, the responsibility of the head of office is to ensure that funds are received within 30 days, unless special conditions are agreed to and applied by the donor.

During the sample review of 21 payment vouchers, in two instances the Office signed contracts with the supplier valued at \$438,212 prior to all the funds becoming available. In addition, the Office did not maintain a record of the contracts that had been signed prior to donor funds becoming available.

The Office explained this decision was made in order to avoid delays in project implementation. In these instances, the purchase order was created in Atlas once the funds became available, which in one of the cases reviewed occurred after the services had been delivered.

This practice of signing contracts outside of the Atlas commitment control module without approved budget override requests creates legal and financial risks for UNDP.

- (b) Recording contract prepayments as expenditure

A prepayment is used when a supplier requires partial or full payment for goods or services prior to delivering them to UNDP. For one-off transactions, a prepaid voucher should be created if the time period between payment and full-service delivery extends over a quarter or year end.

Within the 21 payment vouchers sampled, two purchases orders included contracts with a prepayment element totalling \$263,800, which had been incorrectly recorded as expenditure. Management explained prepayments were expensed since the accrual accounting created additional administrative work for the Office.

This treatment is inconsistent with the International Public Sector Accounting Standards and can lead to an overstatement of reported expenditure in the financial year for the Office.

<b>Priority</b>	Medium (Important)
<b>Recommendation 2:</b>	
The Office should improve financial management by:	
<ul style="list-style-type: none"> <li>(a) preparing a budget override request in the event a contract/purchase order is agreed prior to the receipt of donor funding; and</li> <li>(b) recording prepayments in accordance with the International Public Sector Accounting Standards and expensing them once the goods and services have been received.</li> </ul>	
<b>Management action plan:</b>	
<ul style="list-style-type: none"> <li>(a) The Office will adhere to the budget override policy by requesting the approval of the Office of Financial Resources Management for override requirements exceeding 30 days, with the exception of the EU and trusted UNDP donors with a long-standing record of contributions to UNDP as stipulated by policies.</li> <li>(b) The Office will record all the advances by using the prepayments account only. Respective instructions and clarifications have been provided to the project staff during the working session on 3 June 2019. All prepayments will be recorded in accordance with policies and rules and regulations.</li> </ul>	
<b>Estimated completion date:</b> June 2019	

## 2. Procurement

### Issue 3 Due diligence on review of vendors submitting bids

The 'UNDP Programme and Operations Policies and Procedures' require that the staff entrusted with the responsibility to approve a vendor must ensure the vendor is authentic. For example, the Office should conduct background checks of vendors to ensure they are bona fide companies. This may include reference checking with other entities who have conducted business with the vendor, along with a physical inspection of the vendor's business premises, and verification of authenticity of legal, technical and financial documents.

During the pre-solicitation phase, staff should not use unnecessary restrictive specifications, statements of work or terms of reference that may discourage competition. In markets where there may be limited sources, structured market research should be documented during planning and as part of the procurement process. Furthermore, any interactions with suppliers and potential suppliers should be documented in the presence of more than one individual.

From the review of 18 procurement cases, the following observations were made in relation to the bid submissions:



- In nine procurement cases, there was limited vendor information available within the bid submission documents, such as company website address and address of premises.
- In six procurement cases, the online information relating to the company submitting the bids did not correspond to the products for which they were bidding.
- In three procurement cases, the bid specifications included a long list of specialized items, which may have required more time for vendors to prepare their bids. However, the bid submission deadlines were limited to between 7 and 12 days, resulting in only one or two qualified bids. The Office was unable to demonstrate whether market research had been completed to show a good understanding of the market and to justify the limited number of qualified bids.
- In one instance, the registration number provided by the vendor within the bid submission documents did not correspond to the company within the national tax registration website.
- In one case reviewed by the Regional Advisory Committee on Procurement (RACP), the review minutes highlighted that the Office had been in contact with a supplier to assist in defining the bid specifications, who then later submitted their own bid.

The Office explained that market research is usually carried out for high value procurement cases above \$150,000.

By not having sufficient information regarding the background of the vendor, there is an increased risk of contract obligations not being fulfilled and of irregularities within the procurement process.

<b>Priority</b>	Medium (Important)
<b>Recommendation 3:</b>  The Office should strengthen controls within vendor management by: <ul style="list-style-type: none"> <li>(a) conducting comprehensive research to identify established companies that will be contacted to bid for cases which may be below \$150,000 but still represent high procurement risks (e.g., highly specialized items etc.); and</li> <li>(b) exercising and documenting additional due diligence to confirm the relevant experience of the vendor in cases where limited information is available on the bid submission documents, or website information does not match the services for which the company is bidding.</li> </ul>	
<b>Management action plan:</b>  The Office will exercise additional vigilance by conducting market research and due diligence for highly-specialized procurement cases below \$150,000.  <b>Estimated completion date:</b> July 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.