UNITED NATIONS DEVELOPMENT PROGRAMME
Office of Audit and Investigations

AUDIT

OF

UNDP KYRGYZSTAN

GRANTS FROM THE GLOBAL FUND

Report No. 2058

Issue Date: 8 January 2020

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Executive Summary

The UNDP Office of Audit and Investigations (OAI), from 30 September to 11 October 2019, conducted an audit of two grants from the Global Fund (Output Nos. 101079 and 110810 [HIV/TB]) managed by UNDP Kyrgyzstan (the Office) as the Principal Recipient. 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, risk management, staffing and performance management, capacity development and transition strategy);

(b) programme management (project approval and implementation, monitoring and evaluation);

(c) Sub-recipient management (selection, assessment and contracting, financial and programmatic activities);

(d) procurement (quantification and forecasting, procurement of health products, quality assurance of health products, use of individual contractors, procurement of other goods and services), supply management (inventory, warehousing and distribution), and asset management; and

(e) financial management (revenue and accounts receivable, expenses, and reporting to the Global Fund)

The audit covered the Global Fund-related activities of the Office from 1 January 2018 to 30 June 2019. The Office recorded Global Fund-related expenses of approximately $10.3 million. The last audit of the Office's Global Fund-related activities was conducted by OAI 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's management of the Global Fund grants 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 inadequate capacity assessments of Sub-recipients, weaknesses with regard to the implementation of the quality control plan for health products, and inadequate management of inventory of health products.

Key recommendations: Total = **6**, high priority = **3**

Objectives	Recommendation No.	Priority Rating
Achievement of the organization's strategic objectives	1	Medium
Effectiveness and efficiency of operations	2, 4	Medium
	6	High
Compliance with legislative mandates, regulations and rules, policies and procedures	3, 5	High

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 recommendations are presented below:

Inadequate capacity assessments of Sub-recipients (Issue 3)	The Office had not conducted sufficient capacity assessments of the 13 government entities and 9 NGOs using the standard Sub-recipient Capacity Assessment Tool prior to contracting them. Recommendation: The Office should strengthen Sub-recipient capacity assessments and oversight by completing the assessments of Sub-recipients using the Capacity Assessment Tool and using the results to develop a capacity development plan.
Ineffective implementation of the quality control plan (Issue 5)	A review of the control testing activities disclosed that the quality control plan for 2019 had not been implemented. The plan required testing of products upon arrival which was not completed. Recommendation: The Office should strengthen the quality control process by ensuring the implementation of a quality control plan that is aligned to the procurement schedule and inventory monitoring, to enable testing of pharmaceutical products prior to usage.
Inadequate management of inventory of health products (Issue 6)	A review of inventory records noted that stocks for five TB pharmaceuticals had been fully depleted in the central warehouse as at 4 October 2019. Additionally, a review of the central warehouse distribution records in 2019 disclosed discrepancies for two of four sampled Sub-recipient reports provided by the Office in October 2019. Furthermore, an inspection of inventory in six Sub-recipient locations noted variances in 4 of 29 inventory items valued at $4,550. Stockout was also noted at one Needle Exchange Point (NEP) sampled by the audit team, which only had one health product (2 mL syringes) out of nine health products listed in its September 2019 report to the Office. Finally, 6 million alcohol tissues for use with needles in the central warehouse had not been distributed to the NEP. The Office advised that this was due to the delayed reporting by the NEP, which interrupted the continuous supply of health products to its beneficiaries. Recommendation: The Office should strengthen the inventory management and distribution system by establishing an effective mechanism for timely recording the delivery notes in the Sub-recipient's health products register and following up on reporting discrepancies and adjusting procurement plans based on usage requirements.

Implementation status of previous OAI audit recommendations: Report No. 1742, 26 January 2017.
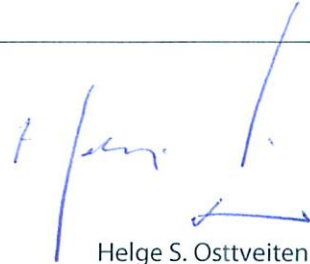   Total recommendations: 1
        Implemented: 1

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 into 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
Director
Office of Audit and Investigations

United Nations Development Programme
Office of Audit and Investigations

I.   Profile of Global Fund grants managed by UNDP Kyrgyzstan

Since 2011, UNDP has been the Principal Recipient of Global Fund grants in Kyrgyzstan (the Country).

Grant No.	Output No.	Description	Start Date	End Date	Budget (in $'000)	Funds Received as of **30 June 2019** (in $ '000)	Implementation Rate	Expenses as of **30 June 2019** (in $ '000)	Global Fund Rating at **30 June 2019**
1057	101079	Effective HIV and TB control project in Kyrgyzstan	1-Jan-18	30-Jun-18	3,510	3,509	98	3,422	A2
1682	110810	Effective HIV and TB control project in Kyrgyzstan	1-Jul-18	31-Dec-20	20,960	12,361	60	7,403	A2

II.   Audit results

Satisfactory performance was noted in the following areas:

(a) <u>Governance and strategic management.</u> Following the decrease in grant funding by 42 percent, and upon request from the Global Fund and the Country Coordinating Mechanism, the Office as Principal Recipient developed a new structure for the Project Management Unit considering the available budget and challenges of the grant implementation. All posts open to competition were finalized by the start of the implementation period of the new grant.

(b) <u>Financial management.</u> Financial management controls were found to be effectively implemented.

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

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

High priority recommendations, arranged according to significance:
(a) Strengthen Sub-recipient capacity assessments and oversight (Recommendation 3).
(b) Strengthen the quality control process (Recommendation 5).
(c) Strengthen the inventory management and distribution system (Recommendation 6).

Medium priority recommendations, arranged according to significance:
(a) Ensure adequate planning and supply of health products (Recommendation 4).
(b) Improve fund utilization (Recommendation 1).
(c) Enhance the data validation process (Recommendation 2).

The detailed assessment is presented below, per audit area:

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The detailed assessment is presented below, per audit area:

A.	**Programme management**

1.	**Project approval and implementation**

Issue 1   Low fund utilization

The 'UNDP-Global Fund Health Implementation Guidance Manual' provides that the Principal Recipient may undertake necessary budgetary adjustments to respond to programme realities. Adequate project monitoring allows for timely decision-making with regard to the utilization of grant funds.

A review of fund utilization during the first year of the grant implementation period disclosed the following barriers that prevented the Office from improving financial performance:

(a)   Challenges with absorption rates

The absorption rate for the first year from 1 July 2018 to 30 June 2019 was 56 and 79 percent for the Principal Recipient and Sub-recipients, respectively. The Office attributed the low absorption was attributed to: (a) delayed implementation of the TB database; (b) phased implementation of sputum specimen transportation system; (c) savings related to discontinued motivational payments to TB patients; (d) rescheduled procurement of health products from 2018 to 2019 due to existing quantities in the Country; (e) inefficient re-programming of unused funds; and (f) delays in programming the Matching Fund.[1]

(b)   Inefficient re-programming of unused funds

The Office was not able to re-programme a balance of $2,415,601 during the previous grant implementation period due to changes in the Global Fund's financial rules that delayed the approval process by up to two months. In addition, as of October 2019, a savings amount of approximately $800,000 from the new grant implementation period was yet to be re-programmed. Following the audit, in October 2019, the Office submitted a re-programming request for both amounts to the Global Fund after extensive consultations with national counterparts.

 (c)   Inefficient programming of the Matching Fund

The Matching Funds totalling $1.5 million from the Global Fund had not yet been fully programmed with one year remaining until the end of the grant. The absorption rates were 63 percent for July to December 2018, and 58 percent from July 2018 to September 2019. The Office indicated that this was due to delayed contracting of non-governmental organization (NGO) networks through the tendering process.

Low absorption rates and inefficient re-programming of unused funds could lead to missed opportunities to optimize the utilization of funds. This can negatively affect the grant performance and the next Global Fund allocation for the Country.

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[1] The new grant agreement from 1 July 2018 to 31 December 2020 included a budget of $1.5 million to catalyze investment towards activities to support removing human rights-related barriers to HIV services; this intervention is referred to as the "Matching Fund."

Priority	Medium (Important)

Recommendation 1:

The Office should improve fund utilization by:

(a) re-programming unused funds and submitting the request in a timely manner for approval by the Global Fund; and
(b) actively monitoring and taking necessary measures to optimize the absorption rate, including making efficient use of the Matching Fund.

Management action plan:

(a) The Office will finalize the budget revision in 2019 and obtain approval of the Global Fund by the end of quarter one of 2020.
(b) The Office will complete additional measures to optimize the absorption rate of the grant including the efficient use of the Matching Fund.

Estimated completion date: August 2020

2. Monitoring and evaluation

Issue 2 <u>Challenges with data validation with end users</u>

The grant agreement between UNDP and the Global Fund states that the Principal Recipient is responsible for the overall monitoring and evaluation of the grants and should carry out monitoring of Sub-recipient performance, including reporting. The Principal Recipient can be supported by the Local Fund Agent for the monitoring of the grants; however, this should be complementary.

A review of the monitoring and data validation processes disclosed that the Office had not yet established a verification mechanism with end users to provide assurance on the reliability of the data reported by Sub-recipients, including their utilization of health products. For instance, the review disclosed the following:

- Data validation for the programmatic and monitoring and evaluation visit reports completed by the Office for two Sub-recipients in the first half of 2019 was limited to reconciling Sub-recipients' supporting documentation with their databases. The Office did not consistently include direct validation with the beneficiaries for services and products received.

- The audit team sampled distribution records of the largest Sub-recipient consumer of HIV health-related products for the months of February, March and September 2019. Health-related products were distributed to outreach workers in fixed quantities. This was done without verifying if all previously distributed products were utilized.

The Office used the independent bi-annual verification completed by the Local Fund Agent, within the framework of the Global Fund grant agreement and the assurance provided by the Country Coordinating Mechanism, to monitor the Sub-recipient performance. However, these independent verifications should be complementary to the monitoring and evaluation undertaken by the Office.

Insufficient data validation increases the risk of inaccurate reporting on performance indicators. It may also hinder detection in the event that health products have been misappropriated.

Priority	Medium (Important)
Recommendation 2: The Office should enhance the data validation process by establishing an effective mechanism for direct verification by the Principal Recipient with end users of the data, including the use of health products reported by Sub-recipients.	
Management action plan: The Office will include an interview with a sample of clients and report on the services/health products provided during the implementation period for all first and second quarter monitoring and evaluation visits (programme) in 2020. **Estimated completion date:** October 2020	

B.   Sub-recipient management

1.   Selection, assessment and contracting

Issue 3   Inadequate capacity assessments of Sub-recipients

UNDP policies stipulate that Sub-recipients could be selected through: (a) direct programmatic engagement; (b) value for money analysis for NGOs; or (c) a tendering process. After the grant is signed, a capacity assessment should be completed for selected Sub-recipients prior to contracting them and, as necessary, a capacity development plan should be developed to bridge identified gaps.

The Office contracted 32 Sub-recipients to implement Global Fund grant activities from 1 July 2018 to 31 December 2020. This comprised of 13 government entities engaged directly, 9 NGOs selected through value for money analysis, and 10 other NGOs selected through a competitive process.

A review of the engagement of the Sub-recipients noted that the Office had not conducted a capacity assessment of the 13 government entities and 9 of 19 NGOs using the standard Sub-recipient Capacity Assessment Tool prior to contracting them.

This occurred due the following reasons:

- A micro-assessment of the 13 government entities was considered by the Office as sufficient; however, this assessment focused on a review of the financial capacity of the Sub-recipients while the Capacity Assessment Tool was a comprehensive review focusing on the programmatic capacity of the Sub-recipients including monitoring and evaluation, stock management and their comparative advantages.

- The Harmonized Approach to Cash Transfer (HACT) risk assessment of Sub-recipients focused on the level of cash advances, without considering the additional risk of managing health products. For instance, two Sub-recipients received health products and supplies amounting to $1.1 million each, while they only received cash advances amounting to $70,000 and $105,000.

- Sub-recipients selected through competitive processes were considered by the Office as low risk, and no further assessment was completed.

As a result, the Office did not develop a comprehensive capacity development plan for its Sub-recipients.

The absence of comprehensive capacity assessments and capacity development plans may lead to inadequate management of resources entrusted to the Sub-recipients, which could impact grant performance and the reputation of UNDP.

Priority	High (Critical)
Recommendation 3: The Office should strengthen Sub-recipient capacity assessments and oversight by completing the assessments of Sub-recipients using the Capacity Assessment Tool and using the results to develop a capacity development plan.	
Management action plan: (a) The Office will finalize the capacity assessments of its Sub-recipients using the Capacity Assessment Tool. (b) The Office will consider Sub-recipients who are managing a high volume of health products for inclusion in the FY 2019 Sub-recipient audit plan. **Estimated completion date:** June 2020	

C. Procurement

1. Procurement of health products

Issue 4 <u>Inadequate planning and monitoring of supply of health products</u>

The 'UNDP-Global Fund Health Implementation Guidance Manual' requires offices to procure health products through established Service Level Agreements with United Nations agencies and/or Long Term Agreements (LTAs) with manufacturers and suppliers. In the event that the pharmaceutical products required from the United Nations agencies cannot be supplied in a timely manner, the offices must request clearance from the Global Fund Health Implementation Support Team to approach commercial LTA holders.

A review of the implementation of the Health Procurement Action Plan that included a visit to a Needle Exchange Point (NEP) in Bishkek noted that the Office procured health products through a Service Level Agreement and LTAs. The Health Procurement Action Plan factored a lead time of 180 days for delivery. However, the mid-term review of the Health Procurement Action Plan indicated that only 28 of 115 purchases, or 24 percent, had met the delivery targets. Procurement for the remaining 87 purchases was delayed by 62 to 244

days, impacting the planned delivery of 32 HIV and 56 TB products by 56 to 300 days, thereby affecting the replenishment of health products (refer to issue 6).

These issues occurred because the Health Procurement Action Plan had not yet been adjusted to reflect procurement and delivery delays or the staggered shipments requested by the National Programme based on their supply plans. The Office acknowledged the importance of updating the lead times in the Health Procurement Action Plan.

Further, where excessive delays were encountered, alternative sourcing from commercial LTAs was not considered in a timely manner. For instance, an order placed with UNICEF in September 2018 for essential medication with expected delivery in March 2019 was received seven months later in October 2019. As the Country's buffer stock was depleted, the Office, in June 2019, initiated another purchase of a smaller quantity through a commercial LTA to address this issue; however, this shipment was not received until after the audit.

Inadequate planning and monitoring of the supply of health products may prevent the Office from effectively addressing supply chain requirements, which could impact the ability to reach beneficiaries in a timely manner.

Priority	Medium (Important)
Recommendation 4: The Office should ensure adequate planning and supply of health products by updating the Health Procurement Action Plan in a timely manner to reflect changes in lead times and actual delivery times.	
Management action plan: The Office will update the Health Procurement Action Plan and the Smart Sheet to reflect changes in lead times and the actual delivery times for health products. **Estimated completion date:** March 2020	

2. Quality assurance of health products

Issue 5   Ineffective implementation of the quality control plan

The 'UNDP-Global Fund Health Implementation Guidance Manual' and the Global Fund Quality Assurance Policy for pharmaceutical products require preparation of an annual sampling plan for quality control testing that is based on the annual procurement plan. Sampling is recommended upon arrival and in the supply chain.

A review of the control testing activities disclosed that the quality control plan for 2019 had not been implemented. The plan required testing of two products upon arrival and two within the supply chain. However, both selected samples delivered in April and July 2019 valued at $66,710 were not tested upon arrival as planned. One of these products valued at $2,405 was distributed directly to the Sub-recipients before testing.

Further, one of the two supply chain products sampled for testing only had a stock of 437 capsules, which would be likely to be consumed prior to the completion of the quality control testing (estimated to take three months).

The above-mentioned issues occurred because quality control tests were conducted annually during the last quarter of the year and were not aligned to the procurement calendar.

Without an effective quality control plan in place, there is a risk that products will be consumed prior to testing being completed.

Priority	High (Critical)
Recommendation 5: The Office should strengthen the quality control process by ensuring the implementation of a quality control plan that is aligned to the procurement schedule and inventory monitoring, to enable testing of pharmaceutical products prior to usage.	
Management action plan: The Office will complete the sampling of health products in accordance with the quality control plan and submit annual progress reports to the UNDP Global Fund Health Implementation Support Team. **Estimated completion date:** June 2020	

3. Supply management (inventory, warehousing and distribution)

Issue 6   Inadequate management of inventory of health products

According to the 'UNDP-Global Fund Health Implementation Guidance Manual' the Office is accountable for inventory until it reaches the final beneficiaries. The Office, in line with the national policy, should establish minimum stock levels to trigger re-orders, factoring procurement lead times and national buffer stock requirements.

The audit team physically verified that a sample of 37 of 80 health products, representing 46 percent in the central warehouse, were properly stored and recorded and had adequate shelf life. However, a review of inventory records noted that stocks for five TB pharmaceuticals had been fully depleted in the central warehouse as at 4 October 2019. The Office considered that the Country's stock for two of the TB pharmaceuticals was sufficient.

A review of the central warehouse distribution records in 2019 disclosed discrepancies for two of four sampled Sub-recipient reports provided by the Office in October 2019. One NGO in Chui Oblast incorrectly reported receipt of 565,792 units of condoms and syringes in May 2019 valued at $55,098 that had not been distributed by the central warehouse. The same Sub-recipient did not indicate receipt of the same products from the central warehouse in April 2019 totalling 243,632 units valued at $39,000 and 169,300 units valued at $4,205 in September 2019.

- An inspection of inventory in six Sub-recipient locations noted variances in 4 of 29 inventory items valued at $4,550. The variances were due to a delay in the recording of vouchers in the distribution register. Stockout was also noted at one NEP sampled by the audit team, which only had one health product (2 mL syringes) out of nine health products listed in its September 2019 report to the Office.

- In addition, it was observed that 6 million alcohol tissues for use with needles in the central warehouse had not been distributed to the NEP. The Office advised that this was due to the delayed reporting by the NEP, which interrupted the continuous supply of health products to its beneficiaries. The Office did not approve distribution as it had not received the reports from the NEPs for the previous period.

Further, the audit team observed that one product (1 mL syringes) was stocked in high quantities by the National Programme, totalling 65,300 units. The National Programme attributed this to a decline in the target group over the years; however, these trends had not been adequately factored into the procurement plans as the Office had yet to review this.

Inadequate inventory management could impact the distribution of health products to beneficiaries and increases the risk of pilferage. This could undermine the achievement of the grant objectives and create reputational risks for the organization.

Priority	High (Critical)
Recommendation 6: The Office should strengthen the inventory management and distribution system by establishing an effective mechanism for timely recording the delivery notes in the Sub-recipient's health products register and following up on reporting discrepancies and adjusting procurement plans based on usage requirements.	
Management action plan: The Office will communicate to the Sub-recipients the process and timeline for recording the delivery notes in the distribution registers for health products. The Office will notify the Sub-recipients on the requirement of recording the delivery notes in the Sub-recipient's health products distribution registers within 10 working days of receipt and monitor compliance on a quarterly basis. **Estimated completion date:** June 2020	

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 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.