UNITED NATIONS DEVELOPMENT PROGRAMME
Office of Audit and Investigations

AUDIT

OF

UNDP OFFICE

IN

KOSOVO[1]

Report No. 2325
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Report on the Audit of UNDP Kosovo[1]
Executive Summary

The UNDP Office of Audit and Investigations (OAI) conducted an audit of UNDP Kosovo (the Office) from 5 to 19 July 2021. 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
(b) Development activities
(c) Operations – procurement, finance, human resources, administrative services, information communication and technology (ICT)

The audit covered the activities of the Office from 1 January 2020 to 30 April 2021. The Office recorded programme and management expenses of approximately $12 million. The last audit of the Office was conducted by OAI in 2017.

The audit was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*. Due to the COVID-19 pandemic, the audit was conducted remotely. Scope limitations due to the nature of the remote audit related to the following activities:

(a) A review of original supporting documentation could not be carried out, and therefore the audit team relied on scanned copies of documents provided by the Office for all audit areas reviewed.
(b) Meetings with Office staff and personnel were carried out virtually, which limited the audit team's understanding of the Office's working environment.
(c) Project visits (location, site visits, meeting with counterparts/beneficiaries) were not conducted.
(d) A physical verification of assets was not performed.
(e) Safe and petty cash contents were not verified.
(f) The information communication and technology area was not reviewed on-site.

Overall audit rating

OAI assessed the Office's performance as **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 management expenditures being above corporate target levels.

Key recommendations: Total = **2**, high priority = **1**

The two recommendations aim to ensure the following: (a) achievement of the organization's strategic objectives (Recommendation 1, high priority); and (b) reliability and integrity of financial and operational information (Recommendation 2, medium priority).

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:

[1] References to Kosovo shall be understood to be in the context of Security Council resolution 1244 (1999), in which Kosovo is not referred to as a country.

Management expenditures above corporate target levels (Issue 1)	The Office's management efficiency ratios (MERs) were 10 percent and 14.4 percent in 2019 and 2020, respectively, which were higher than the corporate targets and the average rates for the Regional Bureau for Europe and the Commonwealth of Independent States (6.6 percent and 6.4 percent, respectively). The Office's low delivery and insufficiently generated income to meet its management costs were factors contributing to its high MERs. The Office's efforts to improve the MER included an increase of the programme budget and improved revenue collection. Recommendation: The Office should improve management efficiency by: (a) establishing, with the support of the Regional Bureau, measures for a gradual reduction of the management efficiency ratio backed by financial analysis; (b) optimizing the use of available resources by establishing higher but reasonable delivery targets considering the operating environment; and (c) improving the implementation of Direct Project Cost and revenue collection targets.

Implementation status of previous OAI audit recommendations: Report No. 1899, 9 January 2018.
Total recommendations: 2
Implemented: 2

Management comments and action plan

The Resident Representative accepted the two 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.

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Helge S. Osttveiten
Director
Office of Audit and Investigations

I. About the Office

The United Nations, including UNDP, is present in Kosovo on the basis of the United Nations Security Council resolution 1244, which provides the mandate for its operations. The Office is located in Pristina, Kosovo. Its programme is included in the 2016–2020 country programme document for the UNDP Country Office in Serbia and covers the following three development priorities:

a) Good governance and rule of law;
b) Inclusive and sustainable growth; and
c) Resilience and environmental sustainability.

During the period from January 2020 to April 2021, the Office spent $10.4 million, a decrease by 9 percent compared to the previous period.

The largest development projects in terms of expenses during the period covered by the audit were:

Title	Expenditure Jan.–Dec. 2020 $million	Expenditure Jan.– Apr 2021 $million
Rapid Response to COVID-19	$2.91	$0.06
Active Labour Market Programme	$1.18	$0.39
Emergency and early recovery support	$0.65	$ -
Kosovo Safety and Security Programme	$0.55	$0.20
Institutional Strengthening of Anti-corruption public institutions	$0.58	$0.30
Total	**$5.87**	**$0.95**

The largest sources of funding of the Office's development activities for the period covered by the audit were:

Donor	Funding for the period $million
European Union	$8.99
Switzerland	$3.05
Sweden	$2.82
Kosovo (As per UNSCR 1244)	$2.56
Luxembourg	$1.19
Total	**18.61**

II. Audit results

Satisfactory performance was noted in the following areas:

(a) Development activities. The audit team reviewed programme and project management and found that controls were functioning as designed. Because of the special status of Kosovo, a formal Programme Steering Committee could not be set up; instead, continuous dialogue with Kosovo institutions and key partners was held. Project boards were established to have an avenue for strategic dialogues and decision-making.

(b) Procurement. Controls over procurement processes were adequately established and operating. The Office took actions to implement minor improvements noted during the audit.

(c) Administrative services. The audit team reviewed the general administration processes as well as asset and vehicle management and noted that adequate controls were established and functioning.

(d) Human resources. The audit team reviewed human resources processes and noted that adequate controls were established and functioning.

OAI made one recommendation ranked high (critical) and one recommendation 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) Improve management efficiency ratio (Recommendation 1).

Medium priority recommendation:
(a) Strengthen payment processing and vendor management (Recommendation 2).

The detailed assessment is presented below, per audit area:

A. Governance

1. Data analytics and performance indicators

Issue 1 Management expenditures above corporate target levels

The Integrated Results and Resources Framework (IRRF) translates the 2018–2021 Strategic Plan into a set of development and organizational indicators that assess UNDP's organizational performance and monitor the delivery of its mandate and vision. One indicator of the efficient management services to support programme delivery was established as the management efficiency ratio (MER). The MER aims at measuring the overall operational efficiency of UNDP offices by comparing the total management expenditures (resources spent on management activities) to the total expenditures incurred for all UNDP activities. The corporate targets of MER were set at 7.65 percent, 7.50 percent and 7.40 percent for 2019, 2020 and 2021, respectively.

The Office's MERs were 10 percent and 14.4 percent in 2019 and 2020, respectively, which were higher than the corporate targets and the average rates for the Regional Bureau for Europe and the Commonwealth of Independent States (6.6 percent and 6.4 percent, respectively). As of 30 June 2021, the Office's ratio was 15.8 percent compared to 5.27 percent for the Regional Bureau's average, and 6.6 percent for the corporate target for 2021.

The Office's low delivery and insufficiently generated income to meet its management costs were factors contributing to its high MERs. The Office had set low annual delivery targets compared to its available resources. For example, in 2019 and 2020, the available resources were $14.5 million and $ 15.8 million, respectively, while the delivery targets were $8.34 million (57.5 percent of available resources) and $8.61 million (54.5 percent of available resources), respectively. The delivery targets were set low based on the Office's delivery capacity and delivery history. The Office explained that the context in which it operates as well as the absence of a Standard Basic Assistance Agreement reduced the scope for certain regular funding mechanisms, such as the Global Environmental Facility or the Green Climate Fund.
The Office's efforts to improve the MER included an increase of the programme budget to $12 million in 2021 that would increase the Office's total expenditures (MER denominator) and an improved revenue collection with a 20 percent increase of Direct Project Costing that would reduce management expenditures (MER numerator).

By not making optimal use of available resources and by not optimizing revenue collection, the Office may not achieve efficient management services to support programme delivery, which could further impact donor trust.

Priority	High (Critical)
Recommendation 1: The Office should improve management efficiency ratio by: (a) establishing, with the support of the Regional Bureau, measures for a gradual reduction of the management efficiency ratio backed by financial analysis; (b) optimizing the use of available resources by establishing higher but reasonable delivery targets considering the operating environment; and (c) improving the implementation of Direct Project Costing considering comprehensive workload study and revenue collection targets.	
Management action plan: The Office and the Regional Bureau acknowledged and recognized the observation as a premise for the context in which the Office operates. Maintaining a strong and vibrant UNDP presence in Kosovo is of political and strategic importance and the Bureau is ready to continue supporting the Office by absorbing the above-average management efficiency ratio while the Office continues to strengthen its Direct Project Costing recovery, resource mobilization and delivery. **Estimated completion date:** December 2021	

B. Operations

1. Finance

Issue 2 Weaknesses in financial management

According to the 'UNDP Programme and Operations Policies and Procedures' a prepayment is used when a supplier requires partial or full payment for goods or services prior to the delivery of goods or services. Prepayments are recorded in the asset account 16065 (prepaid voucher modality). As the goods or services are provided, the prepaid asset balance must be reduced, and an expense recorded for the amount of goods or services received by UNDP. UNDP policies also require that key supporting documents be obtained and verified prior to creating vendors in Atlas (enterprise resource planning system of UNDP), and that payments be processed according to the UNDP Financial Rule 125.11.

A review of the processing of 25 accounts payable vouchers totalling $1.5 million, equivalent to 22 percent of all payments processed during the audit period, disclosed the following:

- The prepayment modality had not been properly applied in four cases amounting to $236,000. In two of them, prepayments to vendors amounting to $75,000 were expensed in December 2020 directly while the goods and services were delivred six mointh later in June 2021. The Office explained that constraints to use the funds prior to the end of the project or year-end prevented the use of prepaid vouchers. As the transactions were not recorded to prepayment account 16065, they were not reflected in the year-end certification. In the remaining two cases, the Office incorrectly applied the prepaid balance of one contract valued at $131,330 against a second contract valued at $29,748 for the same supplier. This led to the overpayment of one contract and the underpayment of the other contract by $5,950.

- In 12 cases amounting to $11,500, the vouchers were ineffectively processed due to data entry errors or to avoid a negative performance rating in the finance monitoring dashboard. In eight of these cases amounting to $1,500, vouchers initially created for one vendor were subsequently modified and processed for a different vendor. The practise creates opportunity for creating and approving fraudelant transactions. In four other cases amounting to $10,000, the vouchers were paid more than 30 days after the receipt of the invoices. These occurred because the approving managers did not comply with the Internal Control Framework in the processing of payments prior to the end of the project to secure the funds, and due to incorrect invoice dates or delays by the supplier in delivering invoice to the Office.

- A total of 298 new vendors were created and approved in Atlas from 1 January 2020 to 30 June 2021. The supporting documentation of 4 out of 11 vendors randomly selected were either missing or incomplete. In addition, the vendor database included 13 cases of duplicate vendor data. Two other vendors were approved after 49 and 131 days after being created or updated in Atlas. This was due to delays in providing missing documentation and clarifications to the Global Shared Services Unit (GSSU).

Weaknesses in payment processing and vendor approval processes could lead to financial irregularities, which could impact the Office's objectives.

Priority Medium (Important)

Recommendation 2:

The Office should strengthen payment processing and vendor management by:

(a) processing and recording prepayments in accordance with UNDP policies and procedures;
(b) ensuring approving managers adhere to the Internal Control Framework requirements in processing payment, exercising thorough review of documents supporting payments and timely addressing payment exceptions; and
(c) obtaining and recording all relevant vendor information before processing them in Atlas, and monitoring and deactivating all duplicate data on regular basis.

Management action plan:

(a) The prepayment account is used and will be used – with no exceptions – in compliance with rules and regulations. The accounts payable and paycycle have been moved from the Office to GSSU as a result of clustering of services as of 10 May 2021. The Office will ensure effective processing of prepayment requests through GSSU by taking the responsibility of finalizing each prepayment request and ensuring that the prepayment account is used in compliance with financial rules.

(b) The accounts payable and paycycle have been clustered services for the Office since 10 May 2021 and project finance staff are obliged to comply with the mandatory review of supporting documents as per GSSU guidance. In addition, the Office will monitor closely any exception to the Integrated Financial Dashboard and will take prompt action to resolve these exceptions.

Estimated completion date: October 2021

Definitions of audit terms - ratings and priorities

A. AUDIT RATINGS

- **Fully 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.
- **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.