Internal Audit of the Democratic People's Republic of Korea Country Office

June 2015

Office of Internal Audit and Investigations (OIAI)
Report 2015/12

Summary

The Office of Internal Audit and Investigations (OIAI) has conducted an audit of the Democratic People's Republic of Korea (DPRK) Country Office. The audit covered governance, programme management, and operations support during the period from 1 November 2013 to 5 February 2015. The scope of the audit included a review of activities supported by the Global Fund to Fight Aids, Tuberculosis and Malaria (hereinafter Global Fund), in accordance with UNICEF and Global Fund's agreement that these activities be subject to an annual audit.

OIAI had conducted an audit of the DPRK in 2013 that covered the period September 2012 to October 2013. This audit had raised a number of observations relating to key work processes of the office in the areas of governance, programme management, and operations support. The current audit excluded areas covered in the 2013 audit report.

The 2011-2015 UNICEF country programme in DPRK has five programme components: Health (including Tuberculosis and Malaria); Nutrition and Care; Education; Water, Sanitation and Hygiene; and Advocacy and Knowledge Management. The Tuberculosis and Malaria programme of the country office is entirely funded by the Global Fund. UNICEF has been the principle recipient of Global Fund funds in DPRK since 2010. The approved funding ceiling for Global Fund was US$ 68.8 million, of which US$ 68.7 million had been received as of 30 November 2014. The country programme has a total budget of US$ 128.8 million for the five-year period (including the Global Fund contribution for that period). Of this, US$ 9.9 million is regular resources (RR) and US$ 118.8 million is other resources (OR). RR are core resources that are not earmarked for a specific purpose, and can be used by UNICEF wherever they are needed. OR are contributions that may have been made for a specific purpose such as a particular programme, strategic priority or emergency response, and may not always be used for other purposes without donor agreement. An office is expected to raise the bulk of the resources it needs for the country programme itself, as OR.

The UNICEF country office is based in Pyongyang, and has a total workforce of 16 approved international posts, two of which were vacant at the time of the audit. The UNICEF staff were supported by 32 personnel from the Government of the DPRK.

Action agreed following the audit

As a result of the audit, and in discussion with the audit team, the country office has decided to take a number of measures. None of these are being implemented as high priority—that is, concerning issues that require immediate management attention.

Conclusion

The audit concluded that, subject to implementation of all outstanding agreed actions (including those arising from the previous audit), the controls and processes over the DPRK office were generally established and functioning. The measures to address the issues raised are presented with each observation in the body of this report.

The country office, with support from the East Asia and the Pacific Regional Office (EAPRO), and OIAI will work together to monitor implementation of these measures.

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Objectives

The objective of the country office audit is to provide assurance as to whether there are adequate and effective controls, risk-management and governance processes over a number of key areas in the office. In addition to this assurance service, the audit report identifies, as appropriate, noteworthy practices that merit sharing with other UNICEF offices.

The audit observations are reported upon under three headings: governance, programme management and operations support. The introductory paragraphs that begin each of these sections explain what was covered in that particular area, and between them define the scope of the audit.

Audit Observations

1 Governance

In this area, the audit reviews the supervisory and regulatory processes that support the country programme. The scope of the audit in this area includes the following:

- **Supervisory** structures, including advisory teams and statutory committees.
- **Identification** of the country office's priorities and expected results and clear communication thereof to staff and the host country.
- **Staffing structure** and its alignment to the needs of the programme.
- **Performance measurement**, including establishment of standards and indicators to which management and staff are held accountable.
- **Delegation** of authorities and responsibilities to staff, including the provision of necessary guidance, holding staff accountable, and assessing their performance.
- **Risk management**: the office's approach to external and internal risks to achievement of its objectives.
- **Ethics**, including encouragement of ethical behaviour, staff awareness of UNICEF's ethical policies and zero tolerance of fraud, and procedures for reporting and investigating violations of those policies.

All the areas above were covered, except for supervisory structures and ethics, both of which were assessed as low risk. The audit also excluded the staffing structure because it was comprehensively addressed in the 2013 audit report. In auditing the above governance areas, OIAI also focused on the management of Global Fund-supported activities, in accordance with UNICEF and the Global Fund's agreement that these activities be subject to annual audits.

The audit found that controls were functioning well over a number of areas. The office regularly reviewed and updated its delegation of authority and ensured that there were no high-risk segregation-of-duty conflicts. During the period under review the office was unable to undertake normal regular cash replenishments because of international sanctions, which did not target humanitarian assistance but nevertheless affected the flow of funds into the country. The office had established adequate processes to prioritize its activities and manage cash flow requirements. However, the audit noted the following.

Risk management

Under UNICEF's Enterprise Risk Management (ERM) policy, offices should perform a Risk and Control Self-Assessment (RCSA). The RCSA is a structured and systematic process for the assessment of risk to an office's objectives and planned results, and the incorporation of action to manage those risks into workplans and work processes. The risks and their mitigation measures are recorded in a risk and control library.

Given the environment in which this office operates, a risk assessment would assist in increasing awareness on limitations, setting an acceptable risk appetite for programming and reducing barriers though proactive mitigating actions. The audit reviewed the office's risk and control library and noted the following.

Identification of risk: The office had a resource mobilization strategy. However, the country has major challenges in attracting donors. At the time of the audit, the report from inSight[1] showed significant funding gaps, particularly in the health (excluding Tuberculosis and Malaria), nutrition, education, and WASH programmes. The Regional Office supplemented the funding levels with thematic funds when available, but there were still gaps.

The office relied on a very few donors to fund the planned programme activities. The majority of funds that were available were from the Global Fund – which at the time of the audit accounted for 52 percent of OR grants allotment, with the next largest donor accounting for only 11 percent. Funds provided by the Global Fund were earmarked for specific aspects of the country programme whilst other high-priority areas relating to the situation of children remained underfunded.

The country office's October 2014 monitoring of OR showed that, for the period 2011-2015, the routine health programme was 20 percent funded, nutrition was about 48 percent funded and water and sanitation (WASH) 41 percent funded. Additionally, the Global Fund funding did not cover programme evaluations. This is despite evaluations being critical for determining relevance, effectiveness, efficiency, sustainability and contribution to equity, and assisting in generation of knowledge for major decisions that UNICEF and the partner must take. Despite this, although the office's risk assessment had identified the lack of donors, it did not clearly set out the impact of the lack of funding in key programme areas or any possible mitigating actions.

Mitigation of risk: In the risk assessment and action plan updated in 2014 by the country office, one of the high risks related to the "difficulty in demonstrating programme results due to lack of data"; however, this risk had no proposed action. The office did state that it was in the process of developing and implementing a monitoring and evaluation strategy to address this, but it was not in place at the time of the audit.

The audit also noted that although seven risks were categorized as high, the action plan did not indicate if any of them would be escalated to the Regional Office or other relevant divisions. A risk relating to cash replenishments, identified in December 2013, was not in the 2014 risk and control library or acknowledged in the 2014 annual management plan (AMP) as

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[1] inSight (sic) is the performance component in UNICEF's management system, VISION (Virtual Integrated System of Information). inSight streamlines programme and operations performance management, increases UNICEF staff access to priority performance information, and exchanges between country offices, regional offices and HQ divisions, as everyone sees the same data/information.

a risk to the achievement of the 2014 programme priorities. As a result the office had not set out what mitigating actions would be taken (though in actual fact it had escalated the issue up to the Regional Office and HQ and an impact analysis had been done).

Monitoring of risk: The latest ERM guidelines, issued in 2015, reiterates that all offices should continue to consider significant risks in preparing their AMPs, and report on measures taken to manage significant risks in their annual reports. This requires that a country office monitor the status of actions it has defined to manage significant risks, and assess/update its risk assessment for emerging and declining significant risks.

The guidelines suggest that this be done by including the risks and relevant actions plans in the AMP and involving the office management team in periodic monitoring. However, the audit noted that the Risk Management Action Plan the office had developed in 2013 had not been reviewed during the annual planning process or in any of the Country Management Team meetings until October 2014. Further, although the office had had a mid-term review in 2013, it did not report its significant risks in the ERM module as required by UNICEF 2013 instructions on ERM.

Agreed action 1 (medium priority): The office agrees to:

i. Ensure that the risk library is comprehensive, regularly updated, reviewed by the Country Management Team and recorded in inSight. The significant risks identified, and corresponding mitigating actions – including those associated with the levels and types of funding – will be clearly articulated in the Annual Management Plan, and in staff performance evaluations where relevant.
ii. Ensure that risks to the achievement of programme priorities identified in the Annual Management Plan have mitigation measures, and that their implementation is monitored regularly.
iii. Ensure a process to determine the risk mitigation actions that will be formally escalated to the Regional Office or risk owner whenever necessary.
iv. In consultation with the Regional Office, realistically assess other resources (OR) funding possibilities and make the necessary adjustments to the planned programme results.

Staff responsible for taking action: Representative, Deputy Representative, and Chief of Operations
Date by which action will be taken: December 2015

Staffing structure

The lack of a competitive local labour market makes it hard for the office to get the required technical skills in-country. The dearth of local technical skills has meant the internationally-recruited staff are effectively solely responsible for the planning, implementation and monitoring of the programmes. The seconded personnel assist with the monitoring visits, particularly in areas to which the internationally-recruited staff do not have access. This means the programme heads of section have to perform the major aspects of programming, as well as the administrative tasks and input of transactions in VISION, on their own. Moreover, when a section head goes on R&R (to which they are entitled at fixed periods), another section head has to act as Officer in Charge (OIC) on their behalf, adding yet more tasks to their portfolio. All of these stresses could have an adverse impact on the quality of work when technical expertise is spread thin.

The staffing constraints had been compounded by Government requirement that, due to Ebola, all people entering the country undergo a mandatory quarantine of 21 days in their accommodation – or if travelling from particular countries in Africa, in a Government facility. The Regional Office, country office and Division of Human Resources have been discussing how best to manage the impact of these measures on staff members, and their decisions may affect the level of programme activities that can be implemented in the country. In the meanwhile the office has put in place support measures, such as a buddy system where designated staff check on those under house quarantine, to try and reduce the stress.

Agreed action 2 (medium priority): The office agrees to, in collaboration with the Regional Office, undertake a specific review on the options for effective implementation of the programme given the technical staffing and operational limitations.

Staff responsible for taking action: Representative, Deputy Representative, Chief of Operations and Regional Chief of Operations/ HR
Date by which action will be taken: November 2015

Governance: Conclusion

Based on the audit work performed, OIA concluded that the controls and processes over governance, as defined above, were generally established and functioning during the period under audit.

2 Programme management

In this area, the audit reviews the management of the country programme – that is, the activities and interventions on behalf of children and women. The programme is owned primarily by the host Government. The scope of the audit in this area includes the following:

- **Resource mobilization and management**. This refers to all efforts to obtain resources for the implementation of the country programme, including fundraising and management of contributions.
- **Planning**. The use of adequate data in programme design, and clear definition of results to be achieved, which should be specific, measurable, achievable, realistic and timebound (SMART); planning resource needs; and forming and managing partnerships with Government, NGOs and other partners.
- **Support to implementation**. This covers provision of technical, material or financial inputs, whether to governments, implementing partners, communities or families. It includes activities such as supply and cash transfers to partners.
- **Monitoring of implementation**. This should include the extent to which inputs are provided, work schedules are kept to, and planned outputs achieved, so that any deficiencies can be detected and dealt with promptly.
- **Reporting.** Offices should report achievements and the use of resources against objectives or expected results. This covers annual and donor reporting, plus any specific reporting obligations an office might have.
- **Evaluation**. The office should assess the ultimate outcome and impact of programme interventions and identify lessons learned.

All the areas above were covered in this audit, with the exception of processes related to agreed actions from the 2013 audit. These included the use of data in programme design, annual planning and in the definition of results, the implementation of the Harmonized Approach to Cash Transfers and the strategies for programme monitoring and evaluations.

The audit found some controls were functioning well. The office used UNICEF's Emergency Preparedness and Response (EPR) System to record key early warning and early action activities. The information in the UNICEF EPR system was regularly reviewed in 2014 by the designated staff in the office. The Country Management Team served as the emergency management team and all staff members were aware of the level of preparedness. Reports to donors were reviewed and sent on time.

However, the audit noted the following.

Planning

The audit reviewed the office's annual work-planning process for 2014.

During the period under review the office had delivered programme supplies worth approximately US$ 29.5 million. Supply plans for technical services are required by Section 4 of UNICEF's Programme Policy and Procedure Manual (PPPM), and by Chapter 3 of the Supply Manual. The office's consolidated supply plan referenced the source of funds, but not the specific workplan activities to which they related. This cross reference is necessary in ascertaining the supplies being purchased are indeed for, and are relevant to, activities that have been planned and approved in that period.

The audit also reviewed the Programme Information Database (PIDB) codes. This coding system is used for results-based planning, and its correct application enables UNICEF to accurately measure, monitor and report on key results. Programme instruction CF/PD/PRO/2014-001 requires all Heads of Offices to designate staff who will periodically verify the correctness of codes used by that office. However, the DPRK country office did not assign responsibility for the review of the PIDB codes used, and there was no evidence of any such review in the 2014 planning, mid-year review or in other documents provided to the audit.

Agreed action 3 (medium priority): The office agrees to strengthen its work-planning processes by ensuring that:

i. Supply plans have clear references to the workplan activities from which they are derived.
ii. Programme Information Database Coding is completed accurately at the beginning of the planning period and periodically reviewed for relevance.

Staff responsible for taking action: Deputy Representative, Supply specialist, PID coding focal person
Date by which action will be taken: October 2015

Processing of cash transfers and reimbursements

For the period from 1 November 2013 to 30 November 2014 the VISION general ledger accounts showed that there had been cash transfers to partners of about US$ 3.9 million of which US$ 3 million was transferred to the World Health Organization (WHO) as the Global Fund Sub-Recipient[2] and US$ 0.9 million was transferred as reimbursements to Government partners.

The audit sampled cash transfers and reimbursements to 10 implementing partners, four to WHO and the remainder to Government partners. The following was noted.

Government partners: The office still uses the Cash Advance to Government (CAG) forms and not the Funding Authorization and Certificate of Expenditures (FACE) forms.[3] The FACE forms were designed to reflect the workplans, which set out the activities for which funds are being requested, or (if the transfer is being liquidated) on which they have been spent. The form also has a cumulative expenditure column that allows for the comparison of funds utilized against an approved budget. With the use of the CAG forms, this comparison is not as easy and the audit noted that in three out of the six samples reviewed, there was no clear linkage between the cash transfer reimbursement requests and the activity in the workplan. The audit

[2] The Global Fund does not manage programmes as such. It disburses funds to one or more Principal Recipient in a country; these can disburse funds to sub-recipients, but retain financial and programmatic responsibility for the grant. UNICEF is the Principal Recipient in the DPRK, with just one sub-recipient in the country (the WHO).
[3] The Funding Authorization Certificate of Expenditure (FACE) form is used by the partner to request and liquidate cash transfers. It is also used by UNICEF to process the requests for and liquidation of cash transfers. The FACE forms should reflect the workplans, which set out the activities for which funds are being requested, or on which they have been spent.

could not therefore confirm that the activities had been planned and budgeted for.

Additionally, there was no analysis of the utilization against the approved activity budget. In four out of the six cases sampled, the actual utilization was below budget, and there was no explanation for the differences.

The UN sub-recipient: A review of the four cash disbursement requests from WHO found that they did not indicate the workplan activity to which they were related. The UNICEF office stated that this was mitigated by detailed quarterly expenditure reports, based on the detailed Global Fund workplan and aligned with the country office's annual workplan. However, indicating the workplan activity at a transactional level would ensure the proper accumulation of expenditure against that activity.

The audit also noted that requests for disbursement were sometimes made in the middle of the period set for implementation (for example, a request was made in March for the implementation period of January to June). This meant in some cases that the payment was made towards the end of the implementation period, which could affect implementation. The reasons for the delay in requests was not recorded.

In all four WHO disbursement requests reviewed, there were differences between the amount requested and the actual payment. There was no documented explanation for the difference. It may indicate that some activities could not be implemented; if so, this should be clarified and the reasons for it analysed.

Agreed action 4 (medium priority): The office agrees to:

i. Review the cash transfer process and ensure clarity and consistency of requests and reimbursements. As part of the process, the office will ensure that standard formats for cash transfer requests and settlements as recommended under the Harmonized Approach to Cash Transfers guidelines are used.
ii. Ensure that partners provide an analysis of significant variance between the budgets set and the actual expenditure claimed, to ensure that bottlenecks or any other impediments to full/planned implementation are identified and addressed.
iii. Ensure the relevant workplan activity is indicated on the disbursement requests and that implementation against the annual workplan is monitored.

Staff responsible for taking action: Representative, Deputy Representative, Chief of Operations, Administrative/Finance Manager, Section Chiefs
Date by which action will be taken: December 2015

Monitoring of supply plan

Supply monitoring is important to ensure timely movement of supplies and their use for the appropriate activities. During the audit's review of review of cash transfers (see previous observation), one Government partner indicated that consumables/supplies that were to be provided by UNICEF had been provided late, and that this had occurred on previous occasions, affecting timely implementation of the activities.

The UNICEF office has some limitation of access in performing supply end-user monitoring. However, it is supposed to be performing checks at institutions it does visit, and should include end-user monitoring in a new monitoring strategy that is being implemented. Careful management and monitoring of supply and beneficiary/end user access is important, both for its own sake and because it is an essential indicator as to how the programme is being implemented.

Agreed action 5 (medium priority): The office agrees to ensure that supplies are monitored in conjunction with the programme activities that they relate to, and that supply end-user monitoring is incorporated into the monitoring strategy being implemented.

Staff responsible for taking action: Deputy Representative, Supply Specialist, Section Chiefs
Date by which action will be taken: June 2015

Programme management: Conclusion

Based on the audit work performed, OIAI concluded that the controls and processes over programme management, as defined above, were generally established and functioning during the period under audit.

3 Operations support

In this area the audit reviews the country office's support processes and whether they are in accordance with UNICEF Rules and Regulations and with policies and procedures. The scope of the audit in this area includes the following*:*

- **Financial management**. This covers budgeting, accounting, bank reconciliations and financial reporting.
- **Procurement and contracting.** This includes the full procurement and supply cycle, including bidding and selection processes, contracting, transport and delivery, warehousing, consultants, contractors and payment.
- **Asset management**. This area covers maintenance, recording and use of property, plant and equipment (PPE). This includes large items such as premises and cars, but also smaller but desirable items such as laptops; and covers identification, security, control, maintenance and disposal.
- **Human-resources management.** This includes recruitment, training and staff entitlements and performance evaluation (but not the actual staffing structure, which is considered under the Governance area).
- **Inventory management.** This includes consumables, including programme supplies, and the way they are warehoused and distributed.
- **Information and communication technology (ICT)**. This includes provision of facilities and support, appropriate access and use, security of data and physical equipment, continued availability of systems, and cost-effective delivery of services.

All of the above areas were covered in this audit, except for asset management, human resources management, and inventory management.

The audit found that controls were functioning well over a number of areas. For instance, bank accounts were reconciled promptly, and bank and cash balances were regularly monitored and well managed.

However, the audit noted the following.

Information and Communication Technology (ICT)

UNICEF offices should have a Business Continuity Plan (BCP) and Disaster Recovery Plan (DRP) so that they can maintain critical operations in a major incident. UNICEF guidance on these[4] requires that the viability, reliability and currency of the plans be evaluated through testing at least once every calendar year. Testing should include the usability and reliability of off-site data, systems, applications, and materials, and a summary of the results should be checked against test goals and plans.

The office's BCP and DRP had been updated on 17 November 2014. However, the last time the BCP/DRP had been tested was 28 December 2012. The office stated that the DRP testing in 2012 was limited to Internet connectivity and the LAN.

The BCP referred to an alternate/recovery site, but it was not named. The office stated that

[4] CF/ITSS/STANDARD/2014.

the recovery sites were the WFP and UNDP[5] compounds and use of either one depended on the situation at hand. However, there was no documented agreement between these UN agencies or agreed procedures in the event of an emergency.

The 2014 BCP stated that fire procedures were in the UN security plan, which was not annexed to the BCP. The last fire drill was stated by the office to have been conducted in June 2013 but there was no record of the fire drill results.

Agreed action 6 (medium priority): The office agrees to ensure that:

i. The Business Continuity Plan and Disaster Recovery Plan are regularly updated and tested and the relevant documents amended and annexed appropriately.
ii. A Memorandum of Understanding outlining clearly the modalities for use of the relevant UN agencies premises, systems and materials for recovery sites, is put in place.
iii. A summary of results is maintained of all testing, including fire drills, and used to update plans as relevant.

Staff responsible for taking action: Chief of Operations and ICT officer
Date by which action will be taken: December 2015

Operations support: Conclusion

Based on the audit work performed, OIAI concluded at the end of the audit that the controls and processes over operations support, as defined above, were generally established and functioning during the period under audit.

[5] World Food Programme; UN Development Programme.

Annex A: Methodology, and definition of priorities and conclusions

The audit team used a combination of methods, including interviews, document reviews, testing samples of transactions. The audit compared actual controls, governance and risk management practices found in the office against UNICEF policies, procedures and contractual arrangements.

OIAI is firmly committed to working with auditees and helping them to strengthen their internal controls, governance and risk management practices in the way that is most practical for them. With support from the relevant regional office, the country office reviews and comments upon a draft report before the departure of the audit team. The Representative and their staff then work with the audit team on agreed action plans to address the observations. These plans are presented in the report together with the observations they address. OIAI follows up on these actions and reports quarterly to management on the extent to which they have been implemented. When appropriate, OIAI may agree an action with, or address a recommendation to, an office other than the auditee's (for example, a regional office or HQ division).

The audit looks for areas where internal controls can be strengthened to reduce exposure to fraud or irregularities. It is not looking for fraud itself. This is consistent with normal practices. However, UNICEF's auditors will consider any suspected fraud or mismanagement reported before or during an audit, and will ensure that the relevant bodies are informed. This may include asking the Investigations section to take action if appropriate.

The audit was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing of the Institute of Internal Auditors. OIAI also followed the reporting standards of International Organization of Supreme Audit Institutions.

Priorities attached to agreed actions

High: Action is considered imperative to ensure that the audited entity is not exposed to high risks. Failure to take action could result in major consequences and issues.

Medium: Action is considered necessary to avoid exposure to significant risks. Failure to take action could result in significant consequences.

Low: Action is considered desirable and should result in enhanced control or better value for money. Low-priority actions, if any, are agreed with the country-office management but are not included in the final report.

Conclusions

The conclusions presented at the end of each audit area fall into four categories:

[Unqualified (satisfactory) conclusion]

Based on the audit work performed, OIAI concluded at the end of the audit that the control processes over the country office *[or audit area]* were generally established and functioning during the period under audit.

[Qualified conclusion, moderate]
Based on the audit work performed, OIAI concluded at the end of the audit that, subject to implementation of the agreed actions described, the controls and processes over [audit area], as defined above, were generally established and functioning during the period under audit.

[Qualified conclusion, strong]
Based on the audit work performed, OIAI concluded that the controls and processes over [audit area], as defined above, needed improvement to be adequately established and functioning.

[Adverse conclusion]
Based on the audit work performed, OIAI concluded that the controls and processes over [audit area], as defined above, needed **significant** improvement to be adequately established and functioning.

[Note: the wording for a strongly qualified conclusion is the same as for an adverse conclusion but omits the word "significant".]

The audit team would normally issue an ***unqualified*** conclusion for an office/audit area only where none of the agreed actions have been accorded high priority. The auditor may, in exceptional circumstances, issue an unqualified conclusion despite a high-priority action. This might occur if, for example, a control was weakened during a natural disaster or other emergency, and where the office was aware the issue and was addressing it. Normally, however, where one or more high-priority actions had been agreed, a ***qualified*** conclusion will be issued for the audit area.

An ***adverse*** conclusion would be issued where high priority had been accorded to a significant number of the actions agreed. What constitutes "significant" is for the auditor to judge. It may be that there are a large number of high priorities, but that they are concentrated in a particular type of activity, and that controls over other activities in the audit area were generally satisfactory. In that case, the auditor may feel that an adverse conclusion is not justified.