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

January 2018

Office of Internal Audit
and Investigations (OIAI)
Report 2017/27

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children

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# Summary

The Office of Internal Audit and Investigations (OIAI) audited the Democratic People's Republic of Korea (DPRK) Country Office during the period from 16 February to 31 May 2016, and subsequently carried out further work at UNICEF headquarters in New York. The audit period covered was from 15 February 2015 to 30 April 2016. This audit did not involve a field visit in-country.

The DPRK country programme for 2011-2015 (subsequently extended through 2016) consists of five main programme components: *Health*; *Nutrition and Care*; *Water, Sanitation and Hygiene*; *Education*; and *Advocacy and Knowledge Management*. There is also a cross-sectoral component. The total budget of the country programme was approximately US$ 128.1 million, of which US$ 9.3 million was Regular Resources (RR) and US$ 118.8 million was to be raised as Other Resources (OR). RR are core resources that are not earmarked for a specific purpose. OR are contributions that may have been made for a specific purpose, and may not always be used for other purposes without the donor's agreement.

The Executive Board approved a one-year extension of the country programme in February 2015. This was to align the UNDP, UNFPA and UNICEF programme cycles, and allow a more thorough review of the current UN Strategic framework. It was also intended to allow UNICEF to update its analysis (SitAn) of the situation of children and women in the country, and to conduct evaluations of the tuberculosis and malaria programmes and the Expanded Programme on Immunization.

Since 2010, UNICEF has been a Principal Recipient (PR) of funds from the Global Fund to Fight Aids, Tuberculosis and Malaria. During this period, UNICEF has signed grant agreements totalling over US$ 81 million. The Global Fund disburses funds to one or more Principal Recipients in a country who can disburse funds to sub-recipients, but who nonetheless retain financial and programmatic responsibility for the grant. UNICEF as PR has one sub-recipient in the country, the World Health Organization (WHO).

UNICEF and other actors are operating within a challenging and rapidly-changing programming environment in DPRK. In this context, OIAI's internal audit sought in particular to assess the effective management of risks to programme implementation, including the programme activities managed under the funding agreement with the Global Fund.

## Action agreed following the audit

The audit identified a number of areas where further action was needed to better manage risks to UNICEF's activities. In discussion with the audit team, the country office and headquarters divisions have agreed to take measures to address these risks and issues.

Two are being implemented as a high priority; that is, to address issues requiring immediate management attention. These are as follows.

- The country office, with guidance from Public Partnerships Division, the Division of Finance and Administrative Management and the regional office, will review and propose practical approaches to address any inconsistencies between donor requirements and UNICEF procedures; and will also address issues around operationalization of the framework agreement.

- The country office will assess and document the level of assurance provided by the current arrangements for programme monitoring and clearly identify, and where appropriate communicate to relevant partners, the accepted programme monitoring risks arising from the operating environment.

## Conclusion

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 the office were generally established and functioning during the period under audit.

The DPRK Country Office, the East Asia and the Pacific Regional Office (EAPRO) and OIAI will work together with relevant headquarters divisions 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 the case of DPRK, the internal audit's focus was in particular on assessing the effective management of risks to programme implementation, including the delivery of programme activities managed under the funding agreement with the Global Fund.

This report presents the more important risks and issues found by the audit, the measures agreed with the auditee to address them, and the timeline and accountabilities for their implementation. It does not include lower-level risks, which have been communicated to the auditee in the process of the audit.

# Audit observations

## Management of Grant Agreement

UNICEF has been the Principal Recipient (PR) for Global Fund funds in DPRK since 2010. On 29 May 2015, on expiry of the previous agreement, a new Framework Agreement was agreed between the Global Fund and UNICEF. Two Grant Confirmations[1] were signed: for the Malaria component worth about US$ 8.86 million for the period 1 March 2015 to 28 February 2018; and for the Tuberculosis (TB) component, worth about US$ 28.44 million for the period 1 October 2015 to 30 June 2018.

Various documents define the implementation procedures for these grants. Besides the Framework Agreement itself, there are supplements to the Grant Confirmations, the Global Fund's Grant Regulations (2014), and its guidelines for grant budgeting and annual financial reporting (2014).

The audit noted the following.

***Disbursement delays:*** Article 1, section 1.3 of the Agreement states that UNICEF will administer the funding received in accordance with its own rules and procedures. However, the audit noted some inconsistencies between the terms of the Framework Agreement and applicable UNICEF regulations and procedures that affected the implementation of the programme. For example, the Framework Agreement states that UNICEF is to receive grant funds in advance of its implementation of relevant programme activities. While funds were received to cover activities ending on 31 December 2015, there were delays in the receipt of funds such that as of March 2016 no funds had been received by UNICEF to implement the activities that were planned to start from January 2016 for the TB project.

The delay appears mainly to have been due to differences in standards for disbursement of funds. A UNICEF country office would generally work on an annual basis according to the

[1] Global Fund procedure is that a Framework Agreement is signed to cover general terms and conditions of cooperation with the country; Grant Confirmations are then issued for specific programmes, and include the terms and conditions specific to that grant.

workplans agreed with the implementing partner. However, the Global Fund required quarterly activity reports and only disbursed funds based on those quarterly reports, despite the clause in the Framework Agreement that stated that UNICEF would proceed based on its own rules and regulations. These delays posed a risk to UNICEF as the country office is expected to deliver activities as planned even where funds are received late.

A further cause of delays in disbursement arose from incompatible reporting procedures. The Framework Agreement states that "reports will be in the form of the Progress Update and Disbursement Request (PUDR) agreed to between the Parties." UNICEF was required to prepare PUDRs "using its standard system-generated donor reports and in line with its financial regulations, rules and policies. It is understood that, in the preparation of PUDRs and all other reports, UNICEF will not be required to go beyond its standard operating procedures".

In 2016, UNICEF introduced a "Donor Statement by Activity" report that replaced various utilization-based reports that country offices were using to provide donors with unofficial financial status updates. The new report allows UNICEF to present identical expenditures in the certified and uncertified versions of the reports. This report does not however provide the Global Fund with the information required in the PUDRs resulting in the request for additional financial information. For example, in February 2016, the DPRK office presented a progress report for the Malaria and TB grants for the periods from 1 March to 31 December 2015 and 1 October to 31 December 2015 respectively, along with corresponding disbursement requests for the period 1 January to 31 December 2016. The Global Fund asked the office to complete the annual cash forecast and the related templates for the PUDR in order to provide a full picture of the total cash needs. This occurred because UNICEF had not agreed with the Global Fund on the acceptable reporting format after introduction of the new donor report format.

The country office acknowledged that the delay in the receipt of funds caused a risk to the activities and reputation of UNICEF, as the office was expected to implement programme activities based on the agreed plan within a specific timeframe. The office had informed UNICEF's Public Partnerships Division (PPD), which had started negotiating with the Global Fund on the agreed timeline for release of funds and on the reporting processes.

***Programme Assets:*** According to the Framework Agreement, during the implementation period, "title to relevant Program Assets shall be held by the Grantee or a Sub-recipient or other entity approved by the Grantee, unless the Global Fund and UNICEF at any time agree that title be transferred to the Global Fund or another entity as mutually agreed." In addition, the Framework Agreement states that the "Grantee shall require each of its Sub-recipients to maintain appropriate records of all fixed assets procured… [and that the]… Grantee will use its internal policies and procedures for recording and reporting on fixed assets. The Sub-recipient will be required to record and maintain separate records for low value assets, and in compliance with asset classification and asset value ceilings in the Grantee's policies and procedures. The records described under this provision shall include fully depreciated, non-operational, or damaged fixed assets with original value, that are not classified as low value assets."

There are contradictions between the requirements cited above and UNICEF's standard procedures and practices. For example, according to UNICEF procedures, title to all programme supplies passes to the implementing partners as soon as the supplies are handed over and supplies are expensed. UNICEF provides offices with guidance on the management of transport supplies such as cars and motorcycles, but there is no UNICEF policy or regulation on programme supplies (such as health equipment or other small value items) that are given to implementing partners. UNICEF's policy on Property and Equipment (P&E) states that items with a value below US$ 2,500 should be treated as expenses rather than as assets; UNICEF's view is that tracking them as assets is not economic.

A Global Fund team that visited DPRK raised a number of issues related to the location of health equipment and of equipment provided under the grant that was not functioning. They suggested that UNICEF should maintain a record of all equipment regardless of its value, and that the country office should design a system for mapping the location of all programme equipment such as X-ray and microscopes provided to the Government. Furthermore, the Global Fund team's report appeared to suggest that all Government requests to relocate programme equipment from one location to another were to be approved by the Global Fund based on information provided by UNICEF. The Global Fund team indicated that as Principal Recipient, the UNICEF country office had an additional responsibility to ensure proper transportation and installation of equipment provided by the Global Fund and to report programme equipment in poor condition. However, allocation to UNICEF of responsibility for detailed monitoring of programme assets and equipment is not in line with the agreement with Global Fund which allows UNICEF to follow its standard practice.

The office had recorded in its database 450 items of vehicles and motorcycles on loan that had been procured using Global Fund contributions. These 'assets on loan' had not been transferred to the Government because the country office retained the title to all equipment purchased by the Global Fund, and needed to report on these items through a Fixed Assets Register. Consequently, the office had to regularly track and report on the condition of any equipment purchased (e.g. motorcycles) including those that had no remaining book value due to depreciation. Of the 450 items on loan, 128 were items with an individual acquisition value ranging from US$ 1,352 (motor-tricycle) to US$ 564 (motorcycle). There were also items on loan procured in 2011 that had no financial value.

The audit team was informed that PPD and the Division of Finance and Management (DFAM) intended, in consultation with the country office, to discuss with the donor a unit value below which vehicles and motorcycles could be expensed rather than be issued on loan, or define an efficient mechanism to manage low-value items.

The ambiguities and inconsistencies between the terms of the Framework Agreement and UNICEF's applicable rules and regulations had affected the implementation of the programme and had reduced efficiency in the management of the grant. The issues related to assets on loan were raised in previous audit reports but were not fully addressed.

**Agreed action 1 (high priority):** The country office with guidance from PPD, DFAM and the regional office, agrees to:

i. Review and devise practical approaches to address any inconsistencies between Global Fund requirements and UNICEF procedures, with particular reference to the recording and disposal of programme assets and assets on loan from the Global Fund programme; and
ii. Agree with the Global Fund the record-keeping and reporting requirements necessary for the timely disbursement of and accounting for programme funds. The agreement should address the continued need for the preparation of Progress Update and Disbursement Request reports and the timing and release of programme funds.

Responsible staff members: Deputy Representative, with PPD Global Funds Manager
Target date for completion: March 2018

## Results-based programme planning

UNICEF offices agree workplans with their implementing partners. According to UNICEF's Programme Policy and Procedure Manual (PPPM), workplans can be developed on an annual or multi-year basis, or as rolling workplans (RWPs).

The RWPs or multi-year workplans are expected to detail outputs, indicators, targets, baselines, activities to be carried out, the responsible implementing institutions, timelines and planned inputs from the partners and UNICEF. Workplans serve as the basis for programme disbursements to partners and are expected to be signed with key partners before the end of February of the year of implementation (as recommended by the PPPM).

UNICEF and the Government had entered into a programme of cooperation from 1 January 2011 to 31 December 2015 (extended through 2016) and a CPAP[2] had been signed covering the country programme period. All workplans were signed at the beginning of the year. The audit reviewed a sample of the workplans and noted that the programme outcomes and outputs[3] of six of them were generally not specific and measurable. In one of the workplans reviewed in detail (Nutrition), there was a discrepancy between the UNICEF outcome stated in the UN strategic framework for the DPRK and the outcome stated in the workplan.

For the Health (Tuberculosis and Malaria) programme funded by the Global Fund, the office is required to implement planned activities as agreed with the Government, the Global Fund and the World Health Organization (WHO). The audit team noted that the grant agreements for Tuberculosis and Malaria (TB) were signed after the workplans because it took a long time for the agreements to be finalized. The activities included in the workplans signed with the Government were therefore approximate and provisional, were not costed, and were not fully aligned with the Global Fund workplan, which was supposed to be the official document for the implementation of the activities under the Global Fund agreements.

Finally, the audit team noted that in February 2015, the UNICEF Executive Board had approved a one-year extension of the DPRK country programme. This was partly to allow completion of planned activities that had been postponed due to funding constraints. However, the 2015/2016 workplans did not indicate which activities had been postponed and which were cancelled. Moreover, the signed workplans were not reviewed or amended to reflect the changes made.

Better internal quality assurance of the work plans could have helped address these issues. The implementation of the Global Fund workplan presented an additional challenge to the programme planning, as it tended to formulate outputs in terms of supplies delivery and

[2] The CPAP is the Country Programme Action Plan, and is a formal agreement between a UNICEF office and the host Government on the programme of cooperation, setting out the expected results, programme structure, distribution of resources and respective commitments during the period of the current country programme.
[3] UNICEF programmes plan for results on two levels. An outcome is a planned result of the country programme, against which resources will be allocated. It consists of a change in the situation of children and women. An output is a description of a change in a defined period that will significantly contribute to the achievement of an outcome.

tended to use phrases such as "completed in a timely manner," rather than the SMART[4] targets and indicators that UNICEF would normally use.

**Agreed action 2 (medium priority)**: The office agrees to strengthen its quality assurance mechanism to ensure that workplans are prepared in accordance with UNICEF's Programme Policies and Procedures Manual. Specifically the office agrees to:

i. Ensure that outputs in the work plans are specific and measurable, and the outcomes are in-line with those included in the UN strategic framework.
ii. Clearly show the implementing and strategic partners in every workplan.
iii. For the project activities funded under the Global Fund agreements, review and agree with the donor on the timely completion of the activity work plan so that it can be aligned with the work plan signed with the implementing partner(s).

Responsible staff members: Deputy Representative
Target date for completion: February 2018

## Programme monitoring

Monitoring is important for the effective and efficient implementation of UNICEF's programmes. By comparing progress against targets, monitoring identifies bottlenecks and barriers so that measures can be devised to overcome them. Besides monitoring progress in the field, country offices should conduct mid-year and annual programme reviews jointly with Government counterparts, to review progress together and identify constraints and lessons learned.

The audit noted the following.

***Monitoring activities:*** The office had a Health and Nutrition monitoring plan and monitoring tools. The Global Fund projects were driven by their own pre-approved performance metrics, and UNICEF, as Principal Recipient, was supposed to receive data demonstrating their achievement from WHO (the Sub-recipient) and the Government. In 2015, the country office had drawn up a monitoring plan that included programme monitoring for the year and the needs of each programme. Mid-year and annual reviews took place in collaboration with the Government.

However, the country office had no established benchmarks for the frequency of monitoring visits, and could not analyse monitoring activities by output and location to align monitoring targets with resources available for this purpose. Field monitoring activities had in fact been greatly affected by the difficulties accessing cash in-country. Moreover, monitoring resources had subsequently been reduced as part of the cash conservation plan begun in March 2016.

Access to field sites was also a practical constraint. The monitoring strategy presentation made to the Ministry of Public Health (MOPH) by the Nutrition programme indicated several restrictions on monitoring. The report of the 2015 annual review indicated that UNICEF international staff have access to 173 out of 208 counties across DPRK. A further 17 counties could be accessed, but only by national personnel working for UNICEF, whilst 18 counties were not accessible at all. The report also stated that UNICEF had limited its support to areas that are not accessible for direct monitoring, except for important public health programmes

[4] SMART means Specific, measurable, achievable, relevant and time-bound.

such as immunization.

According to the office, another limitation was the available travel windows for field visits, as local counterparts might not be available to receive a field visit for two or three months in a calendar year, and as international staff were outside the country for about two and a half months per year. Limited field supervision and monitoring were major constraints identified by various programmes during annual review meetings held in 2015.

***Field-trip reports:*** The audit reviewed a sample of trip reports and noted that all of them adequately recorded objectives of visits, challenges, results achieved by partner and follow-up of previous recommendations.

The reports did not, though, specify linkages to the workplan outputs or state what follow-up actions were discussed during the visits. Some sampled field reports did not use standard checklists to review status, use and effectiveness of programme inputs, and the office did not have statistics on numbers of field missions that reviewed the use of key programme supplies. There was also no follow-up mechanism to monitor outstanding key action points.

***Periodic reviews:*** The office conducted mid-year and annual review meetings. Sample annual review reports stated key achievements, lessons learned or challenges, and included priorities for the following year.

The annual reviews focused on the completion of activities planned in the workplan, rather than achievement of the planned outputs or annual targets. The number of activities not achieved varied between 13 and 33 percent of planned activities. For example, the 2015 annual review found that 33 percent of the planned activities in the WASH[5] programme had not been implemented. The annual review had also found that there had been overambitious planning because the workplan had not been amended to reflect the cashflow and programme funding constraints.

The review also noted that in the case of the Health programme, there had been a late start to programme implementation and a delay in supply procurement due to limited staff capacity (staff absence due to Ebola quarantine, which had lasted until the end of March). For the Nutrition programme, the annual review report noted a need for integrated and coordinated action, and a limited partner capacity reducing the office capacity to monitor the effectiveness of programme implementation.

The annual reviews observed that the absence of written manufacturers' guarantees for supplies that were valid in the DPRK, and limited capacity in the country for repair or replacement of equipment, are issues that may require an assessment of in-country logistics for distribution of supplies.

The challenges in programme monitoring were raised in previous audit reports. Identified actions in response were not, however, sustained due to the complexity of the operating environment.

**Agreed action 3 (high priority)**: The office agrees to continue to assess and document the level of assurance provided by the current arrangements for programme monitoring and clearly identify, and where relevant communicate to relevant partners, the accepted programme monitoring risks arising from the operating environment.

[5] Water, Sanitation and Hygiene.

Responsible staff members: Representative, Deputy Representative and Chief of Operations
Target date for completion: February 2018

**Agreed action 4 (medium priority)**: The office agrees to strengthen programme monitoring and periodic programme reviews by:

i. Planning and reporting of field visits so that they include a review of the status and use of programme inputs, and establish a mechanism to monitor follow-up action of issues noted during field-monitoring visits. The office will adopt the latest programme-specific UNICEF field-monitoring visit templates.
ii. Strengthening its quality assurance of the mid-year and annual review reporting process so that it considers and reports upon outputs achieved, lessons learned, challenges and priorities for the following year and actions to address areas noted as requiring action.

Responsible staff members: Deputy Representative
Target date for completion: February 2018

## Evaluations and related activities

The UNICEF office had made progress by supporting the Central Bureau of Statistics (CBS) in establishment of a Child Data Management Unit (CDMU) and in the signature, for the first time, of a Memorandum of Understanding for data sharing and collaboration on studies and evaluations related to children. The office had also drawn up a multi-year integrated monitoring and evaluation plan (IMEP) at the start of the country programme, and there was a two-year (2015-2016) IMEP that included four evaluations.

The office mentioned a number of challenges beyond its control regarding evaluations. They included difficulties in finding technical experts, donor reluctance to support the evaluation process, and administrative challenges for the Government. The challenges in programme evaluation are an issue that was identified in previous audit reports that was not fully addressed in the existing operating environment.

**Agreed action 5 (medium priority)**: The office agrees to continue discussions with Government to advocate for planned evaluation activities. In the absence of effective evaluations, the office should identify compensating mechanisms to demonstrate programme results and to identify and share learning on how activities may be improved.

Responsible staff members: Representative and Deputy Representative
Target date for completion: The office reports this action has been completed

## Resource mobilization

The total Other Resources (OR) budget was set at a ceiling of US$ 118.8 million. The office's resource-mobilization report as of December 2015 showed an overall funding shortfall of 28 percent. Advocacy programmes had received only 2 percent of required funds; the shortfalls for WASH and for Education were 59 percent and 49 percent respectively. The Health and Nutrition and Care programmes were relatively well funded with respective funding of 91 percent and 77 percent. For these two programmes, the funding will mostly be from the agreements signed with the Global Fund which will provide about 67 percent of the OR budget. Lack of funding risked non-implementation of planned activities.

Difficulties in resource mobilization have contributed to staff vacancies in the office. At the start of the country programme, 16 international staff posts were approved to support programme implementation. Three of the approved international posts were vacant at the time of audit (the WASH, Education and Procurement specialists' positions). No recruitment had been commenced for the WASH or Education positions due to funding constraints.

The regional office informed the audit team that it would be difficult to have a realistic resource mobilization strategy due to lack of clarity from donors and the challenging and unpredictable programme environment. The regional office indicated that past strategies to engage donor countries, funding proposals, discussions and agreements had not succeeded for reasons beyond their control and that of the country office. Notwithstanding the challenges of mobilizing the required financial resources, it was unclear to the audit team how programme activities planned to be supported by OR funding were prioritized.

**Agreed action 6 (medium priority):** The country office agrees, with the support of the regional office and in light of funding constraints and challenges in mobilizing required programme funds, to establish a process to prioritize those programme activities in the work plans that will be supported based on available funding and desired outputs over a specified period.

Responsible staff members: Representative and Deputy Representative
Target date for completion: February 2018

# Annex A: Methodology, and definitions of priorities and conclusions

The audit team used a combination of methods, including interviews, document reviews, and 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 its clients 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 client's own (for example, a regional office or headquarters 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 in the report summary 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 office 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 the office 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 the office needed improvement to be adequately established and functioning.

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