

Audit Report

# Grant Closure Processes

## Follow-up Review

GF-OIG-16-017

4 July 2016

Geneva,

Switzerland

 **The Global Fund**

Office of the Inspector General

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# I. Background

Grant closure is the final stage of the Global Fund grant cycle. It involves an assessment of grant accomplishments, recovery of outstanding ineligible funds, transfer or recovery of cash and transfer or reallocation of assets for continued use in the fight against the three diseases.

In 2013, the Office of the Inspector General (OIG) conducted an internal audit<sup>1</sup> of the Global Fund's grant closure processes. The OIG concluded that major improvements were needed in the management of grant closure activities, including the following four key issues:

- Unknown unspent cash balances in country: no information was available at the Global Fund Secretariat regarding cash balances held by Principal Recipients or Sub-Recipients for almost half of the grants tested.<sup>2</sup> This prevented the Secretariat from planning disbursements based on cash needs, leading to an increased risk of having large cash balances at the end of the grant to be recovered by the Global Fund or reallocated to a new grant during grant closure.
- Unused grants funds remain blocked for longer than necessary after program end date: The release of undisbursed funds had not been prioritized by the Global Fund Secretariat, preventing funds from being made available for other programs.
- Use of funds beyond grant term: the audit identified that Principal Recipients were using cash balances held in country after the grant end date which is prohibited under the grant agreement.
- Delays in closing grants: The OIG identified 248 outstanding grants in closure. Of these, 50% of the grants due for closure by the end of 2012 had not been closed with 80% of these grants overdue by more than a year. These delays were attributed to low prioritization of closure activities by country teams, onerous closure processes, inadequate guidance, and the absence of proper record keeping.

## What has changed since the 2013 OIG report?

To address the issues identified in the 2013 audit, the Secretariat agreed to:

- 1) prioritize the closure of the 248 long-outstanding grants, particularly those due for closure prior to 2012;
- 2) simplify grant closure processes;
- 3) embed closure processes and controls within Global Fund finance and grant management systems; and
- 4) ensure compliance with closure processes.

## Grant closure principles

As part of their effort to address these issues, the Secretariat introduced a new, principles-based Operational Policy Note for grant closure. As per the note, grant closures must adhere to the following four principles as a minimum requirement:

Principle 1: Grant funds should not be left earmarked in the Global Fund Finance systems and/or with implementers for longer than necessary for the implementation of program activities.

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<sup>1</sup>GF-OIG-13-040 Internal Audit of the Processes Underpinning Grant Closure Chapeau Report. [Note: in 2013, per the Disclosure Policy, OIG internal audits were not published on the Global Fund website].

<sup>2</sup> No information available for 22 out of 50 grants reviewed.

**Principle 2:** When they can no longer be used under the grant for which they have been purchased, grant assets should continue to be used exclusively for the purposes of the fight against the three diseases.

**Principle 3:** Country teams should ascertain the extent to which grants have achieved their strategic objectives, and that there is sufficient assurance over the program to confirm any such achievement.

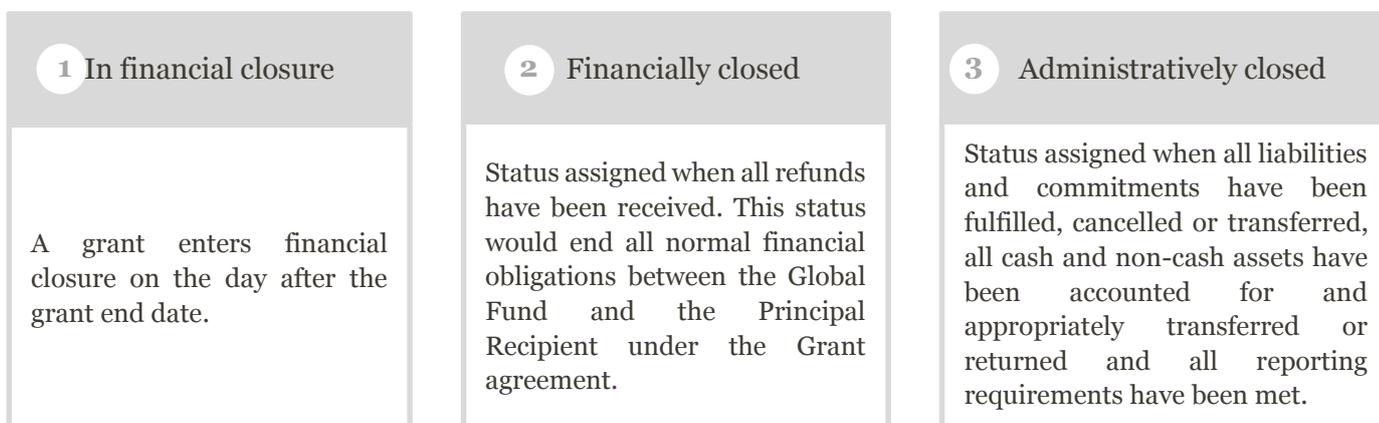
**Principle 4:** All activities conducted with grant funds should be discussed and agreed between the Principal Recipient and the Global Fund, and should be governed by the terms and conditions of the grant agreement.

The grant closure policy clearly defines three types of closure and three different stages of closure.

*Fig 1. Three types of closure*

Closure due to consolidation	Closure of an ongoing grant as a result of a consolidation with a new grant resulting from a Concept Note or with another ongoing grant implemented by the same Principal Recipient. This is the regular and most common type of grant closure.
Closure due to a change of Principal Recipient	Closure of a grant whose implementation responsibilities are transferred from one Principal Recipient to another.
Closure due to “transition” from Global Fund financing	Closure of grant in a country no longer eligible for Global Fund financing for the disease component.

*Fig 2. Three grant closure stages*



## II. Objectives, Scope, Methodology and Rating

Given the significance of the issues identified in the 2013 audit, the OIG conducted a formal follow-up of changes made by the Secretariat to the grant closure process.

### 1) Objectives

The objectives of the review were:

1. to assess the adequacy of the design of controls over current grant closure processes, ensuring timely and accurate completion of the processes, and satisfactorily addressing and preventing the gaps identified in the 2013 audit;
2. to assess the effectiveness of controls over current grant closures in ensuring timely and accurate grant closures without the gaps identified in the 2013 audit.

The audit team reviewed the progress made in implementing the agreed management actions from the 2013 audit. As this is a follow-up review and not a full scope audit, this engagement does not include a complete assessment to provide assurance on the wider accounting, internal control processes and systems applicable to grant closure.

### 2) Scope & Methodology

This review was carried out at the Global Fund Secretariat and included:

- a review of all finance and other policies and processes related to grant closure;
- a detailed analysis of closure documents from a sample of 28 grants including close-out plans, financial reports, asset listings and grant closure plan approval implementation letters as applicable;
- interviews with 48 staff members from various Global Fund divisions and departments, including country teams representing 18 countries, the Grant Management Support Department, the Legal and Compliance Department, the Policy and Strategy Hub, the Risk Management Department and the Finance and Program Finance departments; and
- an analysis of grant data from Global Fund finance and grant management systems.

### 3) Rating

<b>Audit Objective/ Processes</b>	<b>Rating</b>	<b>Reference to findings</b>
Adequacy of the design of controls over current grant closure processes, ensuring timely and accurate completion of the processes, and satisfactorily addressing and preventing the gaps identified in the 2013 audit.	Partially effective	1,3
Effectiveness of controls over current grant closure processes, ensuring timely and accurate grant closures without the gaps identified in the 2013 audit.	Needs significant improvement	2,3

### III. Executive Summary

The purpose of this follow-up audit was to assess whether the new grant closure policies and procedures of the Global Fund, as well as other measures taken since the 2013 OIG audit, are adequately designed, operationally effective and whether they address the key risks identified in the previous audit.

Delays in grant closure may result in cash balances remaining in the country for longer than necessary, reducing the Global Fund's ability to redirect these assets to productive use in its programs and increasing the susceptibility of misuse, misappropriation and embezzlement.

Overall, the OIG noted significant improvements in the overall design of the grant closure policies and processes, particularly the management of cash balances and unused grant amounts as well as the simplification of grant closure procedures. However, various gaps in the compliance of these processes and monitoring of grant closures still exist, particularly with respect to embedding these processes for all ongoing grant closures.

#### **Adequacy of design of grant closure processes**

A new principles-based Operational Policy Note was put in place in December 2014 and simplified guidelines for long outstanding grant closures, in October 2013. The design of these new procedures simplified and accelerated the grant closure process. A new disbursements template was issued in January 2016 to better track cash balances held by the Principal Recipients and Sub-Recipients. Going forward, this will strengthen the controls over final remaining cash balances once they reach the grant closure stage.<sup>3</sup>

Since December 2015, a Recoveries Officer is required to report on all funds recoverable from grant recipients. In the past, only recoveries identified by the OIG were required to be reported to the Recoveries Committee of the Global Fund.<sup>4</sup> Furthermore, the automatic transfer of unused funds from a closed grant to a new grant has now been clarified following a decision by the Grant Approval Committee. This will minimize the amount of any unused funds remaining in grants after the closure date.

Some design gaps were noted with regards to the policy on asset management: for example, there is no specific guidance over asset management and transfers, meaning that the Global Fund does not have a risk-based approach to the completeness and accuracy of asset records and there is no way to ensure that assets are properly used for program purposes for the duration of their useful life. There are inadequate safeguards against duplicate financing of similar assets from next grant cycle funds and misuse of assets beyond approved health-related activities.

#### **Operational effectiveness of grant closure processes**

Tracking of cash balances at Principal Recipient and Sub-Recipient level has been in place since early 2016 through the new Progress Update Disbursement Request. Undisbursed grant amounts are also automatically cancelled or transferred to new grants. However, despite improvements in the design of grant closure processes, the following compliance gaps were identified:

- Significant delays in grant closure remain which were caused by lack of routine monitoring and accountability for grant closures. For example, no regular reporting is performed on grants due to be closed, which would ensure smoother and more systematic follow-up of delays. As a result, 65% of the 262 grants due for closure between January 2013 and December 2015 remain overdue at the time of writing.
- Grants were administratively closed while cash and recoveries were pending and receivable under those grants.

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<sup>3</sup> Estimates of closing cash balance are included as part of budget negotiations prior to signing new NFM grant.

<sup>4</sup> Recoveries typically exclude cash balances. This audit did not review the completeness or accuracy of the recoveries.

- There is no systematic tracking to ensure that the cash refunds or recoveries expected are compared against the actual cash received. There are also weak controls ensuring that all refunds and recoveries have been received before grants are closed. This has resulted in the administrative closure of grants while there were outstanding recoveries.

## IV. Findings and Agreed Management Actions

### **01. There are weaknesses in the accountability and the compliance monitoring mechanisms of grant closure processes.**

Over the past two years, the Global Fund has focused on closing long outstanding grants. Overall, 87% of the 248 grants due for closure by the end of 2012 have been closed. For these older grants, the closure was actively monitored and reported, and flexibilities provided by the new Operational Policy Note were appropriately used based on risk and materiality considerations. However, the OIG noted significant delays in closing grants due for closure after 2012, indicating that the grant closure process has not been systematically embedded: 65% of the 262 grants that were due to be closed between January 2013 and December 2015 remain overdue; of these, 52 have been overdue for more than a year.

Although responsibilities for grant closure activities are well-defined at the individual<sup>5</sup> and the Country Team levels<sup>6</sup>, there is inadequate management oversight to ensure compliance with Global Fund internal policies on grant closure. For example:

- There is no systematic monitoring of grant closure across the whole portfolio as required by the Operational Policy Note.<sup>7</sup> The grant management operational support team has been tracking the long outstanding grants identified in the 2013 OIG audit report, but not the grants with closure date after 2013 on an ongoing basis. In the absence of systematic monitoring, grant closures remain a low priority for country teams, meaning that in-country cash balances, refunds and recoveries may remain in the country longer than necessary. For the samples tested, the OIG auditors noted delays in the receipt of cash balances from the recipients ranging from two to five years, with individual grant amounts of up to US\$190,000.
- Current Global Fund systems do not enable systematic monitoring of recoveries from grants due for closure. An analysis of all Global Fund grants to date showed that funds were returned for 493 grants and funds were de-committed for 367 grants,<sup>8</sup> constituting around two thirds of the total of signed grants to date. However, there is no systematic tracking to ensure that cash refunds or recoveries expected are compared against cash received and there is no segregated control to ensure the completeness of all refunds and recoveries before grants are closed. For example, for a sample of four administratively closed grants tested, there were recoveries of approximately US\$1 million at the time of closure, out of which approximately only US\$0.2 million had been received by February 2016. Although recovery efforts are ongoing, the lack of systematic reconciliation means that there is a risk that the differential amount will not be tracked for ensuring full recovery.

### **02. Grant tracking systems and related documentation do not facilitate timely closure.**

As mentioned in the Operational Policy Note, the completion of the grant closure process confirms that the Principal Recipient does not have any residual financial liabilities to the Global Fund under the grant agreement, and in particular that:

- grant objectives have been met;
- unspent cash held at the country level is reimbursed to the Global Fund or transferred to next grant under consolidation;
- recoverable amounts identified through audit processes are tracked and funds refunded to the Global Fund;
- unused funds are de-committed to make them available for other Global Fund programs;

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<sup>5</sup>In annual individual performance objectives.

<sup>6</sup>In the Country team responsibility matrix from 2013, currently being revised.

<sup>7</sup>As per Section 27 and 28 of the Operational Policy Note issued on 18 December 2014.

<sup>8</sup>Source: Grant Report Detailed run from Global Fund System

- assets are held by grantees or transferred as directed by Global Fund to other entities for continued use to fight the three diseases.

During this review, the OIG noted weaknesses in the financial system and the controls related to grant closure. In particular, a grant can be classified as administratively closed in the system, even when recoveries are expected. This may result in inadequate recovery follow-up process by country teams. For example:

1. Two out of seven “administratively closed” grants tested had recoveries due of US\$438,175 and EUR187,895.
2. All eight grants tested that were classified as financially closed did not have sufficient documentation to demonstrate that all unspent cash held at the country level had been received. This was because the final bank statements had not yet been received by the Country Team.

Furthermore, the auditors noted that the grant naming conventions under the new funding model are obfuscated. Grant numbers remain unchanged across different grant cycles yet grant finance administration systems are only able to retain one status for all grants that use the same name. As such the country teams cannot accurately track the status of previous implementation periods and ensure their timely closure.

As previously raised in the 2013 OIG Annual Report and various past audit reports, weaknesses were identified in the quality and completeness of grant data stored on country teams internal documentation sites.<sup>9</sup> Of the 28 grant-related SharePoint sites reviewed, 15 sites had incomplete and/or outdated information to support the grant closure process. For the remaining 13 grants reviewed, the country teams had obtained waivers for the documentation requirements as closure was long overdue. As a result, the OIG could not assess the documents for completeness.

**Agreed management action 1**

Grant Management and Finance will track status of grant closures including refunds and grant cash balances on an ongoing, portfolio wide basis, and report regularly to the teams and management as required.

**Owner:** Head, Grant Management Division, Chief Financial Officer, Finance Information Technology Sourcing and Administration Division

**Target date:** 30 April 2017

**Agreed management action 2**

The Secretariat’s financial reporting requirements for implementers will be revised to include cash balance reporting and recoveries at the end of the grant closure period, to ensure compliance with grant closure requirements before administratively closing a grant. This will be done through updated operational policy notes that will be operationalized through “Accelerated Integrated Management”, the ongoing information systems project of the Secretariat expected to be completed by 2017.

**Owner:** Chief Financial Officer, Finance Information Technology Sourcing and Administration Division, Head, Grant Management Division

**Target date:** 30 September 2017

<sup>9</sup> BM31\_11-OIGAnnualReport2013\_Report, 14-003 High-Level Audit of the Global Fund Information Technology Systems and Processes and GF-OIG-15-020-Effectiveness of IT controls at the Global Fund.

### **03. There is no specific guidance over asset management and asset transfers.**

The 2013 audit noted that one of the challenges in closing grants is managing the assets remaining at the end of a grant. Since its creation, the Global Fund has financed approximately US\$1.6bn of assets which is 6.6% of total Global Fund grant expenditures.<sup>10</sup>

According to the Global Fund grant regulations, recipients have property titles for the assets during and after the grant period. However, as per the Global Fund Grant Agreement, recipients are required to ensure the continued use of assets procured from the Global Fund grants for the three diseases. For this purpose, the Secretariat requires the submission of a list of all assets procured with grant funds as part of the grant closure requirements. Although grantees are required to maintain asset listings throughout the grant period, this issue is only highlighted by the Country Team at the time of grant closure, and results in grant closure delays.

The OIG found that there are no policies or guidelines relating to materiality thresholds for reporting on assets, meaning that the process is cumbersome and does not generate value compared to the effort involved. Policies in place do not provide detailed guidance on the need for asset verifications by the Local Fund Agents, the form and content of the asset records, custodianship of assets and the controls for ensuring the completeness of asset listings. This means that the requirement for an asset listing is applied inconsistently by different grant recipients across different portfolios. Out of 10 closed grants sampled and tested during this audit, the OIG noted that asset records were missing or incomplete for five grants (50%). Without complete asset listings, it is not possible to assess the materiality of missing assets records for these specific grants.

The control gaps highlighted lead to weak controls over the beneficial use of all assets financed from Global Fund grants, and make them susceptible to misuse, misappropriation and embezzlement. For example, one grant tested had assets worth US\$367,293 procured which were kept in storage for up to four years after the end of the grant. This is an inefficient use of grant funds. Furthermore, there is a risk of financing of assets already purchased in a previous grant, particularly in the case of material, health-related assets, e.g. testing machines and laboratory equipment.

#### **Agreed management action 3:**

Grant Management will ensure that a risk based approach is defined and implemented for recording, utilization and transfer or disposal of assets (particularly for those with a long useful life and including but not limited to infrastructure and other equipment). This approach will be embedded into ongoing grant management procedures through additional guidance given to Country Teams to ensure effective asset management for all material assets procured through the Global Fund grants.

**Owner:** Chief Financial Officer, Finance Information Technology Sourcing and Administration Division; Head, Grant Management Division

**Target date:** 31 March 2017

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<sup>10</sup> Source: EFR report "Infrastructure and other equipment category" received from Grant Finance on 14 March 2016. 6,56% for expenditure, 6,67% for budgets

# Annex A: Status of the Previous Agreed Management Actions

## Recommendation 1

<p>The Secretariat should, as a matter of priority, close all long-outstanding grants, particularly those due for closure prior to 2012. Consideration should be given to:</p> <ul style="list-style-type: none"> <li>• Simplifying the closure process for long-outstanding grant closures, e.g., by limiting the process to: (i) clearance of commitments, (ii) confirmation and recovery of cash balances at PR and lower levels, and (iii) approving disposal of assets; and</li> <li>• Setting up a one-time task force to support Country Teams in reducing the backlog in grant closure.</li> </ul>	
<p><b>Owner:</b> Operational Policy and Process Support Team</p>	<p><b>Target date:</b> 31 December 2013</p>
<p><b>Status:</b> <b>Partially completed</b> – 32 long outstanding grants due for closure prior to 2012 are still overdue for closure. This has been incorporated in Agreed Management Action 1 in this report.</p>	

## Recommendation 2

<p>The Grant Management and Finance divisions should jointly review and identify areas for simplification in the grant closure process. Proposed changes should be embedded in the Finance “Step-Up” project and other grant management systems platforms such as Salesforce. Areas that should be considered for revision include:</p> <ul style="list-style-type: none"> <li>• The rationale for preparing close-out plans and budgets, if necessary redefining the contents of the close-out plan;</li> <li>• The number of independent closure activities undertaken (consider including only critical ones to reduce the resources required);</li> <li>• The number of separate reports required; and</li> <li>• The requirement for multiple layers of review.</li> </ul>	
<p><b>Owner:</b> Operational Policy and Process Support Team and NFM Transition Team &amp; Finance</p>	<p><b>Target date:</b> 31 December 2013</p>
<p><b>Status:</b> <b>Completed;</b> The Operational Policy Note has identified areas for simplification of the grant closure process and allows the Country teams to exercise flexibility in implementation within the operating principles.</p>	

## Recommendation 3

<p>While streamlining the grant closure process, consideration should be given to the following areas to strengthen the grant closure processes:</p> <ul style="list-style-type: none"> <li>• Prioritizing the identification and collection of cash held at country level and the de-commitment of unused funds. These processes should be integrated and follow the final closure of grants;</li> <li>• Developing specific terms of reference for close-out audits to provide assurance on matters critical to the grant closure process;</li> <li>• Setting firm deadlines for specific steps; and</li> <li>• Documenting principles to guide the process for unanticipated closures or closures with special circumstances and giving country teams the discretion to adapt the process to suit unique circumstances.</li> </ul>	
<p><b>Owner:</b> Operational Policy and Process Support Team</p>	<p><b>Target date:</b> 31 December 2013</p>
<p><b>Status:</b> <b>Completed;</b> The grant closure policy was updated and issued on 18 December 2014. Furthermore, a revised <i>Progress Update Disbursement Request</i> (PUDR) template was issued in January 2016 to better track cash balances held by the Principal Recipients and Sub-Recipients, for new implementation periods on ongoing grants. These have addressed the risks raised in this recommendation and the gaps noted in implementation for the older grants have been included in this report and agreed management actions.</p>	

#### Recommendation 4

<p>The Secretariat should enforce compliance with laid down processes by:</p> <ul style="list-style-type: none"><li>• Instituting controls through the Finance Step-Up project and other grant management systems such as Salesforce; and facilitating the provision of critical information for the regular monitoring of grant closure status; and</li><li>• Considering and implementing appropriate incentives to prioritize closure (e.g., by tying the final disbursement to the completion of grant closure activities determined to be critical by the Secretariat).</li></ul>	
<p><b>Owner:</b> Operational Policy and Process Support Team and NFM Transition Team &amp; Finance</p>	<p><b>Target date:</b> 31 December 2013</p>
<p><b>Status:</b> <b>Partially completed</b>; The Global Fund System has been implemented to facilitate the provision of critical finance information for monitoring the grant closure status. There are currently no incentives in place to prioritize closure.</p>	

## Annex B: General Audit Rating Classification

<b>Effective</b>	<b>No issues or few minor issues noted.</b> Internal controls, governance and risk management processes are adequately designed, consistently well implemented, and effective to provide reasonable assurance that the objectives will be met.
<b>Partially Effective</b>	<b>Moderate issues noted.</b> Internal controls, governance and risk management practices are adequately designed, generally well implemented, but one or a limited number of issues were identified that may present a moderate risk to the achievement of the objectives.
<b>Needs significant improvement</b>	<b>One or few significant issues noted.</b> Internal controls, governance and risk management practices have some weaknesses in design or operating effectiveness such that, until they are addressed, there is not yet reasonable assurance that the objectives are likely to be met.
<b>Ineffective</b>	<b>Multiple significant and/or (a) material issue(s) noted.</b> Internal controls, governance and risk management processes are not adequately designed and/or are not generally effective. The nature of these issues is such that the achievement of objectives is seriously compromised.

## Annex C: Methodology

The Office of the Inspector General (OIG) performs its audits in accordance with the global Institute of Internal Auditors' (IIA) definition of internal auditing, international standards for the professional practice of internal auditing (Standards) and code of ethics. These Standards help ensure the quality and professionalism of the OIG's work.

The principles and details of the OIG's audit approach are described in its Charter, Audit Manual, Code of Conduct and specific terms of reference for each engagement. These help the OIG auditors to deliver high quality professional work, and to operate efficiently and effectively. They also help safeguard the independence of the OIG's auditors and the integrity of their work. The OIG's Audit Manual contains detailed instructions for carrying out its audits, in line with the appropriate Standards and expected quality.

The scope of OIG follow-up reviews may be limited, with focus on high risk areas identified in the previous audit, or broad depending on the context, covering risk management, governance and internal controls. Follow-up reviews test and evaluate supervisory and control systems to determine whether risks have been addressed appropriately.