



Investing in our future

The Global Fund

To Fight AIDS, Tuberculosis and Malaria

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For Information

THE GLOBAL FUND SECRETARIAT RESPONSE TO THE OIG PROGRESS REPORT

Purpose:

This paper provides a comprehensive response to the issues raised in the latest OIG Progress Report (GF/B23/10) as requested by the Finance and Audit Committee at its 16th Meeting.

1. INTRODUCTION

1.1 In order to give the Board members and other stakeholders a periodic and complete overview on issues raised and actions taken arising from OIG work, the FAC has requested that the OIG and Global Fund Secretariat report jointly.

1.2 The OIG prefers to report separately (GF/B23/10). Therefore this paper references the OIG findings and gives a detailed response from the Global Fund Secretariat.

1.3 The paper includes three sections:

- i. Preamble and background
- ii. Response to issues raised in the OIG Progress Report
- iii. Conclusion

1.4 Attachment 1 to this paper “**Results with Integrity**” describes in further detail, the Global Fund’s forward-looking response to fraud.

2. PREAMBLE AND BACKGROUND

2.1 When the Global Fund was established, it took into account lessons learned from 40 years of development experience to create a system based on country ownership, performance-based funding, transparency and accountability. These four principles were considered the best way to ensure efficiency, results, ownership and sustainability.

2.2 Working in partnership with 325 Principal Recipients and more than 3,000 sub-recipients across 145 countries the Global Fund has disbursed more than US\$ 13 billion for lifesaving programs. Global Fund financing has contributed significantly to major successes against the three diseases during the past decade.

2.3 The Global Fund, by very nature of its mandate, works in countries and environments which present high levels of risk. It works in countries where often programmatic and oversight capacities are weak, or where financial controls are inadequate, those commonly defined as “fragile” states.

2.4 Along with its commitment to transparency, the Global Fund has had, from the beginning, an uncompromising attitude toward misuse of funds. The focus on transparency and accountability led to a structure which includes six layers of programmatic and fiduciary controls (see page 4 of Attachment 1, Results with Integrity).

2.5 The Global Fund Secretariat greatly appreciates the work of the OIG in identifying areas to strengthen the model, and will continue to maintain a zero tolerance approach to fraud.

2.6 Instances of suspected or confirmed fraud have received a swift and determined response, with programs suspended or terminated in a number of countries, and we are pursuing the recovery of misspent funds.

2.7 Over the last year, the Global Fund has been reinforcing its fraud detection and risk-management processes, with particular attention to the role of Local Fund Agents and fraud-prone activities at the country level. The Global Fund continues to evolve and improve the way it anticipates and mitigates risk to ensure that its funding continues to reach its intended beneficiaries.

2.8 The Office of the Inspector General has launched an ambitious program to audit the Global Fund portfolio over the past few years and there are a large number of audits and investigations in the pipeline. As these inquiries - some covering periods as far back as 2003 - are completed, the share of the Global Fund portfolio which has been audited will have increased significantly, and undoubtedly, so will the cumulative losses. If the amounts reviewed by the OIG double, the amount of losses identified may also double. As a result, we can get a better picture of what losses have been incurred in the past decade.

2.9 However, based on experience gained and lessons learned so far, the Global Fund Secretariat has for more than a year put in place a more robust and timely mitigation response to problems that arise, as well as enhancing systems to prevent losses in the first place. While there is little more that can be done for losses incurred in the past, other than to assist the OIG to identify them and actively pursue recoveries of these losses, the Global Fund will endeavour to ensure that donor funds are used efficiently and effectively, and that the results that are expected, are the results that are achieved. In line with this approach, The Global Fund Secretariat looks forward to receiving the findings of the High Level Panel, which will conduct an independent review of the Global Fund's fiduciary mechanisms in the coming months.

3 RESPONSE TO ISSUES RAISED IN OIG PROGRESS REPORT

3.1 The structure of this section includes a reference to the relevant paragraphs of the OIG Progress Report (GF/B23/10) followed by a response from the Global Fund Secretariat to the key issues raised.

Misleading Media Coverage (Ref. GF/B23/10 paragraph 2.1 - 2.4)

3.2 The Global Fund Secretariat complained to the Associated Press (AP) about its 23 January 2011 inaccurate story and AP did acknowledge that it had rushed the story out without sufficient quality control. The Global Fund Secretariat has strengthened its crisis communication protocols and contracted additional outside counsel on crisis communication. It should be noted that a further misleading article on the Global Fund and drug theft was published by the AP on 21 April, and later corrected by the news agency.

3.3 In the face of persistent demands by media, donors and other stakeholders for a measure of the magnitude of the corruption problem, the following response had been used in some cases:

“Audits and investigations in 33 countries are in progress or have been completed and while these 33 countries represent a significant portion of our portfolio, the Global Fund cannot at this stage determine or estimate the scale of fraud among the totality of its supported programs. However, we do know that, for the 11 countries where audits or investigations have been publicly reported, we are so far demanding US\$44 million in losses to be repaid. This represents 0.3 percent of total money disbursed to date.”

3.4 Considering the recent discussions at the 16th FAC meeting on the need to work with the OIG to find a suitable denominator for FAC consideration, the Global Fund Secretariat is not, and will not be making reference to the 0.3 percent figure as an appropriate denominator.

3.5 The media attention and the subsequent actions and statements by donors and other stakeholders provide a number of lessons. The overall conclusion is that while there should be no reduction in The Global Fund's commitment to its current levels of transparency, a more disciplined and proactive approach to transparency needs to be developed with the OIG. Among the changes to be considered may be:

- i. a more systematic reporting system;
- ii. a shift in updates on numbers from cumulative to annual figures;
- iii. an agreed policy on sharing of draft reports for review and briefing of external partners during the course of investigations;
- iv. the inclusion of a summary of Global Fund Secretariat actions to be published alongside or as part of any report;
- v. proactive announcements by the Secretariat on actions to safeguard assets where appropriate whenever the Secretariat deems the Global Fund's assets to be at risk;
- vi. a comprehensive communications strategy to educate the public on the nature of the Global Fund's fiduciary controls, its transparency policy and the scale and context of the issues of losses and misuse to build an acceptance for the Global Fund's approach to these issues;
- vii. collaboration with other development partners on reporting and discussion of losses, risk, safeguards, controls and the overall benefits of investments for health.

Extent of the problem and communicating the extent of the problem (Ref. GF/B23/10 paragraph 2.5 - 2.18)

3.6 The Global Fund Secretariat is fully committed to working with the OIG and the FAC, to transparently and accurately report on losses identified through the work of the OIG, and to ensure that these figures are consistently presented in an appropriate context. In line with this transparent approach, the additions to the OIG Table of losses which were discussed are presented in more detail below:

- i. **Zimbabwe:** The OIG's Zimbabwe report was issued in March 2009 (TGF-OIG-08-004) and describes a situation where the Reserve Bank of Zimbabwe (RBZ) withheld all foreign currency for all entities operating in the country. The amount affecting the Global Fund was US\$7.56 million, which was later released by the RBZ back to the PRs.
- ii. **India:** An on-going investigation in India has identified US \$1.07 million in ineligible expenses. This investigation is still on-going.
- iii. **Nepal:** A follow-up audit to a previous OIG audit of Nepal is with the OIG for finalization. The FAC thus far has not been informed of any issue or identified misuse of funds.
- iv. **Denominator/comparator:** The OIG wanted to include two new columns in the table of losses indicating the amounts disbursed and the amounts reviewed as figures against which the total amount of misuse could be compared. The FAC has asked the OIG and the Secretariat to present a proposal on what denominator would be most appropriate to the FAC at the May 9 meeting. At this meeting the proposal from the Comprehensive Reform Working Group will also be discussed.

3.7 The table on the next page is the one presented initially to the FAC and in GF/B23/10. The Chair of the FAC communicated his approach to this matter on April 29 2011 in the following communication:

- i. "The original table as presented to the FAC (i.e.: without Zimbabwe, India, Nepal and without the additional columns showing amounts disbursed and amounts reviewed") should be included in any Board papers (OIG Progress Report and Secretariat Response to OIG Matters) that are being sent out now. It can be entitled "Table of losses as presented to FAC in March 2011".

- ii. At the May 9 FAC meeting the OIG and Secretariat should present a (possibly revised) table on which they agree. If there are remaining disagreements on the inclusion or exclusion of numbers, each side should present their reasons for doing so in writing to FAC.
- iii. At the meeting on May 9 the FAC will decide if any revised numbers should subsequently be presented to the Board in the briefing or Board sessions.”

Table 1: Misuse of funds as reported to the FAC (March 2011)

Country (or PR)	Fraud (US\$)	Unsupported (US\$)	Ineligible (US\$)	Unaccounted Income/drugs	Other (US\$)	TOTAL (US\$)
Uganda ¹	-	-	-	-	1,600,000	1,600,000
Mali	4,074,444	1,034,935	-	-	122,106	5,231,485
Djibouti ²	145,893	4,262,288	857,827	-	-	5,266,008
Mauritania ²	6,755,000	-	-	-	-	6,755,000
Cambodia ²	-	222,706	-	1,362,466	-	1,585,172
Cameroon	33,455	2,199,530	3,370,322 ³	-	-	5,603,307
Zambia ²	13,000	5,808,446	4,998,389	-	-	10,819,835
Tanzania	-	-	-	819,000	-	819,000
Haiti	-	519,326	1,253,869	704,730	-	2,477,925
DRC ⁴	-	1,110,107	933,586	-	-	2,043,693
Philippines	-	-	2,021,280	-	-	2,021,280
Rwanda	-	-	-	-	-	-
Total (US\$)	11,021,792	15,157,338	13,435,273	2,886,196	1,722,106	44,222,705

3.8 63 percent of the total amount misused is related to Mauritania, Mali, Djibouti and Zambia. In response to these particular cases of fraud, the Global Fund has taken swift and context-specific action:

¹ The amount is based on recommendations in the Ugandan Government White Paper endorsed in November 2006 for refunds amounting to Ushs 2,745,143,224 which approximates to US\$ 1.6m. The OIG has been supporting on-going investigations in a number of cases.

² The OIG is in the process of conducting on-going investigations of fraudulent activities in these countries. As these investigations are still on-going, we are unable to fully quantify the amounts involved. But we are of the opinion that the amount of reported fraud will increase following the outcome.

³ As documented in paragraph 115 of the OIG Cameroon country audit report dated 5 October 2010, this amount relates to overpayments as a result of over-billing by a procurement agency.

⁴ Due to recent and on-going OIG investigations, please note that the amount of discovered fraud in the DRC has now increased by approximately US\$ 1.75m which has not been reflected in the amounts above.

- i. Relevant grants in Mali, Mauritania, and Zambia were suspended in December 2010, September 2009 and August 2009 respectively⁵, with disbursements, expenditures and activities frozen until further notice, and only lifesaving treatment allowed to continue;
- ii. One malaria grant was terminated and two TB grants were suspended in Mali in late 2010. A further suspension of an HIV grant was announced in February 2011;
- iii. Djibouti, Mauritania and Mali, among other countries⁶, have been placed on the Global Fund's list of "Additional Safeguards" countries, allowing for increased direct scrutiny of activities at the Principal Recipient and sub-recipient levels;
- iv. Evidence has been provided to local authorities in Mali, Mauritania and Zambia in support of criminal investigations⁷.

Rwanda Audit Report (Ref. GF/B23/10 paragraph 3.1 - 3.2)

3.9 As noted by the OIG, the Global Fund programs in Rwanda have shown impressive achievements. Strong CCM oversight and the active engagement of partners have contributed to the achievements recorded to date. As noted by the OIG, many best practices which other countries can learn from were observed. Notwithstanding the considerable program achievement and results, the OIG noted some weaknesses in the financial management capacity of sub-recipients as well as the Project Management Unit's ability to provide an appropriate level of oversight of sub-recipients. Concrete measures to strengthen the identified weaknesses have been put in place, and the benefits of these measures are progressively helping financial and program performance.

Results Achieved (Ref. GF/B23/10 paragraph 3.3)

3.10 It is of utmost importance that the reported results of the Global Fund can be relied upon. The key initiatives used to support data quality include:

- i. On-Site Data Verification (OSDV) - The LFA in 2010 conducted 365 on-site verifications of program data.
- ii. Data Quality Audits (DQA) - The DQA tool and methodology (1) assesses the ability of M&E systems to collect and report quality data and (2) verifies the accuracy of reported data for key indicators at selected sites. On average, 15 to 20 selected grants undergo DQA every year.
- iii. M&E Self Assessments - 85% of disease programs supported by the Global Fund have undergone a self-assessment since 2006.
- iv. M&E Plans - There has been a continuous increase in the number of national M&E Plans prepared, and a continuous improvement has been identified in the quality of M&E plans

3.11 M&E system strengthening measures are followed up by the Secretariat. M&E gaps and strengthening measures identified through M&E self-assessments, LFA PR assessments, OSDVs, DQAs, and OIG processes are consolidated by GF M&E officers, agreed by Country Teams and communicated by the FPM to the PR (through management letters). Then, as part of the Progress Update/Disbursement Request (PU/DR), the PR provides updates on progress made on implementation of the M&E recommendations/strengthening measures.

3.12 The Global Fund results are based on data reported from programs we support using their M&E systems. These results undergo several internal and external checks, at each stage of the grant lifecycle, and data are then compared to results from partner systems before they are released twice per year.

⁵ The Global Fund has also suspended or frozen grants in Ukraine, Uganda, Chad and the Philippines.

⁶ Papua New Guinea and Côte d'Ivoire were also added to the list because of weak financial management systems making them vulnerable to misuse.

⁷ More than 20 arrests have been made by authorities in Mali, Mauritania and Zambia, including of senior officials.

3.13 The Global Fund's approach to data quality is described in detail in the "Results with Integrity" Report (section 5, page 13) which is an attachment to this document.

Procurement and Supply Management (PSM) (Ref. GF/B23/10 paragraph 3.4)

3.14 A number of measures are underway as part of the reform agenda to strengthen procurement processes:

Strengthening of Procurement Information of Pharmaceutical and Health Products

- i. Introduction of a new integrated system to track procurement information.
- ii. A new IT solution for Price and Quality Reporting (PQR) to produce regular online reports for countries.
- iii. Use of PQR data and new performance ratio for health products as part of the performance evaluation at Phase 2 and Periodic Reviews.
- iv. Development of robust early warning system to prevent stock outs of key health products.

Strengthened Quality Assurance for health products

- v. Instruction to Local Fund Agents (LFAs) to verify that PRs are complying with the requirements for quality control testing of pharmaceutical products.
- vi. Implementation of a new QA policy for diagnostics.
- vii. Enhance Expert Review Panel (ERP) process in order to improve risk benefit assessment of pharmaceutical products and identify additional quality sources.
- viii. Assessing the level of implementation of QA policy for pharmaceutical and health products at the time of grant renewals.

Voluntary Pooled Procurement (VPP)

- ix. Improving grant performance through addressing procurement-related bottlenecks.
- x. Through strategic intervention in market place and by pooling of procurement, impact market dynamics to significantly improve price, availability and market sustainability of ARVs, ACTs, and LLINs.
- xi. Implement strategic interventions on procurement of first-line, second-line and paediatric ARVs to further impact on Market dynamics and assure access to medicines.
- xii. Introducing the VPP as a risk mitigation measure for high risk countries for fraud and prevention of stock-outs.

Capacity Building Services

- xiii. Introduction of a systematic process for PSM Capacity building as part of grant management, including the increased use of technical partners
- xiv. Introduction of a mechanism for budgeting and targeting adequate grant funding towards strengthening in-country PSM

Strengthening Pharmaceutical and Health Product Management

- xv. Introduction of the use of Country Profiles in Proposal life cycle as a tool for assessing PSM policies, systems and structures, in order to identify weaknesses to be addressed in program implementation, improve efficiencies of systems, simplify and accelerate grant signing process, leverage support from other partners/donors.

- xvi. Secretariat reviews all PSM Plans for health products under each grant, ensuring that products are selected in line with National/WHO Treatment Guidelines, that quantities are adequate to achieve agreed patient targets and that unit costs are budgeted in line with international reference price and to ensure that adequate systems are built in all its recipient countries for fair, competitive and transparent procurement procedures.
- xvii. The information gathered through the PQR system enables the Global Fund to review procurement performance in grants, and to understand and apply its leverage in the market for buying medicines and other health products to obtain better value for money. It also enables the Global Fund Secretariat to monitor compliance of purchased products with the Global Fund's quality assurance policies, and to apply corrective measures in case of non-compliance.
- xviii. Implementation of the Country Team Approach, to facilitate grant management and grant recipients' interactions with all relevant units in the Global Fund Secretariat (Pharmaceutical Management, Country Programs, Legal, Finance, Monitoring & Evaluation, Performance Impact Effectiveness(PIE), and Partnerships)
- xix. The rolling out of the Country Coordinating Mechanism (CCM) "dashboard" that improves the CCM's role in grant oversight in procurement
- xx. Engage LFA PSM Experts through training workshops, meetings and introduction of updated tools/guidelines on Global Fund requirements for quality PSM assessments, and share lessons learnt and best practices from Pharmaceutical and Health Products Management (PHPM) assessments.

Cash Based Expenditure (Ref. GF/B23/10 paragraph 3.5)

3.15 Recognizing the risk posed by cash-based transaction, the Global Fund Secretariat is taking a number of actions to reduce the likelihood of fraud in relation to these activities:

- i. As discussed in the "Results with Integrity" report, in December 2010 the Global Fund, in consultation with partners and implementers, requested Principal Recipients around the world to submit detailed annual training plans; training activities which do not comply with approved training plans will no longer be eligible for Global Fund funding. Additionally, Local Fund Agent verifications and scrutiny of training activities have been enhanced to include, inter alia, spot-checks and routine verifications of participant-lists;
- ii. As part of the reforms underway in the Global Fund, the Secretariat is currently considering the implementation of integrated financial management systems for all PRs/SRs on budgeting, accounting, assets management and reporting (as of Round10); this should significantly enhance the Global Fund's capacity to monitor country-level activities and expenditures;
- iii. Given the environments in which the Global Fund operates, a blanket prohibition of cash expenditures would not, at this point in time, be feasible. The use of checks and other non-cash means has been discussed with the Office of the Inspector General in the recent past, and moving forward, this approach will be implemented whenever possible.
- iv. Finally, the Global Fund's current push towards improving fiduciary controls at PR and SR level are specifically aimed at strengthening their financial management and internal control systems and mechanisms to transparently track the efficient use of grant funds and increasing the frequency and depth of *verification exercises*. The PRs/SRs will be allowed to reprogram grant funds to quickly implement those measures. LFAs will be asked to do regular spot checks of SRs and high risk activities based on prior Country and PR risk assessment. These will come into effect in 2011.

Record Keeping, Accounting, Co-Mingling of Funds (Ref. GF/B23/10 paragraph 3.6 - 3.7)

3.16 The Global Fund requires Principal Recipients to meet the minimum standards established by the Global Fund for financial management, which includes the requirement to have an effective accounting system in place.

3.17 The LFA assessment of the Principal Recipients' capacity to manage the grant will document any instances where aspects of financial management, including accounting systems have significant weaknesses. In such cases, depending on the scale of the weakness, the Secretariat may:

- i. **Reject the CCM nominated PR:** Where the deficiencies identified are considered to pose significant risks and delays in the management and implementation of the grant.
- ii. **Accept the CCM nominated PR:** Where there is evidence that the risks posed by the weaknesses (or gaps) in the accounting system are manageable within a reasonable period of time (i.e. within 6 months). In this case, the Secretariat works with the PR and LFA in developing appropriate mitigating measures to safeguard grant funds. This can include the reallocation of savings for capacity building.
- iii. **Propose the use of a Fiduciary Agent:** Where the Secretariat feels that the risks cannot be mitigated within a reasonable period and depending on the size and complexity of the grant/PR. In this case, the entire financial and accounting function may be contracted to a Fiduciary Agent (usually independent accounting firms). The Secretariat reviews the Terms of Reference (TOR) for the Fiduciary Agent to ensure that it incorporates the core competencies required and transfer of competence to the PR within a reasonable period of time.

3.18 In applying the options above, the Global Fund Secretariat as part of the mitigating measures may include Conditions Precedent (before disbursement of funds or second disbursement of funds) or Special Conditions (by a specific date, or conditions in place over a certain period) which describes certain actions that the PR must take to address the areas of concern. These conditions form part of the Grant Agreement and non-compliance is taken seriously by the Global Fund Secretariat.

3.19 In moving forward, and taking into account the concerns raised by the OIG, the Secretariat is currently considering revising the minimum acceptable standards for financial management and accounting systems.

3.20 With respect to the co-mingling of funds, and in line with Global Fund policy on common funding mechanisms, the Secretariat uses a risk-based approach in accepting to manage grants in this manner. PRs must ensure that mechanisms and systems are in place to properly identify and provide an accurate status of Global Fund income/expenditures and cash balances at all times. However, taking into account the OIG experience, the Secretariat will strengthen the LFA assessment and verifications to provide greater assurance that the PRs can satisfy the requirements at the time of assessment and during implementation. Where they cannot, the use of common bank accounts will be prohibited.

Lack of cooperation with OIG audits and investigations (Ref. GF/B23/10 paragraph 3.8 - 3.9)

3.21 It is critical for the success of the Global Fund's mission that the Secretariat and OIG speak in countries with one voice. Every time the Inspector General has identified serious issues at country level, the Secretariat has taken swift and determined action including termination or suspension of grants, replacement of PRs and LFAs, or the placement of the country on the Additional Safeguards Policy list. The Secretariat further sets strict conditions for the resumption of suspended or frozen programs, including repayment of misspent funds.

3.22 The Global Fund Secretariat is in no way opposed to including language on in-country commitment to cooperate with the OIG. While the Global Fund Secretariat agrees with many of the points raised by the Inspector General, it also believes that the strict conditioning of continued activities to country-level cooperation with the Inspector General needs to be decided upon on a contextual, country-by-country basis.

LFA (Ref. GF/B23/10 paragraph 3.10 - 3.11)

3.23 Although part of the normal LFA scope of work, the Global Fund Secretariat, OIG and LFAs agree that LFAs have not been sufficiently focused on the identification of fraud and financial mismanagement and that the LFA role is to be strengthened. The findings and recommendations from the Inspector General⁸ are helping to re-shape the role of Local Fund Agents.

3.24 It should be noted that:

- i. Since November 2010, i.e.: in the past 6 months, 47 instances of inappropriate expenditures have been reported to the OIG by the Secretariat, of which 18 cases originated with LFAs.
- ii. The OIG confirms that the referral of alleged cases of fraud/mismanagement by LFAs has increased.

3.25 The Global Fund is taking action when LFAs are underperforming. Through its rigorous performance evaluation system, the Global Fund has re-tendered 15 LFA contracts since January 2009. This amounts to 11% of all LFA contracts. Another 6 LFAs are on a performance plan/probation period.

3.26 As part of the reform program already started in 2010, the Global Fund is strengthening the LFAs' scope of work to focus even more on identifying fraud risks and actual fraud in Global Fund programs, at the PR and SR levels. The Global Fund Secretariat and the Local Fund Agents are taking a more rigorous and systematic approach to risk management, including fraud prevention. Details of these measures are described in the "Results with Integrity" report which is Attachment 1 of this report.

Financial Controls (Ref. GF/B23/10 paragraph 3.12 - 3.13)

3.27 As an overarching principle in the reform agenda, grant management approaches are more tailored to the specific risk profile of the concerned country, for example:

- i. through application of country team approach to higher risk countries
- ii. through tailoring of LFA scope of work for greater scrutiny of implementers and sub-recipients in accordance with identified risks
- iii. through stricter fiduciary control of high risk expenditures
- iv. through application of additional safeguard policies where appropriate

3.28 Risk management is the central theme in Global Fund grant making processes, and the reform agenda seeks to identify any process along the grant life-cycle where risk management can be strengthened in a way that applies Global Fund core principles while increasing efficiency and effectiveness. One example is the application of stricter standards to the use of conditions precedent at grant signing.

3.29 A new KPI on value for money has been introduced, with reporting for the first time in Quarter 1 of 2011.

⁸See for example the OIG Report on Lessons Learned from the Country Audits www.theglobalfund.org/en/oig/reports/?lang=en

3.30 In-depth capacity assessments of PRs are conducted by LFAs and minimum acceptable capacity standards are applied. LFAs are being managed more closely to ensure the robustness of the capacity assessment.

3.31 Conditions to disbursements may be placed in the grant agreement to ensure that weaknesses are addressed prior to disbursements. These conditions are established on a grant by grant basis taking the country and program environment into consideration. As part of the reform agenda, the standards for the use of conditions precedent during signing are being strengthened

3.32 The reform agenda does include an initiative focused on stronger compliance of recipients with existing policies for fiduciary control, including in high risk program activities and expenditures such as trainings, health and non-health procurement, vehicle purchase and others. A retrospective review of the current program budgets is under way as part of this initiative.

Oversight Mechanisms - CCM (Ref. GF/B23/10 paragraph 3.14)

3.33 It is important to emphasize that CCMs are responsible for strategic oversight of PRs and their progress with grants, but that this responsibility does not extend to identifying fraud. With that in view, the Global Fund recommends that annual grant audits be systematically integrated into the set of information CCMs use to provide oversight. In instances of identified fraud—and this needs to be clearly stated as such within the audit report, CCMs would be expected to seek further clarifications from auditors and PRs to take remedial actions, including replacing PRs that are deemed to be directly implicated and/or contributing to the problem.

3.34 As part of the CCM funding policy, actions are already underway to strengthen CCMs. These include establishing a performance-based framework with a particular emphasis on oversight. Once in place, the Global Fund Secretariat should be better positioned to appraise CCMs' strengths and weaknesses and facilitate targeted support where necessary. The new CCM Guidelines, to be presented to the Board for approval at its Twenty-Third meeting, reinforce requirements around the disclosure and mitigation of conflicts of interest.

Mali Investigation (Ref. GF/B23/10 paragraph 3.15 - 3.32)

3.35 The Global Fund Secretariat thanks the OIG for the impressive work undertaken with this investigation.

3.36 In reaction to early information from the OIG, the Global Fund Secretariat terminated, in December 2010, a Tuberculosis grant to the Mali Ministry of Health, while ensuring the continuation of treatment for those thirteen patients under treatment at the time of suspension. At the same time, two Malaria grants (to the Ministry of Health and the non-governmental organization "Groupe Pivot") were suspended. Alternative implementation arrangements - under a new Principal Recipient - were identified and are currently under negotiation.

3.37 At the time of termination (TB) and suspension (Malaria), the procedures in the "Additional Safeguards Policy" were invoked by the Executive Director. In essence, this makes any material managerial decision regarding Global Fund programs in Mali subject to the Global Fund Secretariat's approval, thereby intensifying fiduciary control.

3.38 Once the OIG and the responsible entities in Mali have agreed on a final amount to be reimbursed, the Global Fund Secretariat will make every effort to recover the lost grant funds.

3.39 The OIG commends the LFA for its excellent cooperation with the OIG during the investigation and its increased vigilance. The Global Fund Secretariat will ensure that the current quality of LFA oversight is maintained in the future.

3.40 The Global Fund Secretariat notes the importance of the suspended Principal Recipients for the national response to Tuberculosis and Malaria, and will work, predominantly through partners, to ensure that these entities receive adequate technical assistance to enable them to resume responsibilities for grant management.

3.41 The Global Fund Secretariat will apply lessons learned from the investigation, when negotiating the grants from the approved Round 10 applications. Particular emphasis will be placed on increased scrutiny of cash-based transactions, training plans and other budget lines the OIG identified as particularly vulnerable to misuse.

Theft of Medicines (Ref. GF/B23/10 paragraph 3.33 - 3.36)

3.42 The Global Fund Secretariat and the Office of the Inspector General are at the forefront of the international response to drug theft, working with law enforcement, sister agencies, and drug manufacturers to investigate claims of theft⁹.

3.43 The Global Fund hosted a meeting of concerned stakeholders (the UN Secretary General Special Envoy for Malaria, the World Health Organization (WHO), the Joint United Nations Programme on HIV/AIDS (UNAIDS), the United States Agency for International Development (USAID)/the President's Malaria Initiative (PMI) & OIG, USG/PEPFAR, UNITAID, the GAVI Alliance, Stop TB Partnership, Roll Back Malaria, ALMA and UNICEF) in Geneva on 17 February 2011. The meeting was a first step in agreeing on an action plan to combat the theft and illegal diversion of medicines, a plan which includes such steps as information sharing among partner agencies, joint strengthening of procurement and distribution capacity in developing countries and the application of stringent measures around drug storage and transport.

3.44 Based on information gained from reported cases and ongoing investigations, a portion of these thefts appear to be well-organized, raising the need for concerted action. Long-term solutions to the issue lie in partnering with countries to build secure and sustainable supply chains so that products reach the intended end-users.

3.45 The Global Fund, in coordination with other donors, UN Agencies, grant implementers, drug manufacturers and law enforcement agencies, has embarked on implementing immediate and long-term measures, to address the problem of drug theft. These measures are outlined in more detail in the "Results with Integrity" report in Attachment 1.

3.46 As an immediate action, the Global Fund has identified 56 high risk countries for drug theft, where the LFA will be undertaking a closer assessment of Pharmaceutical Health Product Management (PHPM) risks, including the risk of drug thefts. These 56 countries collectively, accounted for over US\$ 2.1 billion in health product related expenditure as at the end of 2010. Arising from this work, the Global Fund Secretariat will collaborate with the PRs and other partners to develop action plans to mitigate the risks.

⁹ It is important to remember that the Global Fund deals with thousands of pharmacists, doctors and nurses around the world who work to ensure that the free or affordable drugs provided through Global Fund grants end up with the patients they were intended for.

Audit and Investigations Process (Ref. GF/B23/10 paragraph 4.3 - 4.4 and 4.7 - 4.12)

3.47 The Global Fund Secretariat recognizes the challenges faced by the OIG in completing their work. However the ability of the Global Fund Secretariat to sign grants, make disbursements and maintain effective working relationships with Partners is limited due to a lack of information which may be at the disposition of the OIG. We recognize that the sensitivity of this information means it cannot always be shared. Nevertheless, the length of time required to complete an audit, and more particularly an investigation, causes uncertainty.

3.48 While we commend the steps taken by the OIG to improve feedback to the in-country stakeholders, we remain concerned at the length of time take to complete audits and investigations and the continued challenges in sharing critical information which would assist with grant management.

3.49 The Secretariat OIG Working Group is currently preparing updated audit and investigation protocols, a communication protocol and a guidance note for managing grants during audits and investigations which aim at facilitating an improved cooperation between the OIG, the Global Fund and PRs/CCM.

Depth of Investigations (Ref. GF/B23/10 paragraph 4.5 - 4.6)

3.50 Issues around the depth of investigations were a matter which the FAC Sub-Committee on OIG matters discussed briefly at their 16th Meeting as captured in the report of the FAC Sub-Committee (GF/B23/12) and reproduced below:

5.2 In relation to the issue of depth of investigations, the Sub-Committee did not discuss this in any detail but believes this issue should be considered by the High Level Panel. Issues that the High Level Panel might wish to consider are:

- i. Whether it is required that the OIG work continue until court-ready information is prepared, or whether the OIG's work should stop earlier once the Global Fund understands the full scope of the issues. The latter course of action would imply turning over the investigation work to national authorities at an earlier stage than at present.
- ii. Whether handing over investigations at an earlier stage would restrict the ability to fully quantify the misuse of funds in an unacceptable way?
- iii. Whether the current approach to investigations is in line with best practice?

Audits by PRs and SRs (GF/B23/10 Ref. paragraph 4.13 - 4.15)

3.51 In relation to paragraph 4.13, the Grant Agreement requires PRs to notify the Global Fund Secretariat prior to undertaking audits into allegations of fraud. The Secretariat is in turn committed to ensuring that appropriate consultation with the OIG takes place in these instances.

3.52 In relation to paragraph 4.14, in November 2010, shortly after the introduction of the Country Team Approach for China, the Country Team held a meeting with the LFA to discuss the verification arrangements in view of (i) significant growth in value of the China portfolio (ii) the findings of the TRP-mandated external review, and (iii) the Global Fund's new operational policy requiring the LFA to undertake country risk assessments where warranted.

3.53 The Country Team requested the LFA to carry out a "risk analysis of the portfolio", and building on its results, determined that further verification work was warranted (particularly at Sub-Recipient and Sub-Sub-Recipient levels).

3.54 The Country Team, in line with normal day-to-day Secretariat work, requested the LFA to conduct a “financial management verification”:

- i. Financial management verification work is part of routine LFA work.
- ii. Tailoring the scope of the LFA work to the identified risks is the responsibility of the Country Team.
- iii. The Country Team had not been notified of any upcoming OIG audit when this work was being commissioned at the end of 2010; we have since become aware that the OIG intends to audit China in the third quarter of 2011.
- iv. In the absence of information on an upcoming audit or investigation, it is not normal practice (and would be prohibitively burdening both for the OIG and the Secretariat) to inform the OIG of upcoming LFA verifications, let alone to seek the OIG’s approval as suggested in the OIG’s Progress Report.
- v. The LFA was instructed to ensure that all documentation from the verification was retained in the event of any issues being identified which would require subsequent OIG involvement.
- vi. The OIG has been informed of the preliminary findings of the verification.

Recoveries (Ref. GF/B23/10 Missing Reference, view in-between paragraph 4.15 - 4.16)

3.55 The Secretariat has taken action to recover funds where there is evidence of misuse. So far a total of US \$7.6 million has either been refunded, deducted from future disbursements or accounted for. Most recently Zambia and Mauritania have committed to pay back a total of US \$9.5 million. This is additional to previous commitments from Uganda, Cameroun and Cambodia to refund a combined total of US \$4.99 million. In addition to the above figures, the US \$7.56 million withheld from the PR by the Reserve Bank of Zimbabwe was subsequently made available. Therefore the Global Fund Secretariat has either recovered, or has a high expectation of recovery in the short term, of approximately US\$ 22 million (not including the Zimbabwe case, which is not included in Table 1 of this report).

3.56 The Secretariat will continue to pursue its efforts to recover all outstanding amounts.

UNDP (Ref. GF/B23/10 paragraph 4.16 - 4.17)

3.57 UNDP is a long-standing and key partner of the Global Fund. Today, UNDP serves as PR in 27 countries, managing some 60 grants. Both in terms of financial volume and number of grants, UNDP implements 10-11% of the Global Fund’s commitments to recipient countries. UNDP is overwhelmingly a PR in countries facing exceptional development challenges, where alternative implementation arrangements are limited.

3.58 The Global Fund’s access to information held by UNDP is more limited compared to other PRs. The OIG is requesting access to UNDP information in excess of that currently provided by UNDP, as well as that which UNDP might be willing to provide in the future (i.e., a status of a UN member state for donors such as the Global Fund). The OIG maintains that even member state access for the Global Fund would not be sufficient to fulfill its currently defined mandate. The UNDP Executive Board, which has the authority governing the principles of access to information, is likely to discuss this matter in June 2011. By implication, this would suggest engagement of the Global Fund’s Board, as neither Global Fund’s Secretariat, nor the OIG, can directly negotiate with UNDP’s Board.

3.59 The FAC, during its 16th meeting on 22-24 March 2011, discussed the role of UNDP as PR in the Global Fund Model. The Global Fund Secretariat presented the current situation, characterized by restrictions of access to information when UNDP serves as PR - a situation affecting the annual external audit, but also access by the Local Fund Agent (LFA) to financial source documents held by UNDP. Additionally, UNDP does not allow the Global Fund's OIG access to books, records and staff. UNDP refers to its special status as a subsidiary organ of the United Nations and the "single audit principle", which has been reaffirmed by resolution 59/272 of the UN General Assembly. This principle precludes any external audit of UNDP, including those by Governmental bodies or any other external authority such as the Global Fund.

3.60 UNDP's "Office for Audit and Investigations (OAI)" conducts audits of programs financed by the Global Fund, but makes available to the Global Fund only very brief summaries of such audits. As a general rule, UNDP makes its own audit reports available in full only to member states of the UN, but limited to *in camera* review and with a requirement to maintain confidentiality.

3.61 Possible resolutions of this dispute include treating UNDP like any other PR, maintaining the current special relationship, or agreeing on a compromise approach (UN member state status for the Global Fund or even member state status with additional rights). Failure to reach agreement would likely trigger a debate as to whether UNDP can continue to serve as PR in the Global Fund model. If UNDP was excluded from being a PR, a transition plan away from UNDP to other entities would need to be agreed upon. For some countries, if there was no viable alternative, funding would have to stop. Taking the decision to exclude UNDP would also have similar implications on other UN agencies which have similar restrictions.

Recipients Code of Conduct (Ref. GF/B23/10 paragraph 4.18)

3.62 The EMT agreed that a meeting between the Executive Director, the Inspector General, Legal Counsel and the relevant committee leadership (PIC, FAC and Ethics) will be held at the occasion of the Twenty-Third Board meeting to review in depth the draft Recipients Code of Conduct, and decide on the way forward.

Complaints Procedure (Ref. GF/B23/10 paragraph 4.19 - 4.20)

3.63 The Global Fund Secretariat fully supports the initiatives on the complaints procedures and the proposed mediation procedure, for recipients to voice substantive concerns or disagreements about the findings of OIG audits and investigations prior to full blown arbitration. We note that these issues will be considered by the FAC at their next meeting on 9 May 2011.

Disclosure Policy (Ref. GF/B23/10 paragraph 4.21 - 4.24)

3.64 The Global Fund Secretariat notes the FAC Chair's recommendation to refer the issue on whether the Disclosure Policy should be modified to the High Level Review panel, in order to benefit from their expert advice.

The ability of the Office of the Inspector General to report to the Board (Ref. GF/B23/10 paragraph 4.25 - 4.26)

3.65 A description of the issues relating to the submission of the OIG Progress Report is outlined in paragraphs 3.6 to 3.8 of this report.

3.66 The Global Fund Secretariat fully recognizes that independence of the OIG is crucial, and has in no way attempted to interfere with the ability of the OIG to communicate to the Board, and would never do so.

3.67 The message sent to the Board by the Chair of the FAC on May 3 2011 in relation to this issue and the Disclosure Policy is reproduced in Annex 1.

4. CONCLUSION

4.1 The Office of the Inspector General has undertaken an extraordinarily thorough and broad program to review the portfolio of grants of the Global Fund. Some audits go as far back as 2003. A number focus on the period of 2006 - 2009.

4.2 This was a period of extraordinary growth for the Global Fund, and some of the Inspector General's findings reflect that some of the initial systems of fiduciary control were either insufficient or sufficient but inadequately enforced. It has become apparent that during these years of substantial growth, the Global Fund Secretariat in some cases was overstretched, and understaffed in some areas. As a consequence, the Global Fund Secretariat made some mistakes in grant management and oversight which we have since learned from.

4.3 A large number of audits and investigations are in the pipeline, making up a significant part of the overall Global Fund portfolio. Many of these will deal with the legacy of the past years of building up the portfolio. As they are completed, the amount of losses due to misuse and ineligible expenses will grow accordingly, and therefore the Global Fund will continue to face these challenges.

4.4 The Secretariat believes that the improvements made as a result of OIG findings, the reforms being put in place, and the future recommendations of the High Level Panel will together produce a stronger, better Global Fund; one which will be even more efficient than today, and in much better shape to prevent, detect and deal with misuse of funds than it has been in the past, as we continue the fight against the three diseases.

This document is part of an internal deliberative process of the Global Fund and as such cannot be made public until after the Board meeting.

Text of message sent to Board Members on OIG Matters (3 May 2011)**The Global Fund to Fight AIDS, Tuberculosis and Malaria
Message from the Chair of the Finance and Audit Committee**

Dear members of the Board,

On Friday 29 April you received the Progress Report from the OIG (GF/B23/10) including a statement (paragraph 4.25) that "the OIG has been hampered in its ability to report fully and completely to the Board" in connection with information on ineligible, fraudulent, or unsupported amounts (OIG's Report Annex 1).

Having looked into the matter, we believe that there is clearly a misunderstanding regarding this matter. The Global Fund has an absolute commitment to the work of the OIG and to full transparency and there is no desire by any part of the organization to withhold information from the Board or the general public. The issues below were still under discussion by the Finance and Audit Committee (FAC) and were scheduled to be addressed at a FAC meeting on May 9 so that the FAC could provide the Board with a full report.

The Inspector General refers to two issues: the discussion of the Global Fund's disclosure policy and the issue of a table of accumulated losses.

On the issue of the losses table, the FAC agreed that the table of losses would be jointly updated by the OIG and the Secretariat, preferably twice a year, and would clearly differentiate between fraudulent, ineligible and unsupported amounts in order to be able to release accurate and credible information concerning losses to the Board and the public.

The FAC Chair had informed the OIG before April 29 that issues related to the losses table and the disclosure policy would be discussed at the May 9 FAC meeting.

To reassure the Board on this point, we here state the updates that are under discussion:

1. **Zimbabwe:** The OIG's Zimbabwe report was issued in March 2009 (TGF-OIG-08-004) and describes a situation where the Reserve Bank of Zimbabwe (RBZ) withheld all foreign currency for all entities operating in the country. The amount affecting the Global Fund was US\$7.56 million, which was later released by the RBZ back to the PRs.
2. **India:** An on-going investigation in India has identified US \$1.07 million in ineligible expenses. This investigation is still on-going.
3. **Nepal:** A follow-up audit to a previous OIG audit of Nepal is with the OIG for finalization. The FAC thus far has not been informed of any issue or identified misuse of funds.
4. **Denominator/comparator:** The OIG wanted to include two new columns in the table of losses indicating the amounts disbursed and the amounts reviewed as figures against which the total amount of misuse could be compared. The FAC has asked the OIG and the Secretariat to present a proposal on what denominator would be most appropriate to the FAC at the May 9 meeting. At this meeting the proposal from the Comprehensive Reform Working Group will also be discussed.

Regarding the disclosure policy, the FAC identified potential gaps in the current policy. For this reason it was agreed that the FAC Chair and Legal Counsel would prepare amendments for FAC consideration at its meeting on May 9 in advance of the Board meeting on May 10-11, with the aim of discussing these and determining whether to propose an amended Disclosure Policy to the Board. On further reflection, the FAC Chair's intention is to advise the Board to request the High-Level Panel to take the FAC's considerations into account, and not to request the Board to make decisions on amendments.

Best regards,

Peter Van Rooijen
FAC Chair