Audit Report

Global Fund Grant Management in High Risk Environments

GF-OIG-17-002
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The Global Fund
Office of the Inspector General

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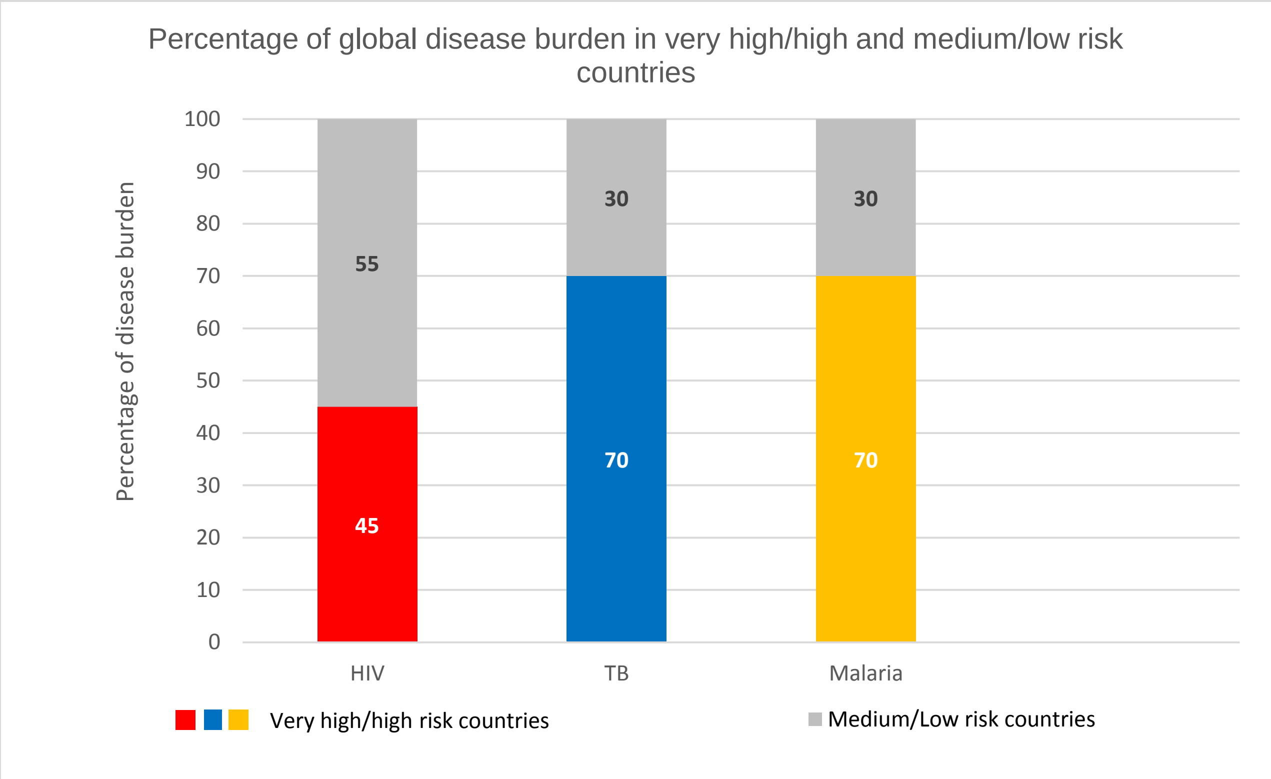
I. Background

The Global Fund provides grants to implement public health programs designed to ambitiously develop and scale up the delivery of health services. In some environments, there are significant risks due to political instability, institutional weaknesses and the sub-optimal capacity of implementers.

In its portfolio of over 100 countries, the Global Fund has classified 47 countries as high or very high risk based on a risk classification known as the External Risk Index (ERI). The ERI is an aggregate of ten indices developed by other organizations that capture political, economic, governance and operational factors contributing to external risk. In April 2016, the Global Fund identified 24 out of those 47 countries as "challenging operating environments". These environments have high ERI and are characterized by weak governance and man-made or natural crises.[1]

Strategic importance of grants in high and very high risk countries[2]
Collectively, the high risk countries account for a significant percentage of the global disease burden as shown below:



Successful interventions in high risk countries is critical for the Global Fund to achieve overall impact.[3] Reducing the disease burden in challenging operating environments is integral to the Global Fund's new 2017-2022 strategy with a particular focus on the countries under this classification. In April 2016, the Board approved a policy on challenging operating environments. A related operational policy note is current being developed by the Secretariat.[4]

Since inception of its new funding model, the Global Fund has signed grants amounting to US$5.7 billion and disbursed US$2.6 billion as at September 2016 to 47 high and very high risk countries. Due to the unique risks and capacity challenges in these countries, 61% of grants are managed by United Nations Agencies and Non-Governmental Organizations.

[1] The Global Fund 35th Board Meeting Minutes: BM53_03-ChallengingOperatingEnvironments_Policy_en.
[2] Where the report references countries as 'high risk' or with 'high' ERI, this refers collectively to high and very high risk countries.
[3] Nigeria and the Democratic Republic of Congo (DRC) represent a significant proportion of the high risk country disease burdens, accounting for 35% of global malaria mortality and 20% of high risk disbursements 2014-15.
[4] Given that this operational policy is still being developed, we have reviewed it under the assumption that ongoing work may develop concurrently with our findings.

Despite the challenges, the Global Fund has made significant and important progress in implementing life-saving interventions in these 47 countries:

- 5 million people have received anti-retroviral treatment through programs supported by Global Fund. This represents 55% of the total number of people on anti-retroviral treatment in all countries supported by Global Fund.
- 424 million bed nets have been distributed to households. This accounts for 64% of total bed nets distributed in all countries supported by Global Fund.
- 8 million tuberculosis (TB) cases have been successfully treated, which accounts for 50% of cases supported by Global Fund in all eligible countries.[5]

Based on the Secretariat's analysis, progress has been made across the three diseases. HIV incidence in 13 high risk countries with a high disease burden decreased by at least 50% from 2000 to 2015. Similarly, TB incidence in seven high risk countries with a high disease burden went down by at least 50% between 2000 and 2015. Finally, malaria-related deaths also decreased by at least 50% in 14 high risk countries with high disease burdens.

Existing mechanisms and tools used in high risk countries

Since it was founded, the Global Fund has developed a number of different tools to tackle the challenges it faces in risky environments.

Additional Safeguard Policy

The Global Fund has strengthened controls and oversight in 19 of the 47 very high and high risk countries, as of September 2016, by invoking a measure called the Additional Safeguard Policy. The measure is designed to be temporary and used 'whenever the existing systems to ensure accountable use of Global Fund financing suggest that Global Fund monies could be placed in jeopardy without the use of additional measures'. Although the Secretariat can use a tailored approach, the following measures are typically utilized under the policy:

- *Approval of implementation arrangements:* The Global Fund, in consultation with the Country Coordinating Mechanism and development partners, selects the implementers of grants based on risks identified.
- *Tighter arrangements on the flow of funds*: this often includes installing a fiscal agent (see below) and implementing a "zero cash" policy. Under this arrangement, sub-recipients do not receive grant funding in advance; instead, disbursement is made (i) on a reimbursement-basis against submission of appropriate invoices and other supporting documentation, (ii) directly to the suppliers by the Principal Recipients (iii) to cover only fixed costs, variable cost are paid as described in one of the previous options.

Fiscal Agents

Additional fiduciary arrangements through the use of fiscal agents are instituted in response to financial risk management. Fiscal agents have been put in place in 23 countries supported by the Global Fund, of which 15 are in high and very high risk countries. The Global Fund may appoint an agent to act as an enhanced control function within the implementers to oversee and verify expenditures of grant funds through a pre-expenditure review and sign off process. They are also appointed to build the financial management capacity of the Principal or sub-recipients.

[5] Figures based on data up to 2015 (cumulative) from the Global Fund Strategic Information Department.

Procurement Agents

In some instances, the Secretariat may decide to institute measures to address procurement-related risks. These measures include direct payment to contractors or vendors and the installation of an in-country procurement agent to manage the implementer's procurement activities or the outsourcing of activities. The Secretariat does not have a holistic view of the effectiveness of procurement agents across the portfolios to enable strategic decision-making.

The Technical Evaluation Reference Group, a group of independent experts which reports to the Global Fund Board, produced a paper called a Thematic Review of the Global Fund in Fragile States in 2014. The review prompted Board discussion on this area and was a critical part of the formation of a new policy called the Challenging Operating Environment Policy, approved by the Board in 2016. The review proposed a number of recommendations including advocating that the Secretariat pay more attention to fragile states.

Ongoing initiatives for grants in high risk environments

As well as the Board approval of the Challenging Operating Environment Policy, other initiatives have been developed by the Secretariat to respond to unique risks in six countries[6] in the Middle East, referred to as the 'Middle East Regional Initiative'. These countries face constantly evolving needs, limited capacity and severe constraints in providing essential services due to conflicts. The response seeks to streamline the implementation arrangements in these countries through the use of a single international Principal Recipient that manages the grants centrally but with satellite offices in the respective countries. It adopts a human rights-based approach which affirms the right to health for key populations and vulnerable groups including refugees and internally displaced people. This requires the implementers to reach out to the intended beneficiaries regardless of their current location, status, or ethnic and religious background.

[6] Iraq, Jordan, Lebanon, Palestine, Syria and Yemen.

II. Scope and Rating

01 Scope

This audit was undertaken as part of the Office of Inspector General (OIG)'s risk-based audit plan for 2016. The overall objective of the audit is to provide reasonable assurance on the adequacy and effectiveness of measures instituted by the Global Fund to manage grants in high risk environments. Specifically, the audit assessed whether:

- processes and measures are adequately designed to ensure achievement of impact in high risk environments; and
- measures and tools are effectively implemented and monitored by the Secretariat with relevant flexibilities.

The audit work included:

- a review of corporate measures designed for grant management in high risk countries such as the Additional Safeguard Policy and the use of fiscal agents;
- a detailed review of grant management processes, measures and tools in 24 high risk environments, namely Afghanistan, Angola, Burundi, Central African Republic, Chad, Eritrea, Guinea, Haiti, Myanmar, Somalia, Ukraine, a multi country Africa (Southern African Community Development grant), Democratic Republic of Congo, Côte d'Ivoire, Ethiopia, Honduras, India, Kenya, Nigeria, Pakistan, South Sudan, Sudan, Uganda and Zimbabwe; reliance was placed on OIG audits conducted in 13 of those countries since 2014;
- a survey of the Global Fund's Portfolio Managers in 47 high risk countries; and
- interviews and discussions with:
  - Principal Recipients, Local Fund Agents and the Country Coordinating Mechanisms of selected high risk countries;
  - United Nations Agencies, Humanitarian and other relevant organizations ; and
  - Global Fund staff in different business units, specifically the Grant Management Division, Risk Management Department, Strategy Investment & Impact Division, Monitoring Evaluation and Country Analysis Team, and the Finance Division.

For the purposes of the audit:

- The OIG considered the 47 countries rated as high or very high risk by the Secretariat in its External Risk Index; this includes the 24 countries classified as challenging operating environments.
- Given that work on developing the Challenging Operating Environments Operational Policy is ongoing, the OIG reviewed it under the assumption that ongoing work may develop concurrently with the findings of the audit.

02 Rating[7]

The audit rating based on the findings are shown in the table below:

Operational Risk	Rating	Reference to findings
Processes and measures are adequately and effectively designed to ensure achievement of impact in high risk environments.	Needs significant improvement	IV 1
Measures and tools are effectively implemented and monitored by the Secretariat with relevant flexibilities.	Needs significant improvement	IV 2.1, 2.2 and 3

[7] See Annex A for the rating definitions

III. Executive Summary

High risk environments, often characterized by political instability, institutional weaknesses and low capacity of the implementers, represent a significant proportion of the global disease burden.[8] Thus, success in these countries is crucial to achieve impact and the Global Fund's mission to end the three diseases. Grant management in such environments requires well designed and flexible approaches to achieve impact.

This audit considered the 47 countries rated as high or very high risk by the Secretariat in its External Risk Index. The 47 high risk countries include the 24 classified as challenging operating environments by the Secretariat in April 2016. This means that 23 out of the 47 risky environments are not necessarily challenging operating environments as defined by the Secretariat and subject to its Challenging Operating Environments Policy.

This OIG audit focused on two aspects:

<u>Whether processes and measures are adequately designed to ensure achievement of impact in high risk environments</u>

The Secretariat relies on a number of mechanisms to manage grants in high risk environments, including the Additional Safeguard Policy and Fiscal Agents. It has developed a set of tools to support Country Teams in risk identification at implementer level. The Secretariat has also:

- introduced more flexibility in its procedures; for example, by simplifying process and requirements for accessing new funding in selected countries including early engagement with the Technical Review Panel;
- developed innovative approaches, for example the launch of the Middle East Regional Initiative to streamline implementation arrangements in Iraq, Jordan, Lebanon, Palestine, Syria and Yemen due to the unique risks; and use of mobile phone based data reporting systems in some areas which are difficult to access; in Ukraine, the Secretariat supported a partnership arrangement to prevent disruption in the delivery of HIV services in conflict affected areas; and
- supported programs to reduce TB and HIV incidence by at least 50% in seven and 13 high risk countries with high disease burden between 2000 and 2015 respectively; malaria related deaths have decreased by at least 50% in 14 high risk countries with high disease burden from 2000 to 2015.

Despite the progress above, there are limitations in the existing systems and tools to enable the Secretariat to proactively identify and assess emerging threats posed by the country context in which the grants are implemented.

Identification and classification of risks
There are inadequate early warning mechanisms or indicators to identify and monitor risk levels of grants in these environments to allow for a timely response; this results in delays and a reactive approach in addressing risks. The audit found that some Principal Recipients in such environments have a set of indicators that enable the collection and assessment of emerging risks; however, it remains unclear how the Secretariat leverages this information for decision-making.

While Country Teams are flexible in managing grants in high risk countries, the absence of a defined risk appetite and minimum verifications required for grants in these environments have affected the ability of Country Teams to take measured risks. For instance, decisions on how much supporting documentation is required to distribute bed nets in conflict-affected areas often delay the implementation of such activities.

Emergency preparation

[8] 45% of the global burden for HIV, and 70% respectively for malaria and Tuberculosis.

High risk environments require proactive planning including engagement with partners to identify suitable options to implement grants during conflicts and other humanitarian emergencies. This reduces the lead time to plan and initiate actions during emergencies. For instance, the Secretariat was able to procure additional anti-retroviral medicines as part of its emergency preparedness plan in Angola when government funding was reduced. The Global Fund has provided contingency funds in the grant budget for Haiti to enable a quick response to emergencies. Despite these gains, the audit found that emergency preparedness had not been consistently incorporated in grant management in high risk environments. As a result, Country Teams will often have to plan a response from scratch during emergencies. Three countries classified as challenging operating environments had developed emergency response plans as of the time of the audit.

The above design gaps are due to the absence of an overarching framework to support grant management in high risk environments. In line with the Challenging Operating Environment Policy approved by the Board in April 2016, the Secretariat is working on an Operational Policy Note to guide Country Teams on grant management in challenging operating environments. When finalized, the note will be applicable to the 24 countries classified as challenging operating environments out of the 47 high risk countries.

The OIG concludes that the design effectiveness of current processes and measures for grant management in high risk environments **needs significant improvement.**

Whether measures and tools are effectively implemented and monitored by the Secretariat with relevant flexibilities

Despite the challenges in high risk environments, the Secretariat has instituted innovative approaches to manage some grants. The audit found that many Country Teams successfully use the flexibilities available to them in the Secretariat's existing processes to manage grants in high risks environments; this includes the ability to quickly reprogram grants to respond to changes in the country context, increased use of tailored performance frameworks, consideration of the country context in the assessment of the grant's performance and a differentiated grant-making process. For instance, rapid mobile phone-based data reporting systems are being used in some areas which are difficult to access. Furthermore a Secretariat-wide project called Implementation Through Partnership (ITP)[9] aims to address implementation bottlenecks in selected countries. This includes 12 high risk countries.

Measures such as Additional Safeguard Policy and Fiscal Agents used in high risk environments have allowed the Secretariat to implement grants in a risk-measured way despite in-country challenges. For example, the audit found that the Additional Safeguard Policy has mitigated financial risks to a great extent through the appointment of United Nations Agencies and International Non-Governmental Organizations as Principal Recipients. Generally, these entities have relatively strong financial management systems compared to in-country implementers.

However, the measures have not always addressed the related risks for which they were instituted. For example:

- Fiscal Agents are installed by the Secretariat at country level to principally mitigate fiduciary risks. The OIG noted gaps in the quality of assurance services provided by the Fiscal Agents. External audit reports for 14 grants in seven high risk countries were qualified due to ineligible and unsupported transactions although Fiscal Agents had already been present for a minimum of 12 months to mitigate those very risks. OIG audit reports on grants in Malawi, Democratic Republic of Congo and Cote d'Ivoire also identified various gaps in the activities of the fiscal agents.[10]

[9] Implementation Through Partnership is a Global Fund initiative for increased technical cooperation through results-oriented support in 20 selected countries.
[10] Country audit report on grants in Democratic Republic of Congo and Malawi (OIG report numbers GF-OIG-16-022 and GF-OIG-16-024 published on 21 September 2016 and 11 October 2016) http://www.theglobalfund.org/en/oig.

- Despite the general progress on financial risk mitigation, supply chain and programmatic mitigations have not shown equivalent progress and are not effectively addressed in ten countries under the Additional Safeguard Policy due to the inherent weaknesses in the national systems. The Secretariat does not have effective and timely corporate measures to enable Country Teams to tailor responses to address supply chain and programmatic issues in high risk environments.

Balance between country ownership and short term measures
In line with the Global Fund's country ownership principle, additional safeguards are required to be short term measures. However, a clear strategy with responsibilities and timelines to phase out the short term measures are not consistently agreed and implemented with in-country stakeholders. The audit noted that 13 out of the 19 countries did not have exit strategies. Moreover, only two countries have transitioned from the Additional Safeguard Policy since 2004.

Monitoring mechanisms of measures were also found sub-optimal. The measures are not regularly monitored to ensure appropriate revisions where necessary. Eleven of the 19 high risk countries have been under Additional Safeguard Policy for at least five years without a reassessment of its effectiveness. Contrary to the Operational Policy Note on the policy, the Secretariat has never presented a report of the status of countries to the Audit and Finance Committee (or its predecessor committee). While Fiscal Agents are required to be assessed every year, the necessary tools and systems have not been developed, resulting in inconsistent reassessments by Country Teams.

The Secretariat has not analyzed and defined thresholds for the costs of doing business in high risk environments. The OIG's analysis of grant expenditure in 2014 and 2015 indicated that five countries spend at least 57% (US$42 million) of their grants on staff costs, overheads, planning and administration costs. With resources allocated to countries based on the disease burden, such high indirect costs affect the ability to fund programmatic activities.

The audit concludes that the existing implementation and monitoring of the additional measures and tools in high risk environments **need significant improvement.**

IV. Findings and Agreed Management Actions

01 Identification, classification and response in high risk environments

A limited framework to support grant management in high risk environments has resulted in inconsistent identification, classification of high risk countries and gaps in response to the identified issues.

Since its creation, the Global Fund has supported high risk countries to implement life-saving interventions. The Board approved a policy on challenging operating environments in April 2016 which covers 24 out of the 47 high or very high risk countries. Although the Secretariat is in the process of finalizing its related Operational Policy Note to support grant management activities in those environments, it has already:

- introduced more flexibility in its procedures; for example, by simplifying requirements for accessing new funding in selected countries;
- developed and expanded partnerships with implementers active in high risk countries; for example, by joining the Global Health Cluster which is a group of agencies, organizations and/or institutions interconnected by their respective mandates to deliver timely, effective and predictable health related interventions while improving accountability and leadership;
- approved several grants under an Emergency Fund[11] to support continuity of treatment and essential services in Sierra Leone and Liberia during the Ebola outbreak in 2014-15, in Nepal following the April 2015 earthquake, in Lebanon and Jordan in response to the Syrian refugee crisis, and in the conflict zones of eastern Ukraine; and
- developed emergency response plans for Burundi, Central Africa Republic, and Somalia.

Whilst the Challenging Operating Environments Policy has been disseminated and specific case studies shared across teams, the initiatives have not yet been institutionalized. The lessons learned have yet to be completed and made available to all Country Teams to better identify, respond and manage partnership challenges in high or very high risk environments on an ongoing basis.

Identification of risks and classification of countries

The Secretariat has invested significant resources and effort into developing tools to assist with identifying risks at the country level including capacity assessments of implementers, biannual progress reviews and a tool known as the Qualitative Risk Assessment, Action Planning and Tracking Tool (QUART). A 2016 initiative at the Secretariat, known as Differentiation for Impact, classified countries as either High Impact, Core (medium sized portfolios and/or high risk) and Focused countries (usually less risky with smaller portfolios); these classifications affect the level of resourcing and expertise to be devoted to the respective portfolios. The Secretariat has further differentiated the management of portfolios to include challenging operating environments so that special consideration can be given to the problems faced in these countries. However, and given that the operational procedures are still under development as the policy was approved in April 2016, this approach has not yet translated into a materially different approach to managing the majority of countries classified as high or very high risk.

- <u>Inadequate proactive and timely identification of risk:</u> following the initial assessments, there are limited mechanisms to proactively identify, assess and report emerging risks posed by changing country context on a timely basis. Although the QUART is updated periodically, regular updating is not mandatory for 32 of the 47 high risk countries. Nine high risk

[11] This provides quick access to funds and greater flexibility to enable the Global Fund to fight the three diseases in certain emergency situations. The purpose of the Emergency Fund is to support the provision and continuity of essential prevention and treatment services for HIV/AIDS, tuberculosis, and malaria during emergency situations that cannot be funded simply through the reprogramming of existing grants

countries have not completed the QUART since 2013. There are large delays between the initial assessment and any subsequent revisions (the OIG noted instances of up to two years for two high impact countries). This results in reactive measures to address risks in the countries. Four OIG audits in high risk countries in 2015[12] (South Sudan, Nigeria, Honduras and Kenya) found ineffective risk identification across programmatic, data quality and supply chain risks. Ongoing assessment and review of key risks and the effectiveness of mitigation measures remains crucial due to the continuous changes in the environments within which grants are implemented. Some Principal Recipients in high risk environments have developed their own indicators to provide early warning trends in risks for timely responses. However, the information is not consistently used by the Secretariat for decision-making.

- A lack of gradation between challenging operating environments: In April 2016, the Secretariat classified 24 countries as challenging operating environments. This classification was focused at the national level without internal or regional sub-classifications despite significant variations. For instance, countries such as Nigeria, Kenya and Ukraine have been classified as challenging operating environments due to ongoing conflicts in particular regions. These conflict areas do not correspond to areas where the majority of the populations targeted by Global Fund programs live. The regional variations require sub-classifications to determine the nature of the risks, interventions, implementers and additional safeguards required to address the challenges. For instance, some regions in Kenya and Ukraine require more humanitarian interventions and tailored risk mitigation measures instead of the traditional measures due to the ongoing conflicts and security crisis.
  Although the Board has adopted the Technical Evaluation Reference Group's recommendation for internal sub-groupings of challenging operating environments,[13] this is yet to be implemented by the Secretariat.

Response in high risk countries: Country Teams are encouraged to be flexible in managing grants in high risk environments including tailored re-programing of grants to respond to changes in country context, as well as simplified grant-making processes for some countries. Under the Additional Safeguard Policy, measures may be instituted to allow implementation of programmatic activities despite in-country risks. Despite the aforementioned positive initiatives in emergency situations, the Secretariat has not defined acceptable risk levels and minimum mechanisms to be instituted by Country Teams to manage grants in high risk environments. The absence of defined acceptable risk levels, minimum measures and verifications required in such environments affects the ability of Country Teams to take measured risks; this often results in delays in their implementation. The auditors noted that the measures and tools instituted in various high risk countries are inconsistently implemented and do not follow a risk-based approach. For example, the fiduciary risks of five countries have been consistently rated as high by the Secretariat over the last two years, with Local Fund Agents identifying significant financial management issues. However, fiscal agents as a preventive measure have not been instituted on those portfolios.

Emergency preparation: High risk environments require proactive planning including engagement with partners to identify suitable options to implement grants during conflicts. This reduces the planning time required to initiate actions during emergencies. For example:

- The Secretariat was able to procure additional anti-retroviral medicines as part of its emergency preparation plan for Angola when government funding was reduced.
- In Haiti, the Global Fund provided a general contingency fund in the grant budget to enable quick response to emergencies (note: this was before the October 2016 hurricane).

Despite these measures, emergency preparation has not been consistently incorporated in the Secretariat's grant management in high risk environments:

[12] Country audit report on grants in South Sudan, Nigeria, Honduras and Kenya (OIG report numbers GF-OIG-16-018, GF-OIG-16-014, GF-OIG-15-022, and GF-OIG-15-011) http://www.theglobalfund.org/en/oig.
[13] TERG_Evaluation2013-2014ThematicReviewFragileStates_PositionPaper_en

- Emergency response planning: The Secretariat currently does not have defined measures and tools that are deployed to manage grants during emergencies. Three countries classified as challenging operating environments had developed emergency response plans as of the time of the audit. As a result of the lack of corporate measures and pre-planning, emergency situations mean that Country Teams will often have to plan a response from scratch. For example, in the Burundi refugee crisis in 2016, it took the Secretariat at least four months to plan a response due to contractual negotiations with a United Nations agency in the absence of a framework agreement. The OIG acknowledges that the need for emergency preparation will be dependent on the nature of the high risk environment which requires continuous monitoring.

- Internal expertise: Grant management in high risk environments is associated with complexities such as operational constraints, sub-par implementers, natural disasters, disease outbreaks, devolved federal structures, and armed conflicts. Our survey respondents indicated that such complexities require significant consultations with external stakeholders and within the Secretariat. However, the absence of internal specialists to deal with the specific complexities of high risk environments has affected the ability to effectively respond to the issues. While the Secretariat was able to distribute bed nets during conflicts in the Central African Republic in 2014 and 2015, these activities were impacted by delays due to long internal consultations and the engagement of external social mobilization consultants.

In-country partnership engagement: The complexities in high risk environments and limited availability of in country partners in most environments require effective engagement and harmonization of risk management with available partners at country level. Despite a lack of formal policies, some countries have explored innovative ways to engage with, and benefited from, in-country partnerships. For instance:

- The Global Fund collaborated with the World Food Programme to store and distribute bed nets in five countries in 2013/2014.
- In Somalia, there is a joined-up risk management approach for United Nations agencies, partners and donors organizations providing humanitarian and development assistance including a dedicated team for harmonizing the risk mitigating measures.

Although not specific to risky environments, the Secretariat has initiated a project called Implementation Through Partnership[14] which is aimed at increasing engagement with partners to address implementation bottlenecks. Despite this progress, and whilst support is available from senior management on request, the Secretariat has no formal guidance, nor a set of tools to facilitate Country Teams engagement and leverage of in-country partners in managing related portfolio issues in high risk environments. For example, 71% of Country Teams who responded to the OIG survey confirmed that the Secretariat does not have guidance on in-country partnership engagement. The Risk Department, in its 2016 corporate risk register, has identified partnerships as planned risk mitigation measures to address impact or mission risks in high disease burden countries and weak public health and community health systems. However, the lack of documented guidance to Country Teams on how to engage with partners has affected the ability to manage cross-cutting risks. The OIG audit reports on Kenya, Uganda, Nigeria and South Sudan[15] in 2015 identified gaps in partnership engagements impacting strategic approaches on targets, funding, data, supply chain and capacity building.[16] For instance, the Kenya audit pointed out the need for thorough and up-to-date mapping of donor interventions for the three diseases to drive a joined-up and shared accountability framework for health service delivery.

[14] Implementation Through Partnership is Global Fund initiative for increased technical cooperation through results-oriented support in 20 selected countries.
[15] Country audit report on grants in Kenya, Uganda, Nigeria and South Sudan (OIG report numbers GF-OIG-15-011, GF-OIG-16-023, OIG-16-005 and GF-OIG-15-016) http://www.theglobalfund.org/en/oig.

Despite the significant progress made in this area, the Global Fund has faced challenges in achieving impact in these countries. The absence of a framework to implement grants in risky environments is causing operational difficulties at the Secretariat level; for example:

- *Delays in grant making*: 78% of grants in high risk environments took more than the Secretariat's agreed three-month window after the first Grants Approval Committee review to reach the second committee. It took an average of more than five months during this period: this was mostly due to capacity constraints at the country level, which required measures to enforce existing differentiated grant-making processes.

- *Failure to adopt flexibilities*: While the Secretariat has differentiated its grant-making processes based on the size of the portfolio and risk levels, Country Teams often do not take advantage of the flexibilities available to them. For instance, 20 grants in high risk environments out of estimated 72 grants which qualified for a "simplified" grant-making process chose to adopt the "full" process.[17]

Overall, 18% of grants in high risk countries are rated "C" or "B2" in the latest available grant rating indicating that grant performance is significantly below the agreed targets.[18]

Agreed management action 1:

The Secretariat will develop:
a) Operational Policy Note for Challenging Operating Environments (COEs) that clarifies the process for classification of countries as COEs including further sub-classifications and the flexibilities available to the countries and how such flexibilities are approved.
b) Guidance for contingency planning for countries facing crisis and emergencies.

Owner: Head of Grant Management
Target Date: 30 June 2017

[17] Under the simplified grant making process, countries are exempted from some grant making processes including the first grant approval committee's review.
[18] Grant rating data taken from Business Analysis & Reporting Tool (BART) August 2016.

02 Effectiveness of safeguards instituted to manage grants in high risk environments

2.1 Gaps in the management and implementation of the Additional Safeguard Policy (ASP) has affected its effectiveness.

In the 19 countries where the Global Fund has invoked the ASP (as of the time of audit), the Secretariat is allowed to appoint Principal Recipients (73% selected are United Nations agencies and Non-Governmental Organizations). However, gaps in the implementation and management of the ASP have limited the Secretariat's ability to significantly address and remedy the issues identified.

Balance between country ownership and short term measures: The Secretariat has instituted short term measures to manage grants in high risk environments; however, there are limited strategies to phase out these short term arrangements and to build capacity with existing country level mechanisms:

- Exit strategies with time bound actions and responsibilities of stakeholders to transition out of the ASP have not been consistently defined, agreed with in-country stakeholders and implemented. For instance, the audit found that there are no strategies to phase out the ASP in 13 out of the 19 countries.
- Where strategies existed (in six countries), the actions are not specific, measurable and time bound with clear responsibilities for all stakeholders. This usually results in countries being under ASP for a long time (the OIG noted that only two countries have been phased out from ASP since 2004).
- Capacity building activities required under the ASP are not consistently implemented. The audit found that plans to address capacity constraints of national disease programs were not prepared by Principal Recipients in five out of the 19 countries under ASP. In a further ten countries, capacity building plans are yet to be developed.
- OIG interviews with Country Teams and selected implementers indicated that it is difficult to get countries out of ASP, creating unwillingness to invoke the policy where necessary. For instance, the Secretariat's assurance providers and OIG investigation reports consistently raised weaknesses in the capacity of government implementers to manage grants in Nigeria, the policy was not invoked until April 2016.
- There is inconsistent application of the ASP across various teams; for example:

    - De facto ASP has been declared in four countries without being formally invoked.
    - In Somalia, ASP was declared in July 2016 despite the country being managed as such since 2004.

No routine monitoring of ASP once invoked: Monitoring mechanisms have not been embedded in the ASP to ensure routine reassessment of its effectiveness. The audit found that 11 of the 19 high risk countries have been under ASP for at least six years (with a maximum of 11 years) without a reassessment of its effectiveness. Contrary to its Operational Policy Note, the Secretariat has never reported the status of countries under the policy to the Audit and Finance Committee (or equivalent committee) or to the Board.

Effectiveness of ASP measures: In most cases, invoking the ASP has significantly reduced financial risks. However, the policy has had limited impact on other significant risks such as supply chain, data and quality of services. The OIG review of 10 countries under ASP identified that issues in supply chain, data and quality of services identified prior to installation of the policy had not been addressed. This is partly due to limited Secretariat measures to address those risks and quality checking of the mitigation measures instituted by Country Teams (mentioned above). For instance, 12 and seven countries under ASP have consistently had high risk ratings in "Health Services and Products Risks" and "Programmatic and Performance Risks" respectively in the last two years according to the Secretariat's risk assessment.

Only 45% of high risk environments have been subject to Operational Risk Committee review to date. A recently approved (September 2016) Operational Policy Note on Risk Management during Grant Life Cycle requires the Risk Department to support Country Teams in assessing effectiveness of measures instituted to address risks.

Agreed management action 2:

The Secretariat will:

a) Develop a system to track countries under the Additional Safeguard Policy (ASP) through its Grant Operational System.
b) Update the Operational Policy Note on ASP to clarify the processes for regular monitoring and review of countries under the Policy and revoke it where appropriate.

Owner: Head of Grant Management
Target Date: 31 December 2017

2.2 Effectiveness of fiduciary measures in high risk environments

The Secretariat has spent significant resources mitigating fiduciary risks in high risk countries; however, systemic financial management issues remain due to gaps in the use of assurance providers.

Fiscal agents, instituted in 23 countries (including in 15 high risk countries) to mitigate financial risks, cost an estimated US$10 million a year; this cost is in addition to Local Fund Agents (annual cost of US$14 million for the 23 countries) and External Auditors (estimated cost of US$3 million). However, due to gaps in the use of assurance providers, some financial management risks remain unaddressed.

Multiple controls and assurance providers creating inefficiencies: There are no defined criteria to determine when additional fiduciary arrangements are required; this has resulted in duplications, rather than complementarity, in the services provided by the assurance providers. For instance, fiscal agents have been installed in addition to Local Fund Agents and external auditors in six countries with low financial risks (according to the Secretariat's risk assessment - QUART) in the past two years. The Fiscal Agents preapprove and sign off on transactions before payments are made. However, the terms of reference of the Local Fund Agents and external auditors have not been tailored to reflect these additional mitigation measures and assurances introduced by the Secretariat.

There are perceived and potential conflicts of interest in the roles of the fiscal agents: As part of their mandate, fiscal agents are required to build the financial management capacity of the grant implementers so that the implementer can ultimately manage its own finances; this creates a perceived and potential conflict of interest in the execution of their roles. The audit found:

- Fiscal agents have not consistently developed and implemented the required capacity building activities in high risk countries. For instance, five out of the 15 fiscal agents in high risk countries have not developed the capacity building plans.
- Where the plans have been developed, the absence of a mechanism to track its implementation results in delayed execution of the plans. For example, a fiscal agent engaged in 2013 did not develop a capacity building plan until March 2016. Similarly, another agent installed in March 2015 only prepared a capacity building plan in August 2016.

Quality of services in high risk environments: The audit found that the additional fiduciary controls in the form of fiscal agents have not consistently addressed the related risks. For example:
- Six out of the 15 high risk countries continue to have high financial risk ratings for the last two years despite use of the fiscal agents.
- The latest external audit reports for 14 grants in 7 high risk countries (Burundi, Chad, Côte d'Ivoire, Democratic Republic of Congo, Guatemala, Liberia and Niger) were 'qualified' despite the use of fiscal agents (for a minimum of 12 months) at a total approximate annual cost of US$ 4.2 million.[19] The basis of the qualification of the audit opinions related to ineligible and unsupported transactions or other control weaknesses. In addition, Local Fund Agent reports for Burundi, Chad, Democratic Republic of Congo and Guinea between 2014 and 2015 consistently identified ineligible material and unsupported transactions despite the existence of the fiscal agents. Furthermore, OIG audit reports on grants in Democratic Republic of Congo, Cote d'Ivoire and Malawi (see below), identified various gaps in activities of the fiscal agents.

Delays in implementation activities: Despite being mandated to improve financial management, the OIG found that submitted funding requests to the fiscal agent for approval often caused delays in program implementation. For instance, in an OIG audit of Global Fund grants in Malawi[20], the auditors noted that it takes an average of 17 days (with a maximum of 126 days)

[19] The reports used were 2014 and 2015 reports based on completion at the time of audit.
[20] Country audit report for Malawi (OIG report number GF-OIG-16-024 published on 11 October 2016) http://www.theglobalfund.org/en/oig

between the fiscal agent's receipt and approval of funding request. According to the fiscal agent Terms of Reference, the turnaround time for approving requests should be a maximum of five days.

The gaps in the quality of the services provided by the agents are compounded by inadequate monitoring of providers by the Secretariat. In line with the fiscal agent Terms of Reference, the Secretariat is required to assess their performance every year. Whilst there are tools to assess the performance of Local Fund Agents who are used in all countries with Global Fund grants, similar tools are yet to be developed for the assessment of the fiscal agents; this has resulted in inconsistent reassessment of agent performance by Country Teams.

The Secretariat has initiated actions including the development of guidelines, tools and revision of Terms of Reference for fiscal agents and other assurance providers to address the identified gaps. The actions are yet to be completed and embedded in the Grant Management Division.

Agreed management action 3:

The Secretariat will:

a) Develop financial risk management guidelines that outline the:

- i) main financial risk management tools;
- ii) roles of the fiscal agent;
- iii) triggers for use of fiscal agents and the process for appointment and removal of fiscal agents
- iv) Processes for management of conflict of interest in the roles of the fiscal agents; and
- v) metrics to measure performance of the agents.

b) Centralize annual performance assessments for fiscal agents.

Target Date: 31 March 2017
Owner: Head of Finance Information Technology Sourcing and Administration Division

Agreed management action 4:
The Secretariat will develop an automated fiscal agents management system which will include need assessment, contract management and performance assessment modules.

Owner: Head of Finance Information Technology Sourcing and Administration Division
Target Date: 31 December 2017

03 Cost effectiveness of grants in high risk environments

The Global Fund could miss opportunities to optimize scarce resources because it has not analysed and monitored the high operating costs of high risk countries.

Grant implementation in high risk environments can be difficult due to security and capacity constraints, and the challenges to find suitable locally-based implementers. In order to achieve its mission, the Global Fund relies on United Nations agencies and Non-Governmental Organisations to implement grants in the most difficult and high risk countries; however, this often comes at a significant cost as these implementers have to set up offices in these difficult environments. Despite this, the Secretariat has not analysed and defined the cost of doing business in these countries; this may result in a loss of opportunity to maximize impact, in the context of funding constraints and risk management.

Significant portions of country allocations being used on human resources, overheads, planning and administration costs[21]: The high risk countries spent an average of 25% (US$622 million) of grant resources on these costs in 2014-15, leaving 75% (US$1.9 billion) for core programmatic activities (based on the Secretariat's data). However, these costs increase to at least 50% (with a maximum of 66%) for ten high risk countries leaving a small part of the resources for core programmatic activities. For instance, five high risk countries spent an average of 57% (US$41 million) of grant resources on human resources, overheads, planning and administration costs in 2014-15, leaving only 43% (US$32 million) for core programmatic activities as shown below:

Country	Expenditure between 2014 and 2015 US$	Human resources, Overheads, Planning and administration	
		%	Amount US$
Angola	7,764,019	66	5,085,694
Palestine	1,408,229	64	907,011
Colombia	14,555,599	58	8,477,692
Djibouti	3,977,763	58	2,302,094
Haiti	45,891,929	55	25,147,309
Total	**73,597,539**	**57**	**41,919,799**

Given that resources are allocated to countries based on the disease burden and ability to pay, the significant use of resources on these costs reduces the ability to implement life-saving interventions. For instance, in Angola - a country with the 22nd highest Global HIV disease burden – The Global Fund and partners are able to provide anti-retroviral treatment for only 29%[22] of the people living with HIV in 2015.

No thresholds for cost categories: The Secretariat relies on implementers to determine the cost of their programs subject to reviews by assurance providers and endorsement by the Grants Approval Committee. The absence of defined thresholds for cost categories have resulted in significant variances in the amounts of human resources, overheads, planning and administration costs. For example:

[21] OIG acknowledge that costs reviewed may also relate to program activities (e.g. HR costs could include program staff costs).

[22] http://data.worldbank.org/indicator/SH.HIV.ARTC.ZS?locations=AO

i) **Human resources cost:** The average staff costs in Global Fund grants from 2014 to 2015 was 18% for the high risk countries. This includes salaries and related employee benefits. Sixteen (16) of those countries spend at least 37% (US$148 million) of grant resources on staff costs, with this percentage increasing to 49%, 44% and 43% for countries such as Palestine, Colombia and Honduras respectively.

ii) **Overheads:** There are six high risk countries that spend an average of 13% (US$5 million) of grant resources (US$39 million) on costs such as management fee, office rent and utilities, with countries such as Iran and Syria spending 15% of resources on overheads. This is above the average cost of 3% across all Global Fund grants in the high risk countries.

iii) **Planning and administration costs:** Similarly, four high risk countries use at least 11% (US$13 million) of grant resources on travel, bank charges, and accounting and audit costs; in Angola, 13% of resources are spent on planning and administration costs. Based on Global Fund's data, the average cost for such activities in the high risk countries is 4% of grant resources.

The OIG acknowledges that analyzing raw costs does not consider the potential differential in the cost of operating in different environments. The Global Fund also works with many partners in-country where direct costs of medicines may be materially paid by other donors. As such, this analysis does not constitute evidence of inefficiencies on its own as the varied cost of doing business in the countries and nature of the implementers may justify the cost. However, in the absence of an in-depth analysis considering all the relevant factors and determination of cost of doing business and appropriate thresholds for various cost categories, the Secretariat may miss the opportunity to ensure effective use of resources in high risk countries.

Agreed management action 5:

The Secretariat will conduct an analysis of cost categories across different types of Principal Recipients in COEs and a sample of non-COE High Risk countries for comparison. This will then be leveraged as appropriate during grant making.

Owner: Head of Finance Information Technology Sourcing and Administration Division
Target Date: 30 June 2017

V. Table of Agreed Actions

#	Category	Agreed Management Action	Target date	Owner
1	Identification, classification and response in high risk environments	The Secretariat will develop: a) Operational Policy Note for Challenging Operating Environments (COEs) that clarifies the process for classification of countries as COEs including further sub-classifications and the flexibilities available to the countries and how such flexibilities are approved. b) Guidance for contingency planning for countries facing crisis and emergencies.	30 June 2017	Head of Grant Management
2	Gaps in the management and implementation of the Additional Safeguard Policy (ASP) has affected its effectiveness.	The Secretariat will: a) Develop a system to track countries under the Additional Safeguard Policy (ASP) through its Grant Operational System. b) Update the Operational Policy Note on ASP to clarify the processes for regular monitoring and review of countries under the Policy and revoke it where appropriate.	31 December 2017	Head of Grant Management
3	Effectiveness of fiduciary measures in high risk environments	The Secretariat will: a) Develop financial risk management guidelines that outline the: i) main financial risk management tools; ii) roles of the fiscal agent; iii) triggers for use of fiscal agents and the process for appointment and removal of fiscal agents iv) Processes for management of conflict of interest in the roles of the fiscal agents; and v) metrics to measure performance of the agents. b) Centralize annual performance assessments for fiscal agents.	31 March 2017	Head of Finance Information Technology Sourcing and Administration Division
4	Effectiveness of fiduciary measures in high risk environments	The Secretariat will develop an automated fiscal agents management system which will include need assessment, contract management and performance assessment modules.	31 December 2017	Head of Finance Information Technology Sourcing and Administration Division

#	Category	Agreed Management Action	Target date	Owner
5	Cost effectiveness of grants in high risk environments	The Secretariat will conduct an analysis of cost categories across different types of Principal Recipients in COEs and a sample of non-COE High Risk countries for comparison. This will then be leveraged as appropriate during grant making.	30 June 2017	Head of Finance Information Technology Sourcing and Administration Division

Annex A General Audit Rating Classification

Effective	**No issues or few minor issues noted**. 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.
Partially Effective	**Moderate issues noted**. 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.
Needs significant improvement	**One or few significant issues noted**. 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.
Ineffective	**Multiple significant and/or (a) material issue(s) noted.** 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 B: 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 our auditors to provide 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 audits may be specific or broad, depending on the context, and covers risk management, governance and internal controls. Audits test and evaluate supervisory and control systems to determine whether risk is managed appropriately. Detailed testing takes place across the Global Fund as well as of grant recipients, and is used to provide specific assessments of the different areas of the organization's' activities. Other sources of evidence, such as the work of other auditors/assurance providers, are also used to support the conclusions.

OIG audits typically involve an examination of programs, operations, management systems and procedures of bodies and institutions that manage Global Fund funds, to assess whether they are achieving economy, efficiency and effectiveness in the use of those resources. They may include a review of inputs (financial, human, material, organizational or regulatory means needed for the implementation of the program), outputs (deliverables of the program), results (immediate effects of the program on beneficiaries) and impacts (long-term changes in society that are attributable to Global Fund support).

Audits cover a wide range of topics with a particular focus on issues related to the impact of Global Fund investments, procurement and supply chain management, change management, and key financial and fiduciary controls.

Annex C: Message from the Executive Director

Many of the world's high-risk environments suffer devastatingly high levels of disease and poverty, and it is critically important for the Global Fund to support prevention and treatment programs to protect families from AIDS, tuberculosis and malaria, where millions of lives are at stake.

High-risk environments, by definition, are challenging places to deliver health services. Yet the health imperatives in these countries mean that the greatest risk is failing to deliver essential services, and that has to be carefully managed with other financial risks. The Global Fund employs strict financial and procurement controls and monitoring, with mechanisms specifically suited to working in high-risk countries and challenging operating environments, to support health services despite all obstacles. We do not have the option of backing away. We have to engage.

In high-risk environments, strict measures to mitigate financial risk – like installing a fiscal agent – requires additional cost and processes. Other factors contribute to additional costs as well, such as paying the salaries of health care providers, a necessary expense for program delivery in high-risk countries. While technically counted as “overhead,” which may make it sound optional, those costs are absolutely essential. The Ebola crisis and other disease outbreaks have highlighted how critical it is to build heath care worker capacity in high-risk environments.

This audit reviewed the adequacy and effectiveness of measures instituted by the Global Fund to manage grants in 47 high-risk countries, and it points to significant progress in recent years that has saved millions of lives. In these high-risk countries, programs supported by the Global Fund have provided 5 million people with antiretroviral therapy for HIV, over 400 million mosquito nets to protect families from malaria, and have tested and treated 8 million people for tuberculosis.

Much of that progress comes from improvements suggested by the Board of the Global Fund on managing risk, including guidance to strengthen fiduciary controls, as well as this year’s Prioritized Action Plan to Accelerate Management for Impact.

Progress has also come from suggestions in audits and investigations by the Office of the Inspector General, an integral and important part of risk management and controls, to complement the Global Fund’s active risk management and controls. Findings and recommendations from audits and investigations have been used to strengthen Global Fund mechanisms to improve the effectiveness and accountability of the Global Fund’s work.

The audit also includes concerns about limitations in existing systems and tools to enable proactive identification and assessment of emerging threats. The cost effectiveness of grants in high-risk environments, and the quality of fiduciary services in high-risk environments, are issues that merit continued scrutiny and consideration. Costs are more significant in high-risk environments, and implementing an Additional Safeguard Policy, or installing Fiscal Agents and Procurement Agents, all increase costs.

The audit points to five countries where aggregate staff costs, staff costs, overheads, planning and administration climbed to 57 percent of their grants. However, factoring in improvements that have been already made to better measure and manage costs under the latest grants, the cost for those countries is now estimated based on budgeted amounts to decrease to only 23 percent of grant funds for the period ending in 2019.

In all cases, the Global Fund has zero tolerance for corruption or fraud, and conducts robust audits and investigations. When an investigation identifies misspent funds, the Global Fund pursues recovery, so that no donor money is lost. The publication of all OIG reports demonstrates the Global Fund’s strong commitment to transparency and accountability.

The Global Fund is constantly strengthening its systems to improve the effectiveness and accountability of our work. In addition to regular risk assessments, and in response to the recommendations from this audit report, the Global Fund is implementing additional measures to mitigate risk and improve effectiveness in high-risk environments, such as:

- The Global Fund is implementing a new Challenging Operating Environment Policy, which focuses more sharply on fragile states and regions and calls for more stringent risk assessments and controls and more rigorous risk assessments to identify emerging threats. The Global Fund issued a related Operational Policy Note to support grant management activities in those environments; and guidance for contingency planning for countries facing crisis and emergencies.

- The Global Fund is developing a system to track countries under the Additional Safeguard Policy through our Grant Operational System, and to update the Operational Policy Note on Additional Safeguard Policy to clarify the processes for regular monitoring and review of countries under the policy.

- The Global Fund is formalizing financial risk management guidelines to outline financial risk management tools and the roles of the fiscal agent; triggers for use of fiscal agents and the process for appointment and removal of fiscal agents; processes for management of conflict of interest in the roles of the fiscal agents; metrics to measure performance of the agents; and centralization of annual performance assessments for fiscal agents.

We value the recommendations on this matter made by the OIG, which further improve our risk management. Thank you for the opportunity to provide context to address the important issues outlined in the OIG report.