



Follow-up Audit Report

Global Fund Grants in the Democratic Republic of Congo implemented by Population Services International

GF-OIG-20-013
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Geneva, Switzerland

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1. Executive Summary

1.1. Opinion

The Democratic Republic of Congo (DRC) is one of the Global Fund's three largest portfolios; as such, it is critical to the organization's mission to end HIV, tuberculosis and malaria. DRC grants are implemented in a challenging operating environment characterized by poor infrastructure, recurring armed conflicts and repeated outbreaks. The Global Fund Secretariat selected Population Services International (PSI) to implement a malaria grant worth US\$173.5 million, the main activity of which was the mass distribution of long-lasting insecticidal nets (LLINs).

In 2017, PSI alerted the OIG to potential irregularities in transportation tenders in the malaria grant. The resulting OIG investigation report¹ published in 2019 and supported by PSI's Global Internal Audit team and PSI Headquarters' management team, found non-compliant expenditures totaling US\$23.7 million, including potential losses of US\$7.4 million due to overpricing which PSI has refunded in full.

OIG performed a follow-up review of the Global Fund grants in DRC in 2018². However, as PSI had stopped implementing Global Fund supported programs in DRC at the time of the audit, the corresponding financial records relating to its grant were not accessible. OIG provided PSI additional time to gather and make available the relevant records, which were provided in various tranches between May and November 2019. This report concludes on the results of this standalone financial audit of the specific PSI grant.

The audit found weaknesses in PSI's detailed budget monitoring, limited controls over the payments of transactions, and recurring practices of non-competitive procurements. There were also significant non-compliant transactions. From an audit sample of US\$77.5 million, OIG found a total non-compliant amount of US\$25.3 million, of which US\$6.2 million is considered potentially recoverable. Assurance arrangements in place, as well as the Global Fund Secretariat's weak grant management oversight and monitoring, were unable to detect or prevent these issues. Overall, OIG found PSI's financial management of the grant and the Global Fund Secretariat's oversight of the grant to be **ineffective**.

Ineffective budget oversight resulted in an unapproved budget overspend of US\$12.8 million

PSI lacked an effective mechanism to monitor the budget by grant activity. While the total budget overrun was 2.6% on the US\$173.5 million grant, there was unauthorized budget overspend of US\$12.7 million at the cost category level, mainly travel-related costs and external professional services, against the initial budget of US\$20.4 million. This provided an inaccurate view of the utilization of grant funds.

The Secretariat did not comply with the protocols set out in the Grant Confirmation and instead communicated directly with PSI's local implementer. Given that some of these communications were to perform specific activities outside of the approved budget and to request PSI's justification on the budget variances, this miscommunication affected PSI's ability to effectively monitor budget variances.

Ineffective use of grant funds due to weaknesses in internal controls, gaps over financial management and weak procurement practices

Financial review of grant expenditures

¹ https://www.theglobalfund.org/media/8376/oig_gf-oig-19-006_report_en.pdf

² See OIG "Follow-up audit of Global Fund Grants in the Democratic Republic of Congo", GF-OIG-19-014, July 2019

Weak oversight and limited assurance mechanisms at all levels impacted the quality of evidence to support payments. OIG performed a financial review of the grant, selecting a sample of 56% (US\$77.5 million³) of US\$130 million expenditures⁴, in accordance with the Global Fund's Budgeting Guidelines⁵ that define the eligibility of grant expenditures for each type of transaction⁶.

Table 1 (lines 1-5) details a total of US\$5.9 million potentially recoverable amounts for transactions where either no supporting documents were provided (\$0.4 million), transactions were insufficiently supported⁷ (US\$2.2 million), or at least one key document was missing (US\$3.3 million).

A key element of an LLIN mass campaign is the 'micro plan', a document signed by the National Malaria Program detailing the budget and the activities to be performed throughout the campaign. In the absence of an approved micro plan, which is considered the detailed roadmap for the execution of the mass campaign, transactions are considered non-compliant as per Global Fund budgeting guidelines. However, notwithstanding the absence of this approved micro plan, OIG was able to establish that the reported activities were indeed performed and the LLINs were procured and distributed. Therefore, whilst the amount in Table 1 (line 3, US\$7.0 million) is non-compliant, OIG does not propose its recovery.

Weak monitoring by PSI's central headquarters procurement unit over the procurements made by its local entity in DRC resulted in non-competitive and non-transparent processes for purchases of goods and services. Procurements performed by PSI's contracted fiduciary agents did not follow any procurement policy, and the contracts signed with those agents are silent on this matter. This has resulted in non-transparent and non-competitive procurement expenditures of US\$5.0 million, as shown in line 5, Table 1. OIG proposes for recovery US\$0.1 million of these expenditures where the audit found evidence of overpricing. These relate to the procurement of vehicles, which were overpriced by 17% compared with similar procurements made centrally by PSI in the same period for the same vehicles. For the remaining amounts, OIG was able to verify that the goods had been delivered and did not find evidence of over-pricing. Therefore, OIG is not proposing recovery for these non-compliant amounts.

Non-compliance with Global Fund Policies

Additional non-compliant amounts identified by OIG relate to an extra payment of US\$3.4 million from grant funds as Indirect Cost Recovery (ICR)/support costs to PSI. This is in contradiction with Global Fund policy, which stipulates that no ICR should be paid to a Principal Recipient when using a fiduciary agent's services⁸. However, despite the amount being included in a number of budget revisions, the Global Fund Secretariat did not dispute the amount during the grant making process, and it was not highlighted as non-compliant by the Local Fund Agent. The Secretariat has agreed to review these costs to determine whether they should be retroactively allowed or recovered.

Approximately US\$1.6 million of additional transactions related to procurement and supply chain management were wrongly recorded in other budget categories. As a result of this misclassification, these amounts were not part of OIG's Investigation scope and therefore not included in the previous recovery calculation. An additional recovery of US\$0.2 million, based on the previously agreed recovery methodology for procurement and supply chain costs⁹, is proposed.

³ This sample included transactions that were paid both from DRC and from PSI Headquarters in the USA.

⁴ The supply chain related costs pertaining to the LLIN mass campaign distribution, which amounted to US\$ 38.8 million, were excluded from the scope of the review. This supply chain line item was previously reviewed by a separate OIG investigation, following specific allegations of overpricing in those costs (see OIG investigation report "Global Fund Grants in the Democratic Republic of Congo - Tender manipulation and overpricing in Malaria grant", GF-OIG-19-006, March 2019)

⁵ Global Fund Guidelines for Grant Budgeting and Annual Financial Reporting August 2014; and The Global Fund Guidelines for Grant Budgeting June 2017.

⁶ https://www.theglobalfund.org/media/3261/core_budgetingglobalfundgrants_guideline_en.pdf - Page 25 to 30

⁷ In this specific circumstance, the OIG could not accept copies as supporting documents for transactions recorded and paid for in DRC.

⁸ Fiduciary agents hired by PSI in the DRC had a specific and unique role. In a typical Global Fund grant, the role of fiduciary agent is to manage and control the banking and financial arrangements and ensuring compliance with all financial requirements of the Global Fund. However, although the fiduciary agents did not implement program activities, their roles and responsibilities were similar to a Global Fund grant sub-Recipient; for example, in the DRC, two of the four Fiduciary Agents hired contractors and suppliers.

⁹ This amount was calculated on the recovery methodology calculation for procurement and supply chain costs reviewed in the OIGs Investigation GF-OIG-19-006.

A further amount of US\$3.8 million of travel costs is considered non-compliant, representing the difference between the overbudgeted amounts less the amounts already listed in Table 1 (as part of items 1-5). OIG was able to verify the authenticity of the supporting documents and has therefore not classified these expenses as recoverable. However, the Secretariat has agreed to review the expenses that exceeded the approved budget to determine whether they should be retroactively allowed or recovered.

The Global Fund Secretariat, and its various assurance providers, did not effectively identify the existence and the extent of the issues noted above, either in the course of their routine oversight activities or during their periodic reviews.

Table 1: Summary of non-compliant and potentially recoverable amounts

Category	Non-Compliant Amount	Potential Recovery Amount
1. Absence of supporting documents	\$369,818	\$369,818
2. Absence of original supporting documents (only photocopies)	\$2,177,244	\$2,177,244
3. Absence of 'micro plan' /Terms of Reference for the mass campaign nets distribution	\$7,040,215	\$0
4. Absence of key documents	\$3,322,052	\$3,322,052
5. Non-transparent and non-competitive procurement	\$4,964,680	\$98,641
Subtotal 1: Financial Review of Grant Expenditures	\$17,874,009	\$5,967,755
6. ICR (7%) on Fiduciary Agent's contract transactions	\$3,414,127	\$0
7. Transactions misclassified and not scoped by the investigation in their final calculation of loss	\$229,909	\$229,909
8. Difference between the over budget expenses in the Travel related cost category less the non-compliant amounts for the same category noted above	\$3,817,820	\$0
Subtotal 2: Non-compliance with Global Fund policies and guidelines	\$7,461,856	\$229,909
TOTAL	US\$25,335,865	US\$6,197,664

1.2. Rating

	Objective 1. Reported expenditures are incurred in accordance with the terms of the grant agreement, and the agreed budget and work plan. Detailed transactions reconcile with the financial statement in the Progress Update and Disbursement Request (PUDR) for the audited period. Ineffective.
	Objective 2. Transactions are supported by adequate documentation confirming their completeness, accuracy and occurrence of underlying events, including value for money. Ineffective.

1.3. Summary of Agreed Management Actions

In addition to the Agreed Management Actions from the OIG investigation report GF-OIG-19-006 (Global Fund Grant in the Democratic Republic of Congo – Tender manipulation and overpricing in Malaria grant), the Secretariat will finalize and pursue, from PSI, an appropriate recoverable amount from the non-compliant expenditures identified in this report.

2. Background and Context

2.1. Overall Context

The DRC is the second largest country by area in Africa, and the third most populated. A national census has not been conducted since 1984, but the Ministry of Health estimates the population to be 94,538,256 in 2019¹⁰. The country ranks 176 out of 187 countries on the 2017 Human Development Index¹¹ and 161 of 180 on the 2017 Corruption Perceptions Index¹²

The health system is organized into 516 health zones (“Zones de Santé”) spread over 26 provinces. The human resources for health professional density is 6 doctors¹³, nurses and midwives per 10,000 people, far below both the World Health Organization’s recommendation of 23/10,000 and the regional average.

The DRC is a challenging operating environment due to its limited infrastructure, military instability in parts of the country, and the threat of deadly epidemics. In August 2018, the DRC experienced its 10th Ebola outbreak in 40 years¹⁴, producing 319 confirmed Ebola cases and 167 deaths by 31st December 2018.

2.2. Differentiation Category for Country Audits

The Global Fund has classified the countries in which it finances programs into three overall portfolio categories: focused, core and high impact. These categories are primarily defined by size of allocation amount, disease burden and impact on the Global Fund’s mission to end the three epidemics. Countries can also be classed into two cross-cutting categories: Challenging Operating Environments and those under the Additional Safeguards Policy. Challenging Operating Environments are countries or regions characterized by weak governance, poor access to health services, and man-made or natural crises. The Additional Safeguards Policy is a set of extra measures that the Global Fund can put in place to strengthen fiscal and oversight controls in a particularly risky environment.

The Democratic Republic of Congo is:

- Focused: (Smaller portfolios, lower disease burden, lower mission risk)
- Core: (Larger portfolios, higher disease burden, higher risk)
- High Impact: (Very large portfolio, mission critical disease burden)**

- Challenging Operating Environment**
- Additional Safeguards Policy**

2.3. Global Fund Grants in Democratic Republic of Congo

The Additional Safeguards Policy (ASP) was invoked for the DRC portfolio in 2011 as a consequence of the country’s need to rebuild its systems, infrastructure and capacity following 21 years of conflict. The ASP was invoked and subsequently reaffirmed by the Secretariat because of weak governance and security threats, the weak management capacity of National Programs, and concerns about corruption and a widespread lack of public accountability. The ASP allowed the Secretariat to put specific safeguards in place, such as the Global Fund’s ability to directly select Principal Recipients (PRs), Local Fund Agent assessments of sub-recipients (SRs), Global Fund control over PR-SR

¹⁰ Plan stratégique national de lutte contre le paludisme 2016–2020, Tableau I : Répartition de la population de la RDC par province (page 3)

¹¹ <http://www.hdr.undp.org/en/countries/profiles/COD>

¹² https://www.transparency.org/news/feature/corruption_perceptions_index_2017

¹³ https://www.who.int/hrh/fig_density.pdf?ua=1

¹⁴ <https://www.msf.org/drc-2018-ebola-outbreak-crisis-update>

management, procurement through an international procurement agent (UNDP and PSI), and additional capacity assessments of the National Programs.

The Global Fund has signed grants of over US\$1.99 billion and disbursed US\$1.58 billion to DRC¹⁵ since 2003; this includes US\$543 million related to five active grants for the January 2018 to December 2020 implementation period, and US\$597 million for the 2015 - 2017 implementation period.

Population Services International (PSI), an International Non-Governmental Organization, was Principal Recipient from 2011 to the 2015–2017 funding cycle. It was discontinued as Principal Recipient for the following cycle (2018 to 2020)¹⁶.

PSI acted as the Principal Recipient and the signatory of the grant agreement, while program implementation in DRC was done through a local entity - Association de Santé Familiale (ASF), a financially consolidated member of the PSI network. PSI and ASF separated in 2017, resulting in the suspension of all Global Fund program activities in DRC implemented by PSI, and the subsequent transfer of the implementation activities to another entity.

The Global Fund signed a Framework Agreement with PSI in 2015 to centralize the assurance mechanism, allowing PSI to rely on its own internal control framework for Global Fund grants:

- Country grant external audits were performed by an external auditor, selected globally by PSI Headquarters.
- PSI Headquarters' procurement process and internal controls were to be assessed periodically by the Global Fund or exceptionally by PSI's external auditor, at the request of the Global Fund.
- The Global Fund granted PSI an exception to opening grant- or country-specific bank accounts at PSI Headquarters, due to PSI's accounting model. Therefore, GF grant funds were commingled with other donors' funds and PSI corporate operating funds. As a compensating control, PSI assigned a specific general ledger code and separate accounting codes for each donor. Global Fund cash balances had to be certified quarterly by PSI's CFO and annually by PSI's external auditor.

During the 2015-2017 funding cycle, PSI implemented one of the three Global Fund malaria grants, the others being implemented by the Ministry of Health and a local NGO (SANRU). The main objectives of the PSI grant (COD-M-PSI) were to: 1) achieve at least 80% of people at risk of malaria sleeping under long-lasting insecticidal nets, 2) cover at least 80% of pregnant women attending ante-natal care with ITPp antimalarial drugs in 308 targeted Health Zones, 3) confirm at least 80% of suspected malaria cases by microscopy or rapid diagnostic tests, in 308 targeted Health Zones, and 4) treat all confirmed malaria cases according to national guidelines in public health facilities and community, in 308 targeted Health Zones.

In implementing the grant, PSI carried out LLIN mass distribution campaigns in 16 of the 20 initially targeted provinces of DRC, distributing 35.6 million LLINs, with some preparatory work done for the other four provinces.

The PSI grant was signed in April 2015 for an initial two-year implementation period, with an initial amount of US\$134.3million. In July 2016, the Global fund approved a third year of implementation and a budget increase of US\$39.2 million, bringing the total grant amount to US\$173.5 million. As of 31 December 2017, the Global Fund had disbursed US\$170.4 million and the total amount spent by PSI was US\$178 million, including an over-expenditure of US\$4.5 million.

¹⁵ <https://www.theglobalfund.org/en/portfolio/country/?loc=COD&k=8821256b-ea63-4407-adbf-3ddf43878055>

¹⁶ Prior to becoming Principal Recipient, PSI had also been implementing Global Fund programs in DRC as a sub-recipient under grants for which UNDP was the Principal Recipient.

Previously Identified Issues

In 2017, PSI alerted OIG to potential irregularities in transportation tenders. Subsequently, and supported by PSI management and its Global Internal Audit team, OIG carried out an investigation¹⁷ of the PSI grant, based on allegations of irregularities in transportation tenders received in May 2017 from PSI. The investigation reviewed a sample of procurement and supply-chain transactions totaling US\$38.1 million. It found non-compliant amounts of US\$23.7 million due to procurement irregularities and systemic overpricing, and potential losses of US\$7.4 million due to overpricing in transportation, warehousing and customs clearance expenditures to the Global Fund. PSI has since refunded the US\$7.4 million to the Global Fund.

Previous relevant OIG work
[Investigation on Tender manipulation and overpricing in Malaria grant GF-OIG-19-006](#)

[Audit of the Global Fund Grants to the Democratic Republic of the Congo GF-OIG-16-022](#)

[Country Audit of the Global Fund Grants to the Democratic Republic of Congo GF-OIG-09-007](#)

The 2016 Audit of the Global Fund Grants to the Democratic Republic of the Congo covered active grants implemented by the Ministry of Public Health of the Government of the Democratic Republic of Congo (Sanru, PSI, Cordaid and Caritas Congo) and their sub-recipients, from January 2014 to April 2016. The audit did not cover DRC-related procurement activities conducted by PSI headquarters, which represented around 11% of the total portfolio budget for 2015-2017. All Agreed Management Actions (AMAs) from the 2016 OIG audit were closed by 30 September 2018.

¹⁷ https://www.theglobalfund.org/media/8376/oig_gf-oig-19-006_report_en.pdf

3. The Audit at a Glance

3.1. Objectives

The audit sought to provide assurance on whether:

1. Reported expenditures were incurred in accordance with the terms of the grant agreement and agreed budget and work plan, and the detailed transactions reconciled with the financial statements in the Progress Update and Disbursement Request (PUDR) for the audited period.
2. Transactions were supported by adequate documentation confirming their completeness, accuracy and occurrence of underlying events, including value for money.

3.2. Scope

This follow-up audit was performed in accordance with the methodology described in Annex B and covered the review of the grant implemented by the Principal Recipient (PSI) and key implementers, including the fiduciary agents and other sub-recipients. As the grant ended on 31 December 2017, the audit focused on a financial review of grant transactions from January 2015 to December 2017 and did not include a review of programmatic or supply chain activities. Assurance on the broader programmatic objectives of the DRC grants is provided in an earlier report of the OIG follow-up audit, published in July 2019¹⁸.

Due to the separation between PSI and its local implementing affiliate in DRC, PSI ceased implementing the Global Fund grant in DRC. OIG could not perform any review of this grant during the DRC follow-up audit performed in 2018, because supporting documentation was not accessible at the time of the audit. As a result, this follow-up audit for PSI was scheduled for 2019 and OIG performed the review in multiple stages as the relevant documentation became available, between April and September 2019, both in DRC and at PSI Headquarters in Washington, D.C.

Exclusion from scope

Procurement and Supply Chain Management costs transactions pertaining to the LLIN mass campaign distribution (US\$38.8 million) were excluded from the scope of the audit review as they were previously reviewed during the OIG investigation¹⁹.

¹⁸ See OIG "Follow-up audit of Global Fund Grants in the Democratic Republic of Congo", GF-OIG-19-014, July 2019

¹⁹ https://www.theglobalfund.org/media/8376/oig_gf-oig-19-006_report_en.pdf

4. Findings

4.1. Ineffective budget oversight resulted in an unapproved budget overspend at category level of US\$12.8 million

PSI monitors the implementation of grant activities of its network members in countries through regular Activity Status Reports and monthly financial reviews. The effectiveness of the monitoring and financial oversight mechanisms, by PSI and by the Global Fund and its assurance providers, was significantly limited by a series of specific circumstances, as follows:

PSI's inability to get accurate information from the PSI DRC team: Information requested by PSI Headquarters from its local affiliate was not always communicated in a timely and accurate manner. This affected PSI's ability to effectively monitor the budget and to justify the different variances at the cost category level. These concerns were escalated internally to PSI's Global Internal Audit team which performed a targeted internal audit, the findings of which were communicated to OIG and ultimately led to the OIG Investigation, published in 2019.

Lack of budget monitoring at grant activity level: For the NFM1 grant implementation period (2015-17), PSI did not monitor budgets at an activity level, but rather at the cost category level. In the absence of detailed monitoring, PSI could not link each activity and the allocated budget with the expenses booked in PSI's general ledger. As a result, PSI could not explain the significant budget variances for travel and professional services costs, or seek Secretariat approval for non-budgeted amounts exceeding the authorized limits, as required by Global Fund guidelines²⁰.

Expenses budget under the previous grant were booked under the NFM grant: The 2012-2014 Single Stream of Funding (SSF) grant should have been closed after the grant period ended, but closure activities were never performed. This, as well as unclear communication between the Secretariat and PSI, resulted in confusion around the actual cash balance of the SSF grant and the final reporting for SSF expenditures by PSI. PSI continued to report the SSF grant expenditures to the NFM grant until 2017, at which point it was requested to report these expenditures separately. This movement of expenses impacted PSI's ability to effectively monitor the grant budget. PSI's external auditor did not provide, nor did the Global Fund Secretariat seek, assurance over the cash balance at the end of the SSF grant. Based on multiple communications between the Global Fund Secretariat and PSI, expenses and fees incurred as part of the SSF grant were reclassified several times and moved back and forth between the old SSF and the new NFM grants. This meant that for part of the NFM grant implementation period, PSI reported actual expenditures for two grants (NFM and SSF) against the NFM budget only. The lack of timely closure of the previous grant and a clear agreement on the handling of the remaining costs served to weaken the overall monitoring of the current grant budget.

Non-compliance with the communication protocols by the Secretariat: The Global Fund's Grant Confirmation was signed by PSI, not by PSI's local implementing affiliate. The Grant Confirmation defines that the relevant contact for communication is PSI Headquarters. However, the Secretariat did not strictly comply with these protocols and instead communicated directly with PSI's local implementer without routinely including the appropriate personnel at PSI Headquarters in Washington in the communication. Given that some of these communications were to perform specific activities outside of the approved budget and to request PSI's justification on the budget variances, this miscommunication affected PSI's ability to effectively monitor budget variances.

The overall budget of the grant was overspent by 2.6% before the recovery of US\$7.4 million following the OIG Investigation, with certain cost categories being exceeded significantly – namely US\$7.0 million of additional travel expenditures (a discretionary cost category) and US\$5.7 million

²⁰ The 2017 Global Fund's Budgeting Guidelines - Page 19 and 58 to 59; the 2014 Global Fund Guidelines for Grant Budgeting and Annual Financial Reporting 2014 – page 27 to 30

of additional external professional services costs (not considered a discretionary cost category). See figure 1 below for further details.

Table 2: Analysis of grant budget expenditure vs actual expenditure

Cost Categories	Approved Budget (including approved reprogramming)	Grant Cumulative Expenditures (including appropriate allocation)	Amount Budget Overspend	% overspent	Overspend beyond the 5% budget flexibility
Travel related costs	US\$19,084,322	US\$27,056,530	(US\$7,972,208)	42%	(US\$7,017,992)
External Professional services	US\$1,306,729	US\$7,033,832	(US\$5,727,103)	438%	(US\$5,661,767)
Programme Administration costs	US\$13,381,442	US\$14,161,404	(US\$779,962)	5%	(US\$110,890)
TOTAL					(US\$12,790,649)

According to the Global Fund’s Budgeting Guidelines, any budget overrun above 5% for discretionary cost categories is a material revision²¹, which requires written pre-approval from the Global Fund which was not sought in this case. See Finding 4.2 for more details on these amounts.

Misclassification of expenses: Ineffective budget monitoring at the activity level is further illustrated by a significant amount of misclassification of expenditures charged to different cost categories, especially for transactions expensed in DRC. Out of the US\$77.5 million transactions tested by the OIG in DRC, 17.8% were classified in the wrong cost categories. This calls into question the depth and quality of the review of the grant’s transactions and related reporting by the different assurance providers.

The misclassifications include transactions totaling US\$1.6 million that should have been categorized under cost category 7 (Procurement and Supply-Chain Management) but which were wrongly allocated across other cost categories and which were consequently not included in the OIG’s investigation calculation of potentially recoverable amounts. See amounts noted in Finding 4.2.

Gaps in Global Fund oversight and assurance: The continuous budget overruns throughout the life of the grant, and the PSI’s local affiliate team’s inability to provide evidence-based budget variance analysis and to monitor the budget by activity, were known to the Global Fund Secretariat. Key financial data were not reconciled between reported expenditures in the audited financial statements, the Annual Financial Report provided by PSI in the Progress Update and Disbursement Request (PUDR), and PSI’s general ledger. Although there was no mechanism to address the associated risks, the Global Fund continued to disburse funds to PSI, and there is no evidence that the matter was escalated and discussed with PSI Headquarters by Global Fund senior management.

There were delays in communicating the findings of the PUDR to PSI, and there was no Secretariat follow-up on these findings. While the Secretariat does not define a timeline for sending PUDR review results to PRs, in the case of DRC, a Management Letter was not issued until a full year after the end of the reporting date, hindering timely decision-making. When issued, Management Letters were sent to the team in DRC without copying the relevant personnel in PSI Headquarters, which affected PSI Headquarters’ ability to effectively investigate and address the issues with the local entity.

²¹ The default definition of a discretionary cost category includes: human resources, vehicles, travel-related costs (per diems, etc.) and indirect costs/overheads.

Lack of clarity on roles and responsibilities for providing assurance: There was a lack of clarity over which assurance provider should review certain transactions and grant assets. For example, according to its Framework Agreement with the Global Fund, PSI is not required to have a dedicated bank account for Global Fund funds; instead, the External Auditor is required to certify the cash balance for each Global Fund grant on an annual basis. However, although PSI sent quarterly fund positions to the Secretariat, none of the Global Fund grants received any independent opinion on Grant Fund cash balances, as required. The external auditor did not express an opinion on grant cash balances in its annual report, having not been requested to do so. Additionally, the Framework Agreement stipulates that the LFA should review the local expenditures incurred in DRC. However, the LFA did not review any local expenditures incurred by the Fiduciary Agent.

Following the OIG investigation of the PSI grant in 2017, the Secretariat and PSI carried out several actions to improve grant oversight including:

- The establishment of cross-functional INGO monitoring group at the Secretariat level to monitor the grant performance and support the Country Teams to unlock bottlenecks in grant implementation;
- The establishment of Global Fund Management Unit (GFMU) at PSI level to strengthen the oversight of the country offices by performing monthly review with the country offices and quarterly reviews with PSI senior management;
- A periodic assessment of International NGOs by a multidisciplinary team within the Global Fund to re-asses the design and operating effectiveness of PSI controls; and
- A reinforced external audit approach for PSI including a change of the auditor, realigning the audit ToRs to the Global Fund standard ToR and more targeted agreed-upon procedures to address critical financial risks.

Agreed Management Action:

There is no additional Agreed Management Action related to the shortcomings listed in the section above.

The issues identified will be mitigated through the implementation of the Agreed Management Actions (numbers 1 and 4) of the OIG investigation report GF-OIG-19-006 (Global Fund Grant in the Democratic Republic of Congo – Tender manipulation and overpricing in Malaria grant). In particular, the prior Investigation requires the Secretariat to:

- AMA1: Evaluate the design and effectiveness of the internal controls implemented by PSI through the creation of a Global Fund Management Unit to mitigate similar future risks; and
- AMA 4: Reevaluate its framework agreement with PSI, based on an evaluation of the effectiveness of PSI's internal controls as part of AMA 1, to clarify the scope of responsibility between different assurance providers, including defining the criteria for the scope of verifications to be conducted by these assurance providers. Furthermore, the Global Fund will review the assurance arrangements with other international non-governmental organizations to determine whether revisions are required to their respective assurance arrangements and framework agreements, and develop a plan to implement any revisions identified.

Although progress has been made in these areas, none of the Agreed Management Actions have yet been fully implemented.

4.2. Ineffective use of grant funds due to weaknesses in internal controls, gaps over financial management, and weak procurement practices

Since August 2011, the Global Fund portfolio in DRC has been managed under the “Additional Safeguards Policy”.²² Justifications for invoking additional safeguards included: weak management and the lack of internal control capacities of Principal Recipients and sub-recipients; weak capacity and oversight of the Country Coordinating Mechanism; and political instability. Due to continued structural weaknesses, the following safeguards remain in force: the selection of Principal Recipients by the Global Fund; specific oversight over the selection and management of sub-recipients by the Principal Recipients; tailored risk mitigation and procurement arrangements.

PSI had implemented malaria grants in DRC as Principal Recipient since 2011; its presumed sound financial management system was one of the criteria for its selection as a Principal Recipient. This audit found material gaps in the payment process and in the quality of supporting documents²³, as well as non-compliance with Global Fund policies.

OIG conducted its review in line with Global Fund Budgeting Guidelines, especially as they relate to the eligibility of grant expenditures, and the minimum documentation required to validate each transaction²⁴. The audit sampled grant transactions for a total amount of US\$77.5 million, made up of transactions paid by the local PSI affiliate in DRC (US\$31.6million) and those paid by PSI Headquarters (US\$45.9 million). The audit scoped out all supply chain transactions pertaining to the LLIN mass campaign distribution (US\$38.8 million) to avoid any duplication with the previous OIG investigation.

Overall, for the audit sample of US\$77.5 million, the OIG found a total amount of US\$25.3 million that was non-compliant, of which US\$6.2 million is considered potentially recoverable, as explained in the table below.

Table 3: Summary of non-compliant and potentially recoverable amounts

Category	Non-Compliant Amount	Potential Recovery Amount
1. Absence of supporting documents	\$369,818	\$369,818
2. Absence of original supporting documents (only photocopies)	\$2,177,244	\$2,177,244
3. Absence of ‘micro plan’ /Terms of Reference for the mass campaign nets distribution	\$7,040,215	\$0
4. Absence of key documents	\$3,322,052	\$3,322,052
5. Non-transparent and non-competitive procurement	\$4,964,680	\$98,641
Subtotal 1: Financial Review of Grant Expenditures	\$17,874,008	\$5,967,755
6. ICR (7%) on Fiduciary Agent's contract transactions	\$3,414,127	\$0
7. Transactions misclassified and not scoped by the investigation in the final calculation of loss	\$229,909	\$229,909
8. Difference between the over budget expenses in the Travel related cost category less the non-compliant amounts for the same category noted above	\$3,817,820	\$0
Subtotal 2: Non-compliance with Global Fund policies and guidelines	\$7,461,856	\$229,909
TOTAL	US\$25,335,865	US\$6,197,664

²² The Additional Safeguards Policy is invoked to enable the Global Fund to institute appropriate risk mitigation measures where Global Fund monies could be placed in jeopardy.

²³ OIG review was performed based on the requirement stated in the Global Fund Guidelines for Grant Budgeting (2017) – Section 5: Eligibility of Grant expenditures and recovery process P25 to P28

²⁴ https://www.theglobalfund.org/media/3261/core_budgetingglobalfundgrants_guideline_en.pdf page 25 to 28]

Financial Review of grant expenditures

1. *Absence of supporting documents.* Expenditures where no supporting documents were provided to the OIG for review totalled US\$0.4 million. While such payments were identified across the grant, more than 65% of these expenditures were found in the travel-related cost category.

2. *Missing original supporting documents.* For transactions recorded and paid in DRC totalling US\$2.2 million, copies as opposed to original supporting documents were provided. Given the specific circumstances of this grant - the known weaknesses in internal controls and oversight and the proven fraud in the same grant executed by the same entity during the same period – OIG could not accept copies as supporting documents for the recorded transactions, and therefore proposes the amounts for recovery.

3. *Absence of mass campaign micro plans.* The micro plan is an important document, detailing the scope of a mass campaign, its budget, and the activities to be performed. As per the Global Fund's Budgeting Guidelines, transactions are classified as non-compliant if their terms of reference (in this case the micro plan) are absent. However, notwithstanding the absence of this micro plan, OIG was able to establish that the reported activities were indeed performed and the LLINs were procured and distributed. Therefore, whilst those amounts (US\$7.0 million) are considered non-compliant, OIG does not propose their recovery.

4. *Absence of key documents.* Through its review, OIG found that transactions totaling US\$3.3 million were not supported by key documents to justify that the activity had happened, or that goods and services were received. Missing contracts, invoices, absence of proof of payments and/or proofs of delivery are the main reasons why the amounts are proposed for recovery. 55% of these unsupported transactions were identified in the travel-related cost category of the grant.

5. *Non-transparent and non-competitive procurements.* During grant implementation, the procurement of goods and services was performed through three channels. Procurements of health products were carried out by PSI Headquarters, while local procurements of goods and services were performed by PSI's local implementer for goods and services related to the LLIN mass campaign distribution. PSI's local implementer also sub-contracted fiduciary agents to carry out payments for distribution activities and to procure related items. Procurements performed by the contracted fiduciary agents did not follow any procurement policy, and the contracts signed with those agents were silent on this matter. PSI's local implementer's policies for purchasing goods and services were vague and non-specific, allowing for national instead of international bidding and restrictive tenders to be used. This resulted in non-compliant procurement expenditures of US\$5.0 million, as shown in the table above. OIG proposes for recovery US\$0.1 million of expenditures where the audit found evidence of overpricing. These relate to the procurement of vehicles, which were overpriced by 17% compared with similar procurements made centrally by PSI in the same period for the same vehicles.

For the LLIN procurements performed by PSI Headquarters (around US\$44 million), the OIG found evidence of fair competition and transparency in the selection of suppliers.

Non-compliance with Global Fund policies and guidelines

6. *ICR (7%) on Fiduciary Agents contract transactions.* PSI was selected as a Principal Recipient in DRC partly in reliance on its sound financial controls to manage the grant. However, PSI was not able to fully implement grant activities, especially with regards to payments for the mass campaign distribution activities. Thus, PSI requested the Global Fund Secretariat to approve the use of four fiduciary agents to carry out payments for activities, to mitigate the fiduciary risks associated with managing cash in remote locations in DRC, and to ensure appropriate supporting documents would be available at the central level (Kinshasa)²⁵. In addition to an average 11% of management and

²⁵ Fiduciary agents hired by PSI in the DRC had a unique and broader role as compared to the traditional fiduciary agents generally hired under the Global Fund programs. In a typical Global Fund grant, the role of the fiduciary agent is to manage and control the banking and financial arrangements and to ensure compliance with all financial requirements of the Global Fund. In the case of DRC, the fiduciary agents actually carried out many activities traditionally associated with an implementing sub-recipient or a procurement agent.

transfer fees charged by the fiduciary agents, PSI charged an extra 7% as support costs, totalling US\$3.4 million.

This is contrary to the Global Fund policy²⁶ that states “*Funding for support costs and ICR shall not be applied when a financial management intermediary (i.e. a “fiduciary agent” or “fiscal agent”) is appointed to oversee and verify expenditures of grant funds*”. The Support Cost policy was updated in March 2015, one month before the signature of the grant; however, the budget negotiated with PSI was based on the old policy and the Secretariat did not update the final budget in line with the new policy. While PSI remains obliged to comply with all Global Fund policies as stipulated in the grant agreement²⁷, it is unclear whether the amount was charged with the consent of the Global Fund Secretariat, therefore the OIG deems this expense non-compliant. The Secretariat has agreed to review these charges to determine whether they should be retroactively allowed or recovered.

7. Transactions misclassified and not scoped by the OIG investigation in their final loss calculation. Approximately US\$1.6 million of additional transactions related to procurement and supply chain management were wrongly recorded in other budget categories. As a result of this misclassification, these amounts were not part of the OIG’s Investigation scope, and therefore not included in the previous recovery calculation. An additional recovery of US\$0.2 million is proposed for recovery²⁸.

8. Difference between over-budget expenses in the travel-related cost category and non-compliant amounts in the same category. Because PSI significantly exceeded the budget for discretionary travel costs by more than the Global Fund’s allowable limit of 5% without obtaining pre-approval from the Secretariat, these amounts are deemed non-compliant. The Secretariat has agreed to review these expenses to determine whether they should be retroactively allowed or recovered.

Expenses for external professional services costs also exceeded their budget significantly, however these are not considered by the Global Fund to be discretionary costs and are therefore not subject to the same cost category restrictions as discretionary costs. Therefore, OIG does not consider these amounts to be non-compliant or recoverable.

Agreed Management Action 1:

Based on the findings of this report, the Secretariat will finalize and pursue, from PSI, an appropriate recoverable amount from the non-compliant expenditures identified in this report. This amount will be determined by the Secretariat in accordance with its evaluation of applicable legal rights and obligations and associated determination of recoverability.

Owner: Head Grant Management Division

Due date: 31 December 2020

In addition to the AMA stated above, the shortcomings related to this section will be mitigated through the implementation of the AMA 3 of the OIG investigation report GF-OIG-19-006 (Global Fund Grant in the Democratic Republic of Congo – Tender manipulation and overpricing in Malaria grant).

Investigation AMA 3: The Global Fund Secretariat will update its Guidelines for Grant Audit to ensure that the auditor engagement includes a review of the controls related to Principal Recipient hired third party agents (including fiduciary agents).

²⁶ https://www.theglobalfund.org/media/3266/core_operationalpolicy_manual_en.pdf Page 65 and page 71

²⁷ Extract from the Grant Agreement: “*The Grantee shall implement the program in accordance with the detailed Program budget agreed with the Global Fund and adhere to the provisions of the “Global Fund Guidelines for Grant Budgeting and Annual Financial Reporting” (2014, as amended from time to time), available at the Global Fund’s Internet site, throughout the Implementation Period*”.

²⁸ This amount was calculated on the recovery methodology calculation for procurement and supply chain costs reviewed in the OIGs Investigation GF-OIG-19-006.

The Global Fund through the grant external audit process will review the terms and conditions of the engagement of such third-party agents, including their adherence to such terms and conditions, specifically when the Global Fund Secretariat considers those fiduciary agents as a risk mitigation factor.

5. Table of Agreed Actions

Agreed Management Action	Target date	Owner
1. Based on the findings of this report, the Secretariat will finalize and pursue, from PSI, an appropriate recoverable amount from the non-compliant expenditures identified in this report. This amount will be determined by the Secretariat in accordance with its evaluation of applicable legal rights and obligations and associated determination of recoverability.	31 December 2020	Head, Grant Management Division

Annex A: General Audit Rating Classification

<p>Effective</p>	<p>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.</p>
<p>Partially Effective</p>	<p>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.</p>
<p>Needs significant improvement</p>	<p>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.</p>
<p>Ineffective</p>	<p>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.</p>

Annex B: Methodology

The OIG 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 documents 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 at the Global Fund as well as in country 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 focus on issues related to the impact of Global Fund investments, procurement and supply chain management, change management, and key financial and fiduciary controls.