



INTERNAL AUDIT DIVISION

AUDIT REPORT

Audit of UNHCR operations in the Russian Federation

Overall results relating to the effective management of UNHCR operations in the Russian Federation were initially assessed as unsatisfactory. Four recommendations have been implemented; implementation of two recommendations remains in progress

FINAL OVERALL RATING: PARTIALLY SATISFACTORY

27 November 2012

Assignment No. AR2011/121/02

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AUDIT REPORT

Audit of UNHCR operations in the Russian Federation

I. BACKGROUND

1. The Office of Internal Oversight Services (OIOS) conducted an audit of the United Nations High Commissioner for Refugees (UNHCR) operations in the Russian Federation.
2. In accordance with its mandate, OIOS provides assurance and advice on the adequacy and effectiveness of the United Nations internal control system, the primary objectives of which are to ensure (a) efficient and effective operations; (b) accurate financial and operational reporting; (c) safeguarding of assets; and (d) compliance with mandates, regulations and rules.
3. UNHCR has been present in the Russian Federation since 1991 when the office in Moscow was established. Since then, UNHCR has been providing protection, support, material assistance to refugees and asylum seekers mostly originating from Afghanistan, several African, Middle East countries, and the former Union of Soviet Socialist Republics. The UNHCR Representation in the Russian Federation (the Representation) has also been involved in assisting the Russian Government to solve statelessness problems resulting from the break-up of the former Soviet Union. In the North Caucasus, UNHCR has been assisting and protecting persons who have been internally displaced by the various armed conflicts, especially by the two Chechnya wars (1994-96 and 1999-2001). In line with its disengagement policy in the North Caucasus, the Representation's office in Vladikavkaz was closed on 30 June 2011. The closure has left the Representation without a presence in this area and UNHCR operations will be monitored and managed through missions from Moscow.
4. The Representation is headed by a Representative at the D-1 level, supported by 58 staff members. The budgets for the Representation averaged \$12.3 million per year for the three years to 2011. The Representation works with 15 implementing partners (IPs) for the delivery of assistance to persons of concern and implementation of its programmes. IP budgets constituted about 45 per cent of the total budgets for the operations in the Russian Federation.
5. Comments provided by the Representation are incorporated in *italics*.

II. OBJECTIVE AND SCOPE

6. The audit was conducted to assess the adequacy and effectiveness of the Representation's governance, risk management and control processes in providing reasonable assurance regarding the **effective management of UNHCR operations in the Russian Federation**.
7. The audit was included in the 2011 OIOS risk-based work plan in agreement with the Bureau for Europe, taking into consideration that the operation in the Russian Federation is one of UNHCR's largest operations in Europe and the planned scaling down of operations in 2011.
8. The key controls tested for the audit were: (a) project management; (b) regulatory framework; and (c) staff safety and security. For the purpose of this audit, OIOS defined these key controls as follows:

(a) **Project management** - controls that provide reasonable assurance that there is accurate and complete monitoring and reporting of project activities and that they are carried out in compliance with UNHCR policies and procedures;

(b) **Regulatory framework** - controls that provide reasonable assurance that policies and procedures: (i) exist to guide the operations in budget, finance, and procurement; (ii) are implemented consistently; and (iii) ensure the reliability and integrity of financial and operational information; and

(c) **Staff safety and security** – controls to provide reasonable assurance that safety and security programmes exist to ensure that staff are aware of UNHCR safety and security policies and procedures, and their responsibility for complying with them.

9. The key controls were assessed for the control objectives shown in Table 1.

10. OIOS conducted the audit from September to November 2011. The audit covered the period from 1 January 2009 to 30 August 2011. Of the 15 IPs operating in the country, OIOS reviewed two international and three local IPs with budgets aggregating \$11.4 million.

11. OIOS conducted an activity-level risk assessment to identify and assess specific risk exposures, and to confirm the relevance of the selected key controls in mitigating associated risks. Through interviews, analytical reviews and tests of controls, OIOS assessed the existence and adequacy of internal controls and conducted necessary tests to determine their effectiveness.

III. AUDIT RESULTS

12. The Representation's governance, risk management and control processes examined were assessed as **partially satisfactory** in providing reasonable assurance regarding **effective management of UNHCR operations in the Russian Federation**. OIOS made six recommendations in the report to address the issues identified in the audit. As regards project management, the Representation had: (a) strengthened controls for IP selection, retention and financial monitoring by setting up a multi-functional selection committee and preparing an action plan addressing weaknesses in the financial monitoring of IPs; and (b) initiated corrective action on the weaknesses regarding the IP external audit reports, but had yet to provide evidence that the audit reports now adhere to the rules. At the time of this report, the Representation had addressed the shortcomings that resulted in the initial unsatisfactory rating for regulatory framework by reinforcing controls to ensure compliance with rules governing the maintenance and processing of monthly accounts and petty cash reconciliations, strengthening payment approval and certification processes and enhancing oversight. New procurement actions were compliant with tendering guidelines. Progress was also being made on the recovery of Value Added Tax (VAT) paid by the Representation. The Representation's arrangements for staff safety and security were satisfactory.

13. The initial overall rating was based on the assessment of key controls presented in Table 1 below. The final overall rating is **partially satisfactory** as four important recommendations have been implemented. Implementation of two important recommendations remains in progress.

Table 1: Assessment of key controls

| Business objective | Key controls | Control objectives | | | |
|--|-------------------------------|------------------------------------|--|------------------------|---|
| | | Efficient and effective operations | Accurate financial and operational reporting | Safeguarding of assets | Compliance with mandates, regulations and rules |
| Effective management of UNHCR operations in the Russian Federation | (a) Project management | Partially satisfactory | Partially satisfactory | Partially satisfactory | Partially satisfactory |
| | (b) Regulatory framework | Partially satisfactory | Unsatisfactory | Unsatisfactory | Unsatisfactory |
| | (c) Staff safety and security | Satisfactory | Satisfactory | Satisfactory | Satisfactory |
| FINAL OVERALL RATING: PARTIALLY SATISFACTORY | | | | | |

A. Project management

Action has been initiated to ensure that IP audit certification complies with UNHCR guidelines

14. The IP external auditors did not comply with UNHCR rules on IP audit certification. Specifically:
- Recommended language and templates prescribed were not used;
 - There was no reference to the auditing standards applied;
 - Audit reports did not certify that the financial statements had been prepared in accordance with appropriate accounting standards;
 - The focus of the management letters was on compliance with Russian Federal Law on salary, taxes and employment laws and not on project-specific focus areas. The audit certification reports did not indicate that internal controls and financial management of the IP had been properly reviewed;
 - No assurance was provided as to compliance with the Terms and Conditions of the Agreement between UNHCR and the IP; and
 - The audit reports did not provide inputs on effective delivery of project services and resource utilization.

(1) The UNHCR Representation in the Russian Federation should set in place procedures to ensure that audit certification reports adhere to UNHCR guidelines, and management letters provide an assessment of implementing partners' internal controls, financial management of funds allocated and compliance with the terms and conditions of the agreement with UNHCR.

The UNHCR Representation accepted recommendation 1 and stated that the office introduced additional measures and tools to reinforce the oversight and monitoring of the audit certificates and compliance with financial rules and regulations governing the IP agreements. Future IP audit

reports would be compliant with UNHCR guidelines. Recommendation 1 remains open pending receipt of IP audit reports prepared in compliance with UNHCR IP audit certification guidelines.

Action was taken to ensure compliance with IP selection and retention procedures

15. There was inadequate compliance with the UNHCR guidelines on IP selection and retention. While the Representation had prepared a checklist for the one new IP it had entered into an agreement with, it had not prepared the checklist for IPs that continued to be associated with the UNHCR. The Representation had also decided not to set up an IP Selection Committee, advising that it had been working with the same partners for many years and was well acquainted with them. OIOS assessed that the capacity and performance of the IPs had not been evaluated as required in the guidelines, which raised concern that IPs could continue to work with UNHCR even when their performance may have been less than satisfactory in the past.

- (2) The UNHCR Representation in the Russian Federation should put in place a mechanism to ensure compliance with UNHCR guidelines for the selection and retention of implementing partners (IP), including the adoption of a risk-management approach, the use of an IP Selection Committee and review of IPs that have been working with the UNHCR for many years.**

The UNHCR Representation accepted recommendation 2 and stated that action to implement the recommendation had been completed. A mechanism in the form of a multi-functional selection committee composed of the Deputy Representative and Protection, Programme and Public Information Professional staff had been established in February 2012. A thorough review of the IPs was done by the multi-functional team at the 2012 planning stage and when developing the 2013 comprehensive plan. The analysis included a review of the efficiency of non-governmental organizations' work, impact on the lives of people of concern and cost-effectiveness for UNHCR. Based on the action taken by the Representation, recommendation 2 has been closed.

Oversight on financial reporting by an IP has improved

16. The UNHCR Manual requires that IPs maintain proper accounting records and related documentation and that amounts remaining unspent at the end of the year are refunded to UNHCR. OIOS selected sample transactions initiated by an international IP delivering health services and noted inadequate justification was provided for expenditures, persistent accounting errors resulting in under and overpayments that remained undetected, and unspent balances not returned to UNHCR. Further, the IP was permitted by the Representation to advance RR1.266 million (\$42,223) from 2010 funds towards meeting 2011 expenditures, on condition that the amounts would be recovered from the 2011 budget. This recovery, however, was only done subsequent to the audit.

- (3) The UNHCR Representation in the Russian Federation needs to put in place procedures to ensure that for an international IP the recording of expenditures is error free and consistent with proper record keeping, and during financial monitoring visits payment vouchers are cross verified.**

The UNHCR Representation accepted recommendation 3 and stated that it had been implemented. An action plan had been prepared and shared with the IP to ensure compliance and this had been followed up and monitored as part of the periodic financial monitoring. In the reports for the last quarter of 2011 and first quarter of 2012 no mistakes were detected. Cross-checks between payment vouchers and medical records were done with each Implementing Partner Financial Monitoring

Report (IPFMR) verification and reflected in notes for the files. IP staff responsible for verification of the invoices and detailed itemized bills from the clinics had been instructed to pay particular attention to this issue. Based on the action taken by the Representation, recommendation 3 has been closed.

IP financial management has been strengthened

17. The UNHCR Manual requires that IPs prepare bank reconciliations at the end of every month. Bank reconciliations provide assurance that transactions and movements of funds are consistently recorded. However, IPs receiving an average of \$2 million per year from UNHCR were only formally reconciling on a quarterly basis. Firms providing IP audit certificates in 2009 and 2010 accepted informal, undocumented monthly reconciliations as sufficient. However, quarterly bank reconciliations do not detect irregularities and errors on a timely basis.

(4) The UNHCR Representation in the Russian Federation should put in place procedures to ensure that implementing partners prepare monthly bank reconciliations.

The UNHCR Representation accepted recommendation 4 and stated that the procedures have been set in place to ensure that the oversight on this matter was reinforced through strengthened monitoring and supervision within the regulatory framework of financial management and control. IP bank reconciliations were now being monitored as part of project control and financial monitoring visits. Based on the action taken by the Representation, recommendation 4 has been closed.

B. Regulatory framework

Action was taken to strengthen internal controls in Vladikavkaz sub-office

18. Petty cash disbursements of over \$0.5 million were made from January 2009 to June 2011, of which \$200,000 could not be accounted for. The audit also identified significant instances of miscoding of vouchers to incorrect expense codes in the sub-office. Following the audit, the UNHCR Inspector General's Office (IGO) initiated an investigation into some related matters in the Vladikavkaz sub-office. The IGO completed its investigation and has referred its findings to the Director of DHRM, for follow-up.

19. Further, the Representation highlighted that the Bureau for Europe and the office in Moscow had taken corrective action on the audit findings as summarized below:

- Reinforcement of internal control mechanisms to ensure compliance with rules governing the maintenance and processing of accounts (i.e., monthly accounts and petty cash reconciliations);
- Strengthening of payment approval and certification processes;
- Consistent supervision and oversight on the risk areas addressed by the audit;
- Maintenance of adequate documentation for payments; and
- Strict enforcement of policy of not sharing passwords to the enterprise resource application software.

MEDEVAC cases are being processed in accordance with guidelines

20. The Staff Administration Management Manual and Inter-office Memo IOM/69 – Field office Memo FOM/72/2007 govern the payment of Daily Subsistence Allowance to staff during medical evacuations (MEDEVAC). However, payment of expenses associated with medical evacuation exceeded amounts allowable by \$4,128 for which recovery had been initiated.

21. On two occasions, a staff member’s medical information was filed with financial and administrative records, risking breach of confidentiality. The Representation advised that while this was a rare error, the focal point was reminded of the requirement for confidentiality of medical records.

Action was taken to ensure compliance with tendering guidelines

22. The UNHCR Manual requires a timeframe of 10 to 14 days for a simple tender offer and 4-8 weeks for vendors to prepare and submit an offer for tenders with complex requirements. In addition, the UNHCR Manual requires that eight vendors be invited for tenders between \$5,000 and \$100,000. Non-compliance in a number of cases resulted in limited competition and increased risk that value for money was not obtained.

(5) The UNHCR Representation in the Russian Federation should ensure compliance with tendering guidelines of the UNHCR Manual.

The UNHCR Representation accepted recommendation 5 and stated that action to implement it had been completed and procurements undertaken by the Representation are now compliant with tendering guidelines in Chapter 8 of the UNHCR Manual. Compliance is ensured through tighter control and oversight. Based on the action taken by the Representation, recommendation 5 has been closed.

Progress has been made in reclaiming VAT paid

23. Up until 2007 UNHCR could claim back VAT. From 2008, the host government is not open to providing a refund because all payments by UNHCR are zero-rated. At the time of the audit, VAT totaling \$822,334 was outstanding for the period from 2003 to 2007 and only \$115,000 had been refunded in the entire period. Inadequate follow-up of outstanding amounts could result in these amounts becoming irrecoverable.

(6) The UNHCR Representation in the Russian Federation should take necessary actions to expedite the process of reclaiming the Value Added Tax.

The Representation accepted recommendation 6, stating that it had been implemented as necessary action had been taken to expedite the process of VAT recovery. The total amount refunded by the end of 2011 (all for Moscow) was \$221,875.31, which indicated that follow-up action was being taken and action was ongoing. Recommendation 6 remains open pending recovery of the remaining VAT amount paid (\$600,459).

File and record management have been improved

24. IOM/017-FOM/017/2009 “Procedures for Filing Field Offices Financial Record Files and Documents” require that each file be clearly marked with a file reference code (e.g. FIN 4.02 for Monthly Accounts and FIN 4.03 for supporting documents) and notes that for audit purposes and as an essential management tool, Heads of Offices should ensure that financial records are regularly updated and

maintained in a proper manner in accordance with UNHCR financial records maintenance procedures. A serious consequence of non-compliance with instructions was that key financial documents, particularly those pertaining to Sub-Office Vladikavkaz, could not be readily located and could not be provided to the auditors. Any delay in providing audit with documents supporting financial transactions calls into question the authenticity of those documents. Reliable and complete filing of supporting documents is a fundamental requirement of internal control. During the audit, a recommendation was raised to address this issue and UNHCR took prompt action to ensure that filing of records is in compliance with IOM/017-FOM/017/2009.

C. Staff safety and security

Adequate staff safety and security measures

25. Overall, arrangements satisfied the requirements of the UNHCR Security Policy in line with the common UN security system. Programmes exist to ensure staff awareness of UNHCR safety and security policies and procedures, including evolving security procedures because some UN bodies and key donors were withdrawing from the region. The closure of key communication facilities was being mitigated by an alternative communication system (e.g. satellite phones) to be put in place, and one field safety assistant and a driver would be maintained. The rest of the security apparatus would be operating from Moscow. UNHCR had also budgeted for safety and security contingencies.

IV. ACKNOWLEDGEMENT

26. OIOS wishes to express its appreciation to the Management and staff of the UNHCR Representation in the Russian Federation for the assistance and cooperation extended to the auditors during this assignment.



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STATUS OF AUDIT RECOMMENDATIONS
Audit of UNHCR operations in the Russian Federation

| Recom. no. | Recommendation | Critical/ ¹ Important ² | C/ ³ O ³ | Actions needed to close recommendation | Implementation date ⁴ |
|------------|--|---|--------------------------------|---|----------------------------------|
| 1 | The UNHCR Representation in the Russian Federation should set in place procedures to ensure that audit certification reports adhere to UNHCR guidelines, and management letters provide an assessment of implementing partners' internal controls, financial management of funds allocated and compliance with the terms and conditions of the agreement with UNHCR. | Important | O | Submission to OIOS of IP external audit reports prepared in compliance with UNHCR IP audit certification guidelines | 31 December 2012 |
| 2 | The UNHCR Representation in the Russian Federation should put in place a mechanism to ensure compliance with UNHCR guidelines for the selection and retention of implementing partners (IP), including adoption of a risk-management approach, the use of an IP Selection Committee and review of IPs that have been working with the UNHCR for many years. | Important | C | Action completed | Implemented |
| 3 | The UNHCR Representation in the Russian Federation needs to put in place procedures to ensure that for an international IP the recording of expenditures is error free and consistent with proper record keeping, and during financial monitoring visits payment vouchers are cross verified. | Important | C | Action completed | Implemented |

¹ Critical recommendations address significant and/or pervasive deficiencies or weaknesses in governance, risk management or internal control processes, such that reasonable assurance cannot be provided regarding the achievement of control and/or business objectives under review.

² Important recommendations address important deficiencies or weaknesses in governance, risk management or internal control processes, such that reasonable assurance may be at risk regarding the achievement of control and/or business objectives under review.

³ C = closed, O = open

⁴ Date provided by the Representation in response to recommendations.

| Recom. no. | Recommendation | Critical¹/ Important² | C/ O³ | Actions needed to close recommendation | Implementation date⁴ |
|-------------------|--|--|-----------------------------|--|--|
| 4 | The UNHCR Representation in the Russian Federation should put in place procedures to ensure that implementing partners prepare monthly bank reconciliations. | Important | C | Action completed | Implemented |
| 5 | The UNHCR Representation in the Russian Federation should ensure compliance with tendering guidelines of the UNHCR manual. | Important | C | Action completed | Implemented |
| 6 | The UNHCR Representation in the Russian Federation should take necessary actions to expedite the process of reclaiming the Value Added Tax. | Important | O | Submission to OIOS of documentation showing the recovery of VAT of \$600,459 from the Government | 31 December 2012 |