OIG RELEASES AUDIT REPORT ON GRANTS MANAGED BY PSI

Losses of $1.6 million identified

PSI contests many of the OIG’s determinations

Editor’s note: By their very nature, audits tend to focus on what is not working well, and to devote much less space to what is working satisfactorily. This summary of the OIG audit of grants managed by PSI reflects that “bias.”

On 31 October 2011, the OIG released three audit reports on eight grants managed by Population Services International (PSI), an international NGO (INGO), in South Sudan (malaria, Round 7), Madagascar (HIV, Rounds 2, 8; malaria, Rounds 1, 4, 7) and Togo (HIV, Rounds 4, 8). The OIG issued a fourth report on PSI Headquarters and on issues that it said were common across all grants managed by PSI (i.e., not only in South Sudan, Madagascar and Togo).

An audit of INGOs was included in the OIG’s annual plan for 2010. PSI was likely selected because it is the largest civil society implementer of Global Fund grants.

The OIG identified what it called “losses” of $1.6 million. None of the losses were in the misappropriated category.

This article provides a summary of the four audit reports. For each of the three country-specific audits, we provide a summary of the OIG's findings concerning PSI and the oversight provided by the CCM, theLFAs and the Global Fund Secretariat; and we summarise the comments from PSI, the CCM and theSecretariat on the audit findings and recommendations. For the fourth report, we provide a summary ofthe OIGs findings and of comments from PSI.

In all four reports, the OIG found that PSI performed well as PR, often in difficult circumstances. The OIG rated PSI's internal controls as "strong."

PSI SOUTH SUDAN

The malaria grant included in the audit had a Phase 1 total value of $33.5 million, of which $26.1 million had been disbursed at the time of the audit. (The OIG report mistakenly says that the grant it audited was an HIV grant.) At the start of the audit report, the OIG acknowledged that PSI Sudan faced a number of challenges in South Sudan, including difficulties in finding competent staff in a post-war environment; insecurity in areas targeted by the programme; poor infrastructure; high illiteracy levels; and lack of baseline data for some indicators.

The OIG identified losses of $527,395, which the OIG said PSI South Sudan should pay back to the Global Fund. This amount consisted of $265,100 in expenditures that the OIG deemed ineligible and $262,295 in expenditures that the OIG said were not supported. (The OIG defines "ineligible" expenditures as costs not in line with the budget and workplan approved by the Global Fund. The OIG defines "unsupported" expenditures as those lacking adequate supporting documents to provide evidence that the activity took place and that the expenditure was in line with programme activities.)

A large part of the ineligible expenditures ($173,753) concerned the payment of salaries to sales staff which, the OIG said, PSI Sudan charged to the grant even though the programmes supported by the Global Fund did not have any social marketing elements, and despite the fact that no provision had been made in the budget for them. A large portion of the unsupported expenditures ($163,350) related to salaries for the Malaria Consortium (MC), a sub-recipient (SR). The OIG said that it was unable to establish the basis used by the MC to allocate salaries to the Global Fund.

The OIG said that the structure and staffing levels proposed by PSI were assessed by the LFA as adequate, but that a number of key positions remained unfilled one year into the grant. The OIG was of the opinion that PSI did not provide evidence that it was doing enough to fill the vacant positions. The OIG said that there were several instances of non-compliance with the grant agreement, such as a failure to test health products as required under the Global Fund's quality assurance policy.

The OIG noted several weaknesses in PSI's financial management systems, such as ineffective monthly budget monitoring, a practice of over-riding authorisation limits, and failure to account for advances on a timely basis. The OIG noted several weaknesses in SR management, such as significant delays in contracting SRs, deficiencies in the SR selection process, and inadequate SR monitoring. The OIG said that country-level procurement was weak, and cited as examples: instances of non-compliance with the approved PSM Plan, inadequate and inconsistent information given to bidders, and incidences of single sourcing without proper justification.

Oversight

CCM. The OIG said that PRs were members of the CCM and had full voting rights, thus creating a conflict of interest situation. The OIG also noted instances where CCM members were involved in operational aspects of the PR, such as the selection of SRs.

LFA. The OIG said that the LFA, KPMG, had appropriately qualified financial management experts, but was not as strong with regard to public health and procurement and supply management. According to the OIG, this resulted in some deficiencies in the quality of work of the LFA, such as failing to detect shortcomings on the part of the PR with respect to indicators and quality assurance measures.

Recommendations, reaction and follow-up

The audit report advanced 36 recommendations to address the weaknesses noted in the audits. The OIG said that after the audit field work and on the basis of preliminary findings, the Global Fund Secretariat developed action plans to address key weaknesses. The OIG added that since the oral de-brief on the audit in South Sudan in May 2010, the CCM, PSI and the LFA started implementing measures to address the findings and risks identified during the audit.

The audit report contained comments from the CCM, the Global Fund Secretariat and PSI. The CCM acknowledged the challenges and capacity gaps identified in the audit, but pointed out that South Sudan is a post-conflict country which just gained independence in July 2011, and that the programmes supported by the Global Fund are functioning in “an incredibly difficult operating environment.” In its comments, the Secretariat reported that since the time of the audit, PSI Sudan has filled all key positions necessary for the successful implementation of the grants.

With respect to the $173,753 in staff salaries which the OIG said were not budgeted for, PSI said that these costs were not for salaries, that they were for stipends and incentives for volunteers, and that they were included in the approved budget as such. PSI added that the initial accounting entries were mis-coded, but that this has been corrected. PSI said that it has the documentation to support this. (PSI subsequently told GFO that the documentation – including journal entries from its accounting system and verified volunteer pay sheets – has been provided to the OIG, and that PSI is working with the Secretariat to bring resolution to this issue.)

Concerning the $163,350 spent by an SR, the MC, which the OIG said lacked supporting documentation, PSI told GFO that MC asserts that it charged staff salaries based on actual time spent on the Global Fund project activities; and that PSI has submitted documentation to support this. PSI said that is working with the Secretariat to review and finalise the MC-related salary costs and that, “if necessary, PSI will ensure that SR costs are reimbursed and reported to the Global Fund.”

PSI took issue with the OIG’s assertion that PSI had failed to test health products. PSI told GFO that PSI has strict testing mechanisms in place to ensure that all of its health products are safe, reliable, and effective; and that PSI tests all health products in conformity with Global Fund requirements.

PSI MADAGASCAR

The five grants included in the audit had a total value of $118 million, of which $39 million had been disbursed at the time of the audit. The audit covered the period 2003 to March 2010. The OIG said that significant control weaknesses and unmitigated risks were “prevalent” in PSI’s management of Global Fund-supported grants in Madagascar. The OIG identified ineligible expenditures of $215,056 which it said should be paid back to the Global Fund.

(Note: There is some confusion in the audit report concerning the amount of the losses. Paragraph 11(a) said $215,056. Paragraph 13 included a list of the ineligible expenses totalling $282,923. GFO has used the lower figure, which is consistent with the amount shown in a Q&A prepared by the Global Fund Secretariat.)

More than half of the expenditures deemed ineligible ($141,750) concerned the finding by the OIG that 25,350 more long-lasting insecticide-treated nets were charged to the Global Fund than were actually delivered. This included 25,000 nets that PSI said were charged to USAID, not the Global Fund grant; the OIG maintained that these nets were also charged to the Fund. One of the costs that the OIG deemed ineligible was a $15,000 charge for oversight activities undertaken by the CCM. The costs involved travel and per diems. The OIG noted that the Global Fund prohibits use of programme funds to pay CCM costs. Other costs deemed ineligible included products distributed for sale (as part of the programme's social marketing component) for which no payment was received by the Global Fund; and VAT paid even though an exemption had been granted.

The OIG said that there was no price control mechanism in place to ensure that PSI's distributors sold products at the intended price. The OIG noted that there had been reports over the years of excessive prices charged to the end beneficiaries of Global Fund products – for example, up to five times the recommended price on the package.

The OIG said that none of the audit reports submitted by PSI met the Global Fund's audit requirements. The OIG said that there were instances where value for money was not obtained, and cited as an example the purchase of four vehicles under the Round 4 malaria grant about two months before grant closure.

The OIG said that programme funds were used to pay staff commissions and bonuses, and fringe benefits such as house rental, gardening, housekeeping, private vehicle costs, private gas, small household appliances and school fees. The OIG said that these charges amounted almost $1 million between 2003 and 2009. The OIG said that that these details were not disclosed to the Global Fund during grant negotiations. The OIG said,

"While these benefits may be part of PSI's remuneration package, the extent of the benefits seems excessive most especially when set against the purpose for which funds were provided i.e. to fight the diseases. The Global Fund cannot dictate what PSI staff should be paid. However, program funds should only be used to pay for what is reasonable so that program funds are used maximally to fighting the diseases."

However, the OIG did not include any staff-related costs in its calculation of losses that PSI should repay.

Recommendations, reaction and follow-up

The audit report advances 22 recommendations to address the weaknesses noted in the audit. The OIG noted the Global Fund Secretariat had already identified and started implementing measures to address the findings and risks identified during the audit.

The audit report contained comments from PSI, the Global Fund Secretariat and the CCM. PSI contested the OIG's findings of loss, particularly concerning two items:

- With respect to $141,750 for bed nets, PSI said that it did not charge the Global Fund for nets paid for by USAID. PSI said that it has submitted documentation to the OIG which shows that the 25,000 nets were identified as USAID nets, and that payment for those nets was allocated to USAID.

- With respect to the CCM oversight costs, PSI said that it complies with the current Global Fund policy on the prohibition of using programme funds to cover CCM costs, "but respectfully notes that an exception to the policy was specifically made to PSI by the Global Fund program officer."

(In its comments, the Secretariat said that it will ask the LFA to carry out a review of these two items.)

PSI said that it does not accept responsibility for the other losses identified by the OIG and that it is working closely with the Secretariat to resolve these issues. PSI told GFO that it takes issue with the OIG's assertion that the PSI audit reports did not meet Global Fund requirements. PSI said that it did meet the requirements that were in place at that time, but that the Global Fund revised its audit requirements in 2010. PSI said that it is not proper to evaluate PSI's work prior to 2010 based on rules that were not in place then.

With respect to the OIG's comments on staff commissions and bonuses, PSI told GFO that it maintains strict adherence to Global Fund compensation rules and regulations for both local and international staff. PSI said that compensation levels, including salaries, bonuses, commissions, and allowances adhere to local country employment laws, international best practice, and the Fund's guidelines for budgeting human resources. PSI said that all compensation decisions made by PSI were in line with these rules and were approved by the Global Fund during the budgeting process. PSI said that, contrary to what the OIG asserted, PSI does not include the costs of gardening and housekeeping in its benefits.

PSI said that it has benchmarked its benefit package several times to other international organisations, and that PSI is an "average" payer of these benefits. With respect to allowances for international staff, PSI said, it bases its international allowances as closely as possible on allowances paid by the U.S. State Department. PSI said that a standard international package includes post allowance, post differential, danger pay for eligible posts, education allowance and housing allowance; and that these allowances are fairly standardised and are accepted by major donors.

The CCM had no particular comment on the results of that audit, but expressed its commitment to monitor the implementation of all recommendations, in close collaboration with the LFA.

PSI TOGO

The two HIV grants included in the audit had a total value of $41 million, of which $31 million had been disbursed at the time of the audit. The period covered by the audit was 2005 to March 2010. The OIG identified losses of $864,869, which the OIG said PSI Togo should pay back to the Global Fund. This amount is made up of $377,047 in ineligible expenditures and $487,822 in expenditures that the OIG deemed "inappropriate." The ineligible expenses included $248,539 for disbursements of funds from the Round 4 HIV grant to the National AIDS Control Programme, the National AIDS Control Committee and the Ministry of Health. The OIG said that these payments were effected without sub grant agreements, budgets or work plans, and that the funds had not been accounted for.

Most of the expenditures that the OIG said were inappropriate related to $431,939 from the sale of condoms donated by USAID, distributed using the Global Fund money and, according to the OIG, not reported to the Global Fund. The OIG said that the grant agreement requires that income incidental to grant programmes should be reported to the Fund and should be used for programme activities. In the audit report, the OIG quoted PSI as saying that the funds were reported and refunded to USAID; however, the OIG said, PSI could not provide documentary evidence to support this claim.

Recommendations, reaction and follow-up

The audit report advanced 18 recommendations to address the weaknesses noted in the audits. The OIG said the Global Fund Secretariat, PSI and the CCM had already identified and started implementing measures to address the findings and risks identified during the audit.

The audit report contained comments from PSI, the Global Fund Secretariat and the CCM. In its comments, PSI acknowledged that PSI Togo disbursed $248,539 to three state entities, and that it did not have contracts with these entities, or budgets or work plans. PSI explained that the funding provided was intended to strengthen the institutional capacity of these three entities. PSI said that while this item had not been included in the Round 4 proposal, it was incorporated into the budget during grant negotiations following the suggestion of the team leader from the Global Fund Secretariat. PSI said supporting documents were provided and that the LFA validated the expenditure. (In its comments on this issue, the Secretariat said it will work with the OIG to provide PSI with clarifications on the nature of the documents that PSI needs to provide to prove that the expenditures of $248,539 were for used for programme purposes.)

Concerning income from the sale of condoms donated by USAID ($431,939), PSI said that USAID had not imposed any restrictions on the use of this income. PSI said that the money was used for programmes, including research, distribution, promotion, travel, storage and additional packaging for condoms. PSI said that these expenditures were described in its quarterly report, and that right up until the distribution of the last condom in October 2007, neither the LFA nor the Global Fund made any mention of the need to validate this expenditure. Furthermore, PSI said, the data relating to the sales of these condoms was checked by the LFA during a data verification exercise in 2006. PSI said that it disagreed with the OIG’s conclusion that PSI should return the $431,939 to the Global Fund Secretariat. (In its comments on the condoms issue, the Secretariat said that it is seeking more information from the OIG, that it will review the issue, and that it will adopt a position on the basis of this review.)

In its comments, the CCM raised no concerns about the audit findings.

PSI HQ / COMMON ISSUES

PSI and its affiliates are PRs in 12 countries and an SR or sub-SR (SSR) in 20 others. In its fourth PSI-related audit report, the OIG said that despite the fact that PSI operates in challenging environments in many of these counties, PSI had achieved commendable results. The OIG said that, overall, PSI had instituted good policies in the management of programme funds, but that there is scope to further improve their implementation at field office and headquarters (HQ) levels.

The OIG said that the Global Fund requires that when international NGOs are nominated as PR, the arrangement is intended to be temporary, and the PR is expected to build the capacity of national entities to take over as PR. The OIG said that this did not happen in the grants managed by PSI that the OIG audited. The OIG said that it appreciated that

“there are potential risks associated with transitioning to systems with inadequate capacity or quality since shortcomings in such systems can jeopardise grant implementation. However, unless a process to build the requisite capacity and transition grants to national programs is instituted, this may never happen and it runs counter to the principle of ‘national ownership.’ ”

In a similar vein, the OIG said that PSI, like many other PRs, had set up structures parallel to the national ones because the latter were viewed as being cumbersome or inadequate to support programme implementation. The OIG said that this is contrary to the Global Fund principles that advocate for the use of national systems to the maximum extent possible.

The OIG said that LFAs did not have the necessary access to the expenditures managed by PSI HQ, and that in most countries where PSI is a PR, this represents a significant proportion of overall grant expenditure.

The OIG said that PSI maintained all grant funds in a pooled account, and that PSI's accounting system was unable isolate bank balances by country, donor and grant. As a result, the OIG said, the LFA was unable to validate the bank balances reported in the PU/DRs and could not provide assurances concerning the accuracy of programme transactions and bank balances. The OIG said that PSI should either open a separate bank account for Global Fund grants or improve its accounting system.

With respect to common costs and overhead charges, the OIG noted that PSI's financial guidelines were unevenly applied in different countries; that direct costs related to the HQ were charged in addition to overhead costs; that rates were not adjusted to take into account differences in responsibilities when PSI was PR and when it was SR; and that there were no independent processes to validate the overheads charged.

The OIG said there were significant weaknesses in the capacity of PSI staff to effectively procure programme products. The OIG said that all procurement and supply management assessments undertaken by the LFA were at the country level and that, at the time of the audit, no assessment had been undertaken of the HQ's capacity to handle procurements. The OIG said that this was contrary to the grant agreement, which stipulates that the PR's capability to procure health products be assessed due to the complexity and significant risks associated with the procurement of such products.

With respect to SR management, the OIG said that there were significant delays in contracting of SRs, shortcomings in the SR selection process, and inadequate SR monitoring.

Recommendations and reaction

The audit report advances 25 recommendations to address the weaknesses noted in the audits. In a letter dated 14 October 2011, which is reproduced in the audit report, PSI said that it "largely accepts the observations and recommendations" of the OIG, "with a few notable exceptions." Some of the exceptions concerned observations in the report that are directly related to findings in the PSI South Sudan, PSI Madagascar and PSI Togo audit reports which PSI had already questioned (see above).

There is a section of the report where all of the recommendations are listed and where PSI provides comments. While PSI accepted most of the recommendations, it is clear from its comments that PSI disagreed with some of the findings on which the recommendations were based.

In response to a recommendation from the OIG that PSI develop plans for capacity building and transition, PSI said that it fully supports the Global Fund's operating principle of country ownership, and that, as PR, PSI has consistently demonstrated its support for programmes that reflect country ownership and that value country-directed programme development and implementation processes. PSI said it looks forward to working with the Secretariat and CCMs to more fully evaluate the countries where this would be most feasible. PSI said that while it is fully committed to capacity building, it has found that costs for capacity building are often cut by the Global Fund, particularly in the current era of financial constraints. PSI said that it will continue to work with the Secretariat to identify the financial and human resources needed to do the capacity building.

With respect to access by LFAs to documents at HQ, PSI said that it has repeatedly invited the LFAs (or their U.S.-based representatives) to visit its HQ office to access documents. PSI's HQ has a policy that it will not send original documents outside of the organisation (since original documents are required to support other audits). PSI said that it has offered to send certified copies of HQ documents to the LFAs. However, PSI said, some LFAs maintain that original documents are necessary, so clarification on this issue from the Secretariat would be welcome. PSI said that it welcomes the Secretariat's decision to conduct an LFA assessment of PSI's headquarters, and is working with the Secretariat to ensure this happens quickly.

Regarding the OIG's finding that PSI's accounting system was unable to isolate bank balances by country, donor and grant, PSI told GFO that it can and does reconcile all its donor funds though an activity management system that tracks receipts from donors, fees and revenues earned, and expenditures on an activity-by-activity basis. Since the system was implemented in 2008, PSI said, additional controls and reports have been introduced to ensure that at any point in time the system can produce reports that identify the exact amount of outstanding funds from the Global Fund held by PSI on a grant-by-grant basis. In addition, PSI said that its system of controls and the reports are extensively audited by global auditors each year, and that the auditors provide assurance that all cash is properly accounted for and that all donor account balances are accurate.

Concerning shared costs and overhead charges, PSI said that it adheres to Global Fund budgeting guidelines. PSI said that it has shared with the OIG its plan for global implementation of a new common cost policy, which it expects to implement in early 2012. Regarding overheads, PSI said that its Global Fund budgets have included fees that were specifically approved by the Fund, and that there was some variance in fees among different country programmes. However, PSI said, the Global Fund has released new guidelines on indirect cost recovery rates which standardise the fee rates for PRs and SRs. PSI said that it is applying the new guidelines on all grants signed after 18 April 2011.

In response to a recommendation from the OIG that PSI should strengthen the capacity of its procurement unit by ensuring that staff have appropriate skills and tools to manage the procurement process, PSI said,

"PSI stands behind the competency of its procurement staff and of its internal capacity development processes that allow staff to constantly improve their skills… PSI's procurement staff brings unique backgrounds and skill sets to PSI: for example, close to three quarters have lived or worked abroad in the countries where PSI works. This international experience equips them to understand the operating context of PSI's programs… Staff members at minimum hold a bachelor degree, and at least five staff members have a master degree in business, public health or international development. Over half have held positions in which purchasing, logistics or government contracting was part of the job."

COMMENTS BY THE HEAD OF PSI ON ALL FOUR AUDITS

When we were preparing this article, Karl Hofmann, President and CEO of PSI told GFO that "as one of the largest civil society implementers of Global Fund grants, PSI welcomed the opportunity to work with the OIG to demonstrate how PSI's internal control mechanisms at both the Headquarters and country-level operate to ensure PSI's compliance with Global Fund guidelines." Hofmann welcomed the OIGs positive comments concerning PSI's grant oversight measures and concerning PSI's role in achieving significant programmatic results, often in challenging circumstances. He added,

"For areas in which both the OIG and PSI identified opportunities for improvement, PSI has already taken concrete action to address the issues and will continue to do so. With respect to the questioned costs in the reports, PSI has provided the OIG detailed explanations and supporting documentation for all questioned costs. We are already working closely with the Secretariat to bring final resolution to these issues."

The audit reports on PSI, and all of the other OIG reports released on 31 October 2011, are available on the Global Fund website here.

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