

**INTERNAL AUDIT REPORT  
EARMARKING OF DONOR FUNDS  
MARCH 2016**



## Conclusion

Our audit procedures were designed to provide assurance to management and the Gavi Board that the processes related to the earmarking of donors funds are well designed and operating effectively.

Through our audit procedures, we have confirmed that the risks associated with the earmarking processes are well understood and are being effectively managed. In particular, donor funds are dealt with transparently with the allocation of programme payments being clearly documented and donor transactions being proactively managed. We have identified certain areas where there is opportunity to improve the design and operating effectiveness of the internal controls.

We note that management have identified two operational risks relating to key person dependency and reliance on manual processes. These risks were being addressed by management at the time of the audit with mitigating controls being implemented where necessary. As a result, these issues have not been raised as audit issues but have been included in the report as we believe they are relevant risks in the earmarking processes.

## Internal Audit Issue Summary

Issue Description	Rating	Ref	Page
Compliance with Earmarking Principles for Private Sector Donors	L	2015-07.01	3
Compliance with Earmarking Principles for Sovereign Donors	L	2015-07.02	5
Monitoring of Indicators for Earmarked Funds	L	2015-07.03	6
Guidelines for Non-Vaccine Donations In-Kind and Activities Outside of Board-Approved Programmes	L	2015-07.04	7

## Summary Performance Ratings on Areas Reviewed

For ease of follow up and to enable management to focus effectively in addressing the issues in our report, we have classified the issues arising from our review in order of significance: High, Medium and Low.

In ranking the issues between 'High', 'Medium' and 'Low', we have considered the relative importance of each matter, taken in the context of both quantitative and qualitative factors, such as the relative magnitude and the nature and effect on the subject matter. This is in accordance with the Committee of Sponsoring Organisations of the Treadway Committee (COSO) guidance and the Institute of Internal Auditors standards.

Rating	Implication
High	Address a fundamental control weakness or significant operational issue that should be resolved as a priority
Medium	Address a control weakness or operational issue that should be resolved within a reasonable period of time
Low	Address a potential improvement opportunity in operational efficiency/effectiveness

## Contents

Summary of Findings	1
Appendix 1: Detailed Findings and Recommendations	3
Appendix 2: Management Identified Issues and Initiatives	8

## Distribution

### Title

Managing Director, Finance and Operations

Senior Director, Finance & Chief Accounting Officer

Managing Director, Resource Mobilisation & Private Sector Partnerships (RMPSP)

Director, European Strategy

## For Information

### Title

Chief Executive Officer

Deputy Chief Executive Officer

Managing Director, Audit & Investigations

Executive Team

Director, Legal

Director, Policy and Performance

Head, Financial Operations

Senior Finance Manager, Contribution & Partner Programme Grants

Senior Manager, Global Expert Services

Manager, Global Expert Services

Analyst, Global Expert Services

Head, Risk

# Summary of Findings

## Audit Objective

Our audit assessed the design and operating effectiveness of the key internal controls related to earmarking of donor funds covering the agreement, recording and management of donor earmarks as well as the allocation of programme payments.

## Audit Scope and Approach

We adopted a risk-based audit approach informed by our assessment of the system of accounting and internal controls and tested where necessary a sample of transactions to validate the proper operation of these controls.

This audit was designed to assess the:

- Design and operating effectiveness of the key controls;
- Economy and efficiency of the utilisation of resources;
- Quality of implemented governance and risk management practices;
- Compliance with relevant policies, procedures, laws, regulations and donor agreements.

The scope of this audit covered the earmarking of donor funds in the period 1 January 2014 to 30 September 2015. In particular, the audit covered the following key earmarking processes:

- Negotiation and agreement with donors;
- Identification and recording of donor earmarks;
- Receipt of donor funds;
- Programme payments and donor attribution;
- Donor reporting.

Please note that the following areas were excluded from the audit scope:

- Process for securing donor pledges and contributions;
- Management of donor relationships;
- Investment of donor funds in the short-term and long-term investment portfolios;
- Preparation, review and agreement of donor contracts;
- Financial reporting of restricted and unrestricted funds.

## Background

Gavi is funded by governments, corporations, foundations and private entities. From 2000 to 2015, 77% of Gavi's funding came from governments, 22% from foundations, corporations and organisations, and the remaining 1% came from the private sector.

Since 2011, Gavi has been broadening its donor base and drawing additional contributions from new sovereign donors, private sector entities (through the Matching Fund initiative) and private individuals. As a result there has been a shift in the nature of grants being awarded, with a growing tendency for donations to be directed towards specific vaccine programmes, geographic regions, countries or projects, and with relatively limited (1-3 year) timeframes in which to spend the funds.

Generally, private sector funds are earmarked to some extent and these earmarks are usually acceptable as long as the earmark is for Board-approved programmes. In addition, earmarks are inherent in some of Gavi's funding mechanisms, such as the Advance Market Commitment (AMC) and International Finance Facility for Immunisation (IFFIm).

For funding from sovereign donors, the Board has stated that it seeks and greatly prefers non-earmarked multilateral funding to allow for maximum flexibility, predictability and country-demand driven programming. However, in exceptional cases, earmarks may be accepted based on agreed principles.

When agreeing earmarks with donors, the benefits of using earmarking to access new or additional funds has to be assessed against the risk of limiting Gavi's ability to fully and equitably implement its strategy.

Once earmarks have been agreed, the effective management of donor funds in accordance with the donor agreements is vital to ensuring Gavi maintains its reputation as an effective vehicle through which development funds can be delivered securely.

The Finance team is responsible for ensuring compliance with donor earmarks. All donor funds are commingled and therefore earmarks

# Summary of Findings

are managed through the accounting system and manual financial records. Finance manually attribute programme and grant payments to donors based on analyses of the earmarks and assessment of relevant priorities.

An analysis of the month-end donor balances has been completed and over the previous twelve months the percentage of donor funds subject to earmarks varied between 0.3% and 12% (excluding AMC), and between 4% and 31% (including AMC). On average, 4% (excluding AMC) and 14% (including AMC) of the donor funds were subject to earmarks<sup>1</sup>.

In addition, an analysis of the cash proceeds received by Gavi from 2000 – 2015 has been completed and the approximate proportion of these proceeds subject to earmarks is 9% (excluding AMC).

## Conclusion

Our audit procedures were designed to provide assurance to management and the Gavi Board that the processes related to the earmarking of donors funds are well designed and operating effectively.

Through our audit procedures, we have confirmed that the risks associated with the earmarking processes are well understood and are being effectively managed. In particular, donor funds are dealt with transparently with the allocation of programme payments being clearly documented and donor transactions being proactively managed. We have identified certain areas where there is opportunity to improve the design and operating effectiveness of the internal controls.

## Summary of Issues Arising

Our audit identified four low-rated audit issues relating to compliance with earmarking principles for private and sovereign donors, monitoring of indicators for earmarked funding and the approval process for donations earmarked for activities outside of Board-

approved programmes. A detailed analysis of these issues has been provided in Appendix 1.

## Management Identified Issues and Initiatives

Two internal control issues had already been identified and were being addressed by management at the time of our audit. As a result, these issues have not been raised as audit issues in this report, but have been noted in Appendix 2 of the report for completeness.

We will continue to work with management to ensure that these audit issues are adequately addressed and required actions undertaken.

We take this opportunity to thank the Finance and Resource Mobilisation and Private Sector Partnerships teams for their assistance during this audit.

Chrysantus Nyongesa  
Head of Internal Audit

<sup>1</sup> This analysis was based on the month-end net donor balances as per the Donor Dimensions in AX for the 12 months from 30 November 2014 to 31 October 2015.

# Appendix 1: Detailed Findings and Recommendations

Issue No.	Issue Rating	Issue Description	Risk/Implication	Recommended Actions	Management Comments	ET Member/ Action Owner	Target Completion Date	Status
2015-07.01	Low	<p><b>Compliance with Earmarking Principles for Private Sector Donors</b></p> <p>1. The key principles relating to earmarking of private sector donor funds are currently documented in the Matching Fund Memorandum of Understanding (MOU) between Gavi, DfID and the Gates Foundation. The MOU states that non-earmarked funding is strongly preferred but that earmarks will be considered if required to engage a new private sector partnership, as long as the earmarks do not create significant additional workload or costs for the Secretariat or the eligible countries, and do not direct or influence Gavi's funding decisions.</p> <p>We note that this MOU continues to be in effect until 31 December 2017, but that only specific funds can be matched under the MOU after November 2016.</p> <p>2. All proposed earmarks are discussed and agreed with the Finance team prior to finalisation with the donor. This ensures that the earmarks can be fully complied with, do not overlap with other donors, and are appropriate. Further, in accordance with the Guidelines on Signature Authorities for Legal Agreements (approved by the CEO in 2010), Finance clearance is required prior to a donor agreement being signed.</p> <p>During our audit we confirmed that Finance is engaged prior to donor agreements being signed. However, we were unable to obtain evidence of formal Finance validation of the earmarks for all the private donors selected.</p>	<p>Earmarks may be agreed to that are not aligned to Gavi's strategy, influence Gavi's funding decisions, require significant additional resources, or involve additional costs for the Secretariat or the eligible countries.</p> <p>Earmarks may be agreed to that cannot be fully complied with (for example, if there are not enough approved programmes available).</p>	<p>It is recommended that Management:</p> <ol style="list-style-type: none"> <li>1. Considers including the earmarking principles for private sector donors in the Private Sector Strategy for 2016-2020 and ensure the principles cover matched and un-matched donations</li> <li>2. Considers making the internal validation process more explicit in the New Business Forms, particularly in relation to Finance validation and the availability of programmes to meet the required earmarks</li> <li>3. Considers updating the New Business Pipeline and Process to ensure that compliance with the earmarking principles for private sector donors is clearly evidenced (e.g. consideration of transaction costs, exit strategy, etc.)</li> </ol>	<p>1. Management agrees with the recommendation. The RMPSP department is currently finalizing their private sector approach for 2016-2020, the principles will be included in the annex of the document.</p> <p>2. Management agrees with the suggestion and will further explain the validation process within the NBC forms. However, it is important to clarify that all donor agreements and proposals are approved by RMPSP management after considering Finance's recommendations on absorptive capacity of earmarks.</p> <p>3. Management acknowledges the recommended changes and will take the necessary steps to ensure that the principles are integrated within the documented process.</p>	<p><b>MD, RMPSP</b> <b>MD, Finance &amp; Operations</b></p> <p>Senior Manager, Global Expert Services, RMPSP Senior Director, Finance &amp; Chief Accounting Officer</p>	31 July 2016	Open

# Appendix 1: Detailed Findings and Recommendations

Issue No.	Issue Rating	Issue Description	Risk/Implication	Recommended Actions	Management Comments	ET Member/ Action Owner	Target Completion Date	Status
		<p>We note that the RMPSP team implemented a New Business Pipeline and Process in Q2 2015. This process should ensure that there is formal consultation and validation with the relevant Secretariat teams for all new private sector donor arrangements. However, formal Finance validation is not mandatory in this process.</p> <p>3. Through our audit procedures, we selected a sample of earmarked private donor arrangements and assessed whether they complied with the earmarking principles in the MOU. We confirmed that the earmarks did not direct or influence Gavi's funding decisions. However, we were unable to evidence formal assessment of the impact of the arrangements on the Secretariat's resources. In particular, two of the earmarked private donor arrangements sampled appear to create additional workload for the Secretariat, although it is unclear if this meets the definition of 'significant'.</p> <p>We note that the newly implemented New Business Pipeline and Process includes a formal assessment of the proposed donor arrangements including the impact on the Secretariat's resources. However, the assessment does not currently include the impact on the recipient countries.</p>						

# Appendix 1: Detailed Findings and Recommendations

Issue No.	Issue Rating	Issue Description	Risk/Implication	Recommended Actions	Management Comments	ET Member/ Action Owner	Target Completion Date	Status
2015-07.02	Low	<p><b>Compliance with Earmarking Principles for Sovereign Donors</b></p> <p>1. The key principles for accepting earmarks on sovereign donor funds are documented in the Long-Term Funding Strategy (LTFS) approved by the Board in 2012. Earmarked sovereign donor proposals are considered on a case-by-case basis taking into account the following principles:</p> <ul style="list-style-type: none"> <li>• Alignment with Gavi-approved programmes;</li> <li>• Additionality of support to unrestricted funding from Gavi donors;</li> <li>• Negligible transaction costs for countries;</li> <li>• Manageable transaction costs for the Secretariat and partners.</li> </ul> <p>Through our audit procedures we were unable to evidence how the transaction costs for the earmarked sovereign donor arrangements selected were formally assessed prior to agreements being approved.</p> <p>2. As with earmarked funding from private sector donors, all proposed earmarks are discussed and agreed with the Finance team prior to finalisation with the donor. However, we note that there is currently no formal process in place to ensure that Finance validation is obtained. For some of the sovereign donors selected, we were unable to obtain evidence of Finance validation for the arrangement, although we confirmed that Finance were aware of and monitoring all the relevant earmarks.</p>	<p>Transaction costs (associated with bilateral funding) for eligible countries, partners and the Secretariat may be significantly higher than expected or what is considered reasonable.</p> <p>Finance may not be engaged on a timely basis meaning that donor earmarks may be agreed to that cannot be fully complied with.</p>	<p>It is recommended that Management:</p> <ol style="list-style-type: none"> <li>1. Maintains documentation to evidence compliance with the sovereign donor earmarking principles contained in the LTFS</li> <li>2. Considers implementing a formal process to ensure that Finance validation is obtained during the negotiation of earmarks with sovereign donors</li> </ol>	<p>1. Management agrees to continue strengthening their RMPSP standard operating procedures in regards to earmarking. At present, the RMPSP department ensures that all email-interaction and supporting documents are logged and documented.</p> <p>2. Management will work with the Finance team to ensure the appropriate earmark validation is given. Management will continue to ensure this is formalized within the earmarking principles and guidelines.</p>	<p><b>MD, RMPSP</b> <b>MD, Finance &amp; Operations</b></p> <p>Director, European Strategy, RMPSP</p> <p>Director, US Strategy, RMPSP</p> <p>Senior Director, Finance &amp; Chief Accounting Officer</p>	31 July 2016	Open



# Appendix 1: Detailed Findings and Recommendations

Issue No.	Issue Rating	Issue Description	Risk/Implication	Recommended Actions	Management Comments	ET Member/ Action Owner	Target Completion Date	Status
2015-07.03	Low	<p><b>Monitoring of Indicators for Earmarked Funds</b></p> <p>The LTFS approved by the Board in 2012 includes certain operational and risk management criteria to be considered in the management of earmarked donor funds. One of these criteria is the monitoring of earmarked funds as a percentage of Gavi's total funding. It was suggested that this indicator should be calculated on an annual basis and reported to the Executive Committee when certain thresholds are met. It is unclear exactly how this indicator should be calculated (for instance, based on month-end donor balances, cumulative cash proceeds or contributions over a specified period of time, etc.). We calculated this indicator based on various methods and found that the proportion of earmarked funds approximately ranged from 4% to 9% (excluding AMC) depending on the calculation method used. This indicator could be used to provide some insight into the trend of the proportion of funds being earmarked, as well as the impact on resources to manage these earmarks and on the strategy.</p>	<p>The proportion of earmarked funding and impact on Gavi's resources and strategy may not be proactively managed.</p>	<p>It is recommended that Management:</p> <p>Clarifies how the proportion of earmarked funds should be calculated, and then monitors this indicator on at least an annual basis.</p>	<p>Management agrees with the recommendation of clarifying the methodology of monitoring the proportion of earmarked funding.</p>	<p><b>MD, RMPSP MD, Finance &amp; Operations</b></p> <p>Manager, Global Expert Services, RMPSP Senior Director, Finance &amp; Chief Accounting Officer</p>	31 May 2016	Open

# Appendix 1: Detailed Findings and Recommendations

Issue No.	Issue Rating	Issue Description	Risk/Implication	Recommended Actions	Management Comments	ET Member/ Action Owner	Target Completion Date	Status
2015-07.04	Low	<p><b>Guidelines for Non-Vaccine Donations In-Kind and Activities Outside of Board-Approved Programmes</b></p> <p>Donations-in-kind relating to vaccines must comply with the Vaccine Donation Policy approved by the Board in 2009.</p> <p>However, there is currently no policy guideline for other types of donations-in-kind received (for example, technical assistance provided or staff seconded to the Secretariat by a donor), or donations proposed for activities not relating to Board-approved programmes (for example, funds provided for a specific project).</p> <p>We note that the New Business Pipeline and Process implemented in Q2 2015 should ensure that there is a formal review process for all new private sector donor arrangements, including donations-in-kind.</p>	<p>Earmarked donations could be accepted for projects/activities outside of Board-approved programmes that are not aligned to Gavi's strategy, create a conflict of interest or create additional operational or reputational risks for Gavi</p>	<p>It is recommended that Management:</p> <p>Considers including principles relating to other types of donations-in-kind received (e.g. technical assistance or donations for activities outside of Board-approved programmes) in the Private Sector Strategy for 2016–2020, and ensures compliance with these principles is evidenced through the New Business Pipeline and Process</p>	<p>Management agrees with the recommendation. The in-kind principles and guidelines are to be developed as part of the implementation of the private sector approach priority work area of 'Integration.'</p>	<p>MD, RMPSP</p> <p>Senior Manager, Global Expert Services, RMPSP</p> <p>Director, Global Operational Partnerships, RMPSP</p>	31 Dec 2016	Open

# Appendix 2: Management Identified Issues and Initiatives



Two internal control issues had already been identified and were being addressed by management at the time of our audit. As a result, these issues have not been raised as audit issues in this report, but have been noted below for completeness.

## **Key Person Dependency**

The Senior Finance Manager, Contribution & Partner Programme Grants is responsible for managing compliance with donor earmarks on an on-going basis. Donor earmarks are managed through the use of Donor Dimensions in the Microsoft Dynamics Axapta 2012 Accounting System (AX) as well as a series of Excel spreadsheets.

Management have identified that there is currently a key person risk for the earmarking processes. In order to address this risk, an additional member of the Finance team has been designated to provide back-up for these processes as required.

In addition, detailed operational procedures have been documented as well as a set of principles to be followed in attributing and prioritising programme payments to individual donors.

We believe that these actions will adequately address the key person dependency risk.

## **Manual Processes**

The key processes and controls for earmarking of donor funds are manual and based on Excel spreadsheets.

Management have identified that reliance on manual processes and controls can increase the risk of human error. In addition, the additional checks implemented to manage this risk can be time-consuming. As a result, potential system solutions have been investigated to supplement the current processes.

It is understood that Management will continue to monitor and assess the resources required to maintain the manual processes, particularly if the level and complexity of earmarking

increases. The requirement for a system solution will be regularly assessed and included in the budget and workplan when considered necessary.

Through our audit procedures we confirmed that the key controls are operating effectively. However, we believe that as the proportion and complexity of earmarks increase, it may become more efficient to introduce a system solution, in particular in helping to proactively manage the full utilisation of donor funds prior to termination date.

The cost and implementation of a system needs to be assessed against these benefits. We support management's decision to regularly monitor this.