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|  | |  | | --- | | **Guidelines for Annual Audit of Global Fund Grants**  Terms of Reference for a Systems Audit of Global Fund (TGF) Supported Programs | |  |

November 2019 Geneva, Switzerland

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**Terms of Reference for a Systems Audit - Design and operating effectiveness of the Internal Control System**

1. **Program background, audit structure and description of entities**
   1. **Program Background: [to be completed by the Principal Recipient]**
2. The Principal Recipient should include a brief background on the grant including its main objectives and activities. Reference may be made to the program description in the Grant Confirmation.
3. The Principal Recipient should describe any key information about the grant amount and implementation cycle which is important to understand the scope of the audit. For example, the phase of the grant, the total amount committed, any changes to the structure of the grant e.g. consolidation with another grant, amount budgeted for the year of audit and amount disbursed by the Global Fund to the Principal Recipient and from the Principal Recipient to the Sub-recipients.
   1. **Program Entities and audit approach: [to be completed by the Principal Recipient]**
4. The Principal Recipient should describe the nature of the audit and how it is categorized, explaining any agreed exceptions. The Principal Recipient should tabulate all entities covered by the audit including entity name, legal status, audit scope, main activities funded and amount of expenditure in the reporting period and any other pertinent information that the auditor should be aware of.
5. **Objectives**
6. The **objective** of this audit is to:
   * Enable the Auditor to express an opinion on whether the Internal Control System implemented by the Principal Recipients (or and sub-recipients) to manage the risks that can prevent the achievement of the program’s objectives and which existed at *[date],* was suitably designed and operate effectively.
   * Provide recommendations for all findings regarding the design and operating effectiveness of the internal control system. Recommendations shall be classified by severity and include, where possible, a suggested timeline for implementation.
7. **Standards and Guidance**
8. The auditor will perform this systems audit in accordance with the following standards:

* International Framework for Assurance Engagements particularly the International Standards on Assurance Engagements 3000 (ISAE 3000) relating to Assurance Engagements Other than Audits or Reviews of Historical Information of the International Federation of Accountants (IFAC).
* The above standard is a subset of the International Standard on Quality Control (ISQC) which in turn, is a subset of the IESBA Code of Ethics for Professional Accountant. The engagement should also be performed in accordance with both these standards.

1. **Available documents and facilities**
2. With respect to each grant, the Principal Recipient will provide the auditor with access to the procedures manual pertaining to the grant as requested by the auditor. An indicative list of the documents which may be requested by the auditor includes:
3. Grant and sub-grant agreements, including the detailed budgets;
4. Financial procedures manuals, systems descriptions or any other documentation explaining the processes contributing to the production of reliable financial reports and maintaining internal control, either at Principal Recipient or sub-recipient levels;
5. Any formal documentation of the operational controls used to manage the grant agreement;
6. Interim monthly or quarterly grant activity reports, as applicable (programmatic as well as financial);
7. General ledger, cash book, other important books and records held at either Principal Recipient or sub-recipient level;
8. Bank statements;
9. Important correspondence between Global Fund and Principal Recipient, Principal Recipient and sub-recipients pertaining to grant implementation matters;
10. Minutes of management meetings;
11. Internal audit reports relevant to Global Fund expenditures or any systems, governance or other issue which impinges on Global Fund grants.
12. The Auditor’s latest Management Letter
13. The Global Fund Performance letters
14. **Scope**
15. This audit will be performed based on the requirements of the Global Fund auditing guidelines. The audit will be performed at the Principal Recipient’s offices and could include the offices of all or some of the sub-recipients or any other location used for grant purposes (e.g. warehouses) depending on the risks and/or level of funding*.*
16. The **Program subject to audit** covers the controls around the activities set out in the Grant Agreement and other related documents. An indicative list of controls is provided in Attachment 1 of these terms of reference.
17. The **subject of the audit** is the **design** **and operating effectiveness of the Internal Control System** which existed at [*date*].
18. The Principal Recipient management must collaborate with the auditor and provide them with all the necessary information. The auditor must inform the Global Fund for immediate action in situations where a limitation in the auditor’s scope of work is noticed. This will consist in assessing whether the audit should continue or not and, should it continue, whether the audit scope and the timelines of reporting should be changed.
19. **Audit Procedures**
20. The audit should be carried out in accordance with the **procedures** set out in the following sectionandwhich cover audit documentation and evidence, planning, fieldwork, and reporting. Particular attention should be paid to the following :
21. The risk-based evaluation of the design and operating effectiveness of internal controls shall include the following minimum procedures:
22. Obtain an understanding of the design of the internal control related to the Global Fund program and assess if they are used in operations.
23. Assess inherent risk and control risk and summarize the risk assessments for each assertion.
24. Evaluate the control environment, the adequacy of the systems, and control procedures with emphasis on the policies and procedures that pertain to the Principle Recipient’s ability to effectively manage key processes:
25. **Program Management (including sub-recipient Management**): The audit should examine the Principle Recipient’s internal functions for managing Global Fund grants including: Existence of operating procedures for all key business processes related to the execution of activities funded under the Global Fund grants as well as evaluation of control systems for:

* Managing human resources,
* Identifying programmatic risks and taking proactive actions to mitigate them,
* Demonstrate ethical values

Review evidence of:

* Transparent processes for selection of sub-recipients and adequate systems for continuous assessment of sub-recipients;
* Availability of adequate contractual agreements between the Principal Recipient and its sub-recipients;
* Ensuring adequate and timely financial and program implementation and monitoring at all levels
* Pro-active coordination and oversight of sub-recipient activities through systematic reviews of sub-recipient activities, analysis and communication of findings following these reviews.

1. **Finance and Accounting Systems**: Review the Principal Recipients’ processes to efficiently book, consolidate and report financial information consistent with the assertions embodied in each cost category and module/intervention of the Annual Financial Report. The Auditor will need to ensure that areas to which significant program budget is allocated are included in the testing [[1]](#footnote-1).This shall include the review of control systems for:

* Ensuring that transactions charged to the program are properly budgeted and supported
* Cash management.
* Procuring goods and services (non-health products from the request to the payment);
* Managing and disposing of equipment purchased under the grant;
* Managing Payroll;
* Verifying the budgeting and the forecasting process.

1. **Monitoring and evaluation systems:** Assess the design and operational capacity of monitoring and evaluation processes that the Principle recipient uses for generating/channeling information that is reported to the Global Fund in the Performance framework including:

* Examination of the M&E planning processes,
* Review of data handling processes,
* Evaluation of the adequacy of data verification mechanisms,
* Review of the quality and completeness of data analysis by the Principal Recipient
* Assessment of staffing arrangement including segregation of duties for effective coordination of the M&E function (including the oversight over sub-recipient M&E systems)

1. **Procurement and Supply Chain systems**: Review the Principle Recipient’s governance mechanisms for ensuring efficient procurement processes and outcomes as well as effective distribution systems. This must include a walkthrough to identify the controls, understand the design and test them where relevant for effectiveness.
2. Where the Principal recipient has outsourced part or all of the above process to a third-party organization, the auditor is required to review the controls implemented by this organization. Organizations such as the Fiscal Agents, the Fiduciary Agents, etc. may be selected by the Global Fund or the Principal Recipients to mitigate some of the operational risks of the program[[2]](#footnote-2).
   1. **Audit Documentation and Evidence**
      1. **Access to Records and Documents of the Principal Recipient**
3. The auditor should have full and unrestricted access at any time to all records and documents to the audited entity’s staff and to the Principal Recipient 's locations insofar as this is possible and relevant to the audit of the Program. The auditor may request the Principal Recipient to get access to third-party entity engaged by the Principal Recipient.
4. The auditor is required to make available its audit working papers to the Global Fund if requested.
   1. **Planning**
      1. **Kick-off meeting with the Principal Recipient**
5. The auditor will arrange for an opening meeting with the Principal Recipient and the fiscal/fiduciary agent if applicable, to discuss and agree the approach, objectives, scope and expected timelines of the audit.
6. During the preparatory and kick-off meetings, the auditor may request some information that she/ he considers important for the preparation of the planning meeting. She/He may also contact the Principal Recipient directly to obtain such information. For all Focused countries, the attendance of the Local Fund Agent is mandatory. In High Impact and Core countries, the participation of the LFA would be based on Country Team need. The Fiscal/ Fiduciary Agents if any, must attend those meetings.
   * 1. **Audit planning**
7. The auditor should plan the audit in order that it is done effectively and efficiently. The auditor must ensure that appropriate attention is devoted to the main processes of the grant that must be determined in line with the grant budget and the initial risk assessment.
8. The auditor should have an audit plan documenting the audit approach and key principles of audit planning, fieldwork and reporting. The auditor should have an audit work program that details and documents the audit tests and procedures.
9. Before the start of the fieldwork and before the kick-off meeting, the auditor should provide to the Global Fund and the Principal Recipient, the audit plan for each grant including the scope of the review. Particular attention will be paid to the audit approach at Principal Recipient but also at the selected aub-recipients.
   * 1. **Risk Assessment**
10. The main risks to the attainment of the program objectives must be assessed by the auditor. The assessment should form the basis of the auditor’s approach and should be sufficient to design the audit procedures relating to the design of the Internal Control System. The auditor should assess whether the design of the Internal Control System sufficiently mitigates those risks.
11. **Risk assessment** is the identification and analysis of risks associated with the achievement of operations, financial reporting, and compliance goals and objectives. This, in turn, forms a basis for determining how those risks should be mitigated and managed during grant implementation[[3]](#footnote-3).
12. The Operational Risk Framework of the Global Fund uses the following sub-categories of financial risk to determine the overall financial risk assessment of individual grants:

* Inadequate Flow of Funds Arrangements
* Inadequate Internal Controls
* Financial Fraud, Corruption and theft
* Inadequate Accounting and Financial Reporting
* Limited Value for Money
* Inadequate Auditing Arrangements

1. The Auditor should ensure the financial risk is assessed around these sub-categories for the Principal Recipients, any selected aub-recipients and or any third-party managing one core financial process of the Principal Recipient. The auditor should refer to the Global Fund Guidelines on Financial Risks and the Financial Management Handbook or Grant Implementers for further details.
   1. **Fieldwork**
      1. **Audit evidence for control design**
2. The auditor should identify and assess the key controls of the Principal Recipient (and selected sub-recipient when required) and specifically those relating to the Program which are designed to prevent and detect the main financial risks (as described in the paragraph 23 above) with respect to the Program funding. The outcome of this review should inform the Global Fund on whether the controls as designed are, individually or in combination, suitable and effective with respect to the achievement of the program objectives.
3. Regarding the assessment of the design effectiveness, the auditor is required to perform a walkthrough. The following procedures could be used by the auditors for the assessment of the design and operating effectiveness of the Principal Recipients (or/and selected sub-recipient) internal control:
4. Inquiries with the Principal Recipient (or selected sub-recipients) staff;
5. Inspections of relevant documents;
6. Observation of implementation of the controls;
7. Reperformance of internal control procedures.
8. In any case, the auditor must provide his/her proposed detailed approach to achieve the objectives of the audit to the Global Fund or/and to the Principal Recipient.
   * 1. **Assessment of the operating effectiveness of controls**
9. The auditor should test those internal controls that have been determined as necessary to achieve the internal control objectives and assess their operating effectiveness throughout the period.
10. An internal control is operating effectively if, individually or in combination with other controls, it provides reasonable assurance that:
11. The Entity's internal control objectives are achieved and in particular that risks to the achievement of the objectives of the Program are properly managed and controlled;
12. The risks of error, irregularities and fraud with regard to Program funding are properly and timely prevented or detected.
13. When designing and performing tests of controls, the auditor should:
14. Perform other procedures in combination with inquiry to obtain evidence about:
    * How the internal control was applied;
    * The consistency with which the internal control was applied; and
    * By whom or by what means the internal control was applied;
15. Determine whether internal controls to be tested depend upon other controls (indirect controls) and, if so, whether it is necessary to obtain evidence supporting the operating effectiveness of those indirect controls; and
16. Determine means of selecting items for testing that are effective in meeting the objectives of the procedure.
17. When determining the extent of tests of controls, the auditor shall consider matters including the characteristics of the population to be tested, which includes the nature of controls, the frequency of their application (for example, monthly, daily, a number of times per day), and the expected rate of deviation.
18. Audit procedures for tests of controls may include but are not limited to inspection (of records, documents and assets), observation, inquiry of management and others within the Principal Recipient (or selected sub-recipients), confirmation, recalculation and reperformance.
    * 1. **Sampling and other means of selecting items for testing**
19. When designing and performing tests of controls, the auditor may apply audit sampling or other means of selecting items for testing. Audit sampling involves the application of audit procedures to less than 100% of items within a population of audit relevance (e.g. a class of transactions or account balance) such that all sampling units have a chance of selection in order to provide the auditor with a reasonable basis on which to draw conclusions about the entire population.
20. Audit sampling can use either a statistical or non-statistical approach. The auditor may use a judgmental selection of specific items from a population (e.g. high value or key items, all items over a certain amount, items to obtain information or items to test control activities).
    * 1. **Using the work of internal auditors**
21. If relevant for the audit, ISA 610 “Using the Work of Internal Auditors” should be used by the auditor. If the auditor assesses that an internal audit function can be relied on for the assignment, the auditor should:
22. Evaluate the specific work of the internal auditor and to what extent such work can be considered for the audit
23. Assess if the work of the internal audit is adequate for the objective of the audit.
    * 1. **Written representations**
24. In assurance engagements other than audits or reviews of historical financial information (ISAE 3000), the auditor should obtain representations from the management. A written representation is a statement by the management provided to the Auditor to confirm certain matters or to support other audit evidence. The management of the Principal Recipient who has the primary responsibility for the Program and its financial aspects will be requested to sign the representation letter.
    * 1. **Complementary letter**
25. The auditor may at any time during the audit process draw up a complementary letter if he/she considers that the Global Fund must be informed about facts and issues that are or may be urgent or of particular interest and importance to the Global Fund.
26. For instance, this could be the case of any fraud or irregularity that has occurred or that is likely to occur. The Global Fund will decide on follow-up measures including where appropriate the launching of an investigation by its Office of Inspector General.
    * 1. **Debriefing Memorandum**
27. The auditor will draft a Debriefing Memo for the closing meeting which will provide the main findings for discussion. The auditor should send a copy of the memo to the Global Fund.
    * 1. **Closing Meeting**
28. The auditor is expected to provide the conclusions of his/her work during a closing meeting with the Principal Recipient and the selected sub-recipients when relevant.
29. For all Focused countries, the attendance of the Local Fund Agent is mandatory. In High Impact and Core countries, the participation of the LFA would be based on Country Team need. The Fiscal/ Fiduciary Agents if any, must attend those meetings.
30. The purpose of this meeting is to discuss the Debriefing Memo and to obtain the confirmation and initial comments of the Principal Recipient (and the selected sub-recipients) on the auditor's findings and recommendations. The auditor and the Principal Recipient should agree the outstanding information to be provided by the Principal Recipient and where applicable a deadline for submission.
31. Using his/her professional judgement and/ or the appropriate standards, the auditor will deal with the comments of the Principal Recipient and by the Global Fund Country Team representatives and take these into account for the audit report.
    1. **Reporting**
       1. **Reporting Requirements and Language**
32. The Systems Audit report should be in line with the reporting template provided in Annexes 4 and 5 of these terms of reference. The report should be provided in English.
    * 1. **Draft report**
33. The Principal Recipient would provide comments on the auditor’s draft report within 10 calendar days from receipt of the draft report. The relevant Global Fund’s Country Team may also request to review the draft report. Following the review of the draft report, should the Global Fund request the auditor to carry out additional work, a new reporting deadline could be agreed.
34. The auditor should submit an updated draft report which takes into account the comments to the Principal Recipient (and eventually the Global Fund) within 5 calendar days from receipt of the comments. The Principal Recipient would provide feedback to the auditor within 5 calendar days from receipt of the updated draft report.
35. If the Principal Recipient 's comments are not received within this deadline, the auditor reminds the Principal Recipient until a written reply from the Principal Recipient is received. In case of excessive delays from the Principal Recipient (more than 10 calendar days), the auditor should contact the Global Fund to find out an appropriate solution.

* + 1. **Final report**

1. Once the auditor receives the final comments from the Principal Recipients, the final report is expected to be issued within the next 5 calendar days.
2. The auditor should submit three original hard copies to the Principal Recipient and one electronic copy of the final report to the Principal Recipient and to the Global Fund[[4]](#footnote-4). In the cover note, the auditor should confirm that three original paper versions of the final audit report have been sent to the Principal Recipient.
3. In any case, the Principal Recipient should ensure the auditor sends directly to the Global Fund an electronic copy of the reports[[5]](#footnote-5)

**Attachment 1: List of key controls to consider for testing**

| **Finance section** | **Example of financial Key controls** |
| --- | --- |
| ***Cash and Bank*** | * Segregation of duties: * Payment: Separate preparation, authorisation and signature. * Recording: Separate bookkeeping and cash custody * Reconcile payment document with original of supporting documents * Institute double signatures on bank account * Perform petty cash reconciliation and Perform bank reconciliation periodically (at least monthly) by independent people (not custodian of petty cash / bank) including resolution of discrepancies and explanations for significant and unusual reconciling items and signed management review |
| ***Assets Management[[6]](#footnote-6)*** | * Keep an up-to-date asset register based on periodic (preferably annual) physical count of the fixed assets. All assets should be tagged with a unique identification number * Reconcile the asset register with the general ledger and investigate difference for adjustment * All vehicle should have a logbook including data on distance travelled and fuel consumption. * On a periodic basis (weekly or monthly), compare average fuel consumption of the period with average fuel consumption of past period and explain variance. * Check, on a sample basis, occurrence of individual trips in the logbook and verify reasonableness of the distance travelled with the mileage meter of the vehicle. |
| ***Procurement[[7]](#footnote-7)*** | * Ensure procurement process is open and transparent; * Procurement evaluation should include a conflict of interest declaration process that all evaluators should complete * Segregation of duties: ensure those performing procurement are different from those authorising the contract with a supplier; * Ensure that: * The evaluation report of the proposals signed by all evaluators, * The contract align with the winning proposal/minutes of the evaluation. All difference should be signed off by the person that has such authority in the organisation; * At delivery of the goods (or the service), verify that the goods/service tally with the purchase order in term of quantity and specification. This control must be materialised |
| ***Financial Reporting*** | * Check that financial report agrees with underlying accounting report at both the Principal Recipient and the Sub-recipients; * Ensure there is a proper trail from the accounting records to the supporting documents; * Perform monthly budget monitoring and explain variance; * The accounting manager must ensure that there is a proper trail from accounting records to original of supporting documentation; * The CFO must sign off the financial reports sent to the Global Fund. |
| ***Payroll*** | * Timesheet must be approved by the person's supervisor on a monthly basis. Ensure timesheets are reviewed by a responsible individual within the programme (e.g. the team leader or the head of programme support unit); * On a monthly basis, compare the level of payroll with the level of the previous month and explain any variance. This control must be documented; * Ensure that there is adequate segregation of duties between preparation and payment of payroll; * Ensure that each new staff has a proper working contract; * Check accuracy and completeness of the monthly payroll amount; * On a monthly basis, ensure that the total paid amount tally to the approved payroll amount. |
| ***Sub-recipient monitoring*** | * Compare Sub-recipient funding request with the approved budget and ensure reasonableness based on absorption capacity * Compute quarterly absorption rate per Sub-recipient and take action to improve absorption * On a quarterly basis, check percentage of ineligible expenditure and take action on the root causes thereof * Review monthly the ageing balance of advances to Sub-recipient * Ensure regular site visits to the Sub-recipient followed up by a report to be discussed and shared with the Sub-recipient with recommendations and follow up actions * Ensure that a physical inventory of fixed assets at Sub-recipient level is done at least once a year. Any discrepancies should be communicated to the Sub-recipient and followed up to ensure that remedial action is taken by the Sub-recipient. * Perform a review annually on the internal control of the key Sub-recipient by the internal audit/ external audit. Internal control weaknesses should be communicated to the Sub-recipient and followed up to ensure that remedial action is taken by the Sub-recipient. * On a quarterly basis check a sample of expenses related to training/community activities carried out at Sub-recipient level to ensure that they are reasonable and in line with common practices. |
| ***Stock management[[8]](#footnote-8)*** | * Complete at least annually a stock count and reconcile the result thereof with the general ledger. All differences should be investigated; * Segregation of duties between: * custody of stocks and verification tasks such as reconciliation * management of stocks and authorisation of stock movements * management of stock and accounting of stock movement in the system * At reception of the drugs, ensure that the purchase order matches the good(s) received in quantity and specification * Compute monthly the level of stock expired or scrapped and design an action to reduce them |
| ***Entity-level controls*** | On a monthly basis (could also be quarterly depending on the periodicity), the top management could receive the following information and ensure appropriate actions are taken:   * Absorption rate for the period and in aggregate of the program; * accuracy of disbursement forecast; * cash balance level at Principal Recipient and Sub-recipients and comparison with previous periods; * Percentage of completion of management actions (TGF/ Audit/ OIG, etc.); * Ageing balance of advances to Sub-recipients and staff not liquidated; * percentage of stock (in value) that is scrapped or expired * Number of fraud event detected, amount at stake and measure taken. |

1. For instance, if the program budget is heavy on travel and training, the processes around such activities must be reviewed apart of the non-health procurement process. [↑](#footnote-ref-1)
2. The Global Fund Guidelines on Financial Risk Management could provide further details on the definition and roles of such third-party agents. [↑](#footnote-ref-2)
3. "Guide to Internal Controls - Finance.missouri.edu." <https://finance.missouri.edu/wp-content/uploads/guide-to-internal-controls.pdf>. [↑](#footnote-ref-3)
4. When the Audi firm is directly selected by the PR and therefore has a direct contractual relationship with the PR, it is expected that this contract includes a clause requiring to the Auditor to send directly an electronic copy of the final audit report to the Global Fund. [↑](#footnote-ref-4)
5. This is the responsibility of the auditor and should be mentioned in the contract between the PR and the Auditor. [↑](#footnote-ref-5)
6. Includes the following: Motorized and non-motorized vehicles, Equipment (including office and health equipment), Stock of health products and Civil works (renovation, refurbishment, construction, etc.) [↑](#footnote-ref-6)
7. Health and non-health [↑](#footnote-ref-7)
8. Mainly health products whether they are managed directly by the Principal Recipient or third-party agent such as a central medical store [↑](#footnote-ref-8)