

## **Chapter 8**

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# **International Co-operation**

## 8.1 Overseas Development Aid

### Background

Irish Aid, formerly Development Co-operation Ireland, which is a directorate of the Department of Foreign Affairs (the Department) is responsible for the administration of Ireland's programme of assistance to developing countries. The largest proportion of assistance is provided for in Subhead B - Bilateral and Other Co-operation. Expenditure from this subhead in 2005 amounted to almost €340m.

Irish Aid programme expenditure comprises grants to third parties such as partner governments, non-governmental organisations (NGOs), United Nations agencies, other multilateral bodies and aid partners. It also involves an element of direct expenditure. Funding may be disbursed from Departmental Headquarters or through Overseas Offices in the developing world. Table 30 shows the make up of expenditure for the years 2003 – 2005.

Table 30

	2003 € m	2004 € m	2005 € m
Grants to Countries having Irish Aid Overseas Offices <sup>34</sup>	130	143	145
Other Grants (e.g. to NGOs, Multilateral agencies)	110	146	<sup>35</sup> 189
Direct Expenditure	14	6	6
<b>Total Charge to Subhead B</b>	<b>254</b>	<b>295</b>	<b>340</b>

Additional direct expenditure of €11m (2003), €9m (2004) and €11m (2005) is included in Subhead A – Salaries, Wages and Allowances.

### Bilateral Assistance

Bilateral Assistance comprises support for eight specific programme countries and certain other regions and countries, assistance through non-governmental organisations (NGOs), support for the fight against HIV/AIDS and rehabilitation assistance.

Since 2005 eight countries - Ethiopia, Lesotho, Mozambique, Tanzania, Uganda, Zambia, Timor Leste and Vietnam – have been designated as programme countries by Irish Aid. These countries have a very low ranking in terms of human development indicators such as the percentage living in absolute poverty, life expectancy, adult literacy, infant mortality, access to safe water, sanitation and health services. In addition, assistance is provided for specific projects in a number of other regions and countries for example the western Balkans, Eastern Europe, Zimbabwe, South Africa and Palestine.

The bilateral relationship between Irish Aid and programme countries is governed by individual country strategy plans. These are negotiated between Irish Aid, and the relevant national government. Other donors and a number of the larger international organisations are consulted as appropriate. The plans are focused round the achievement of sustainable poverty reduction targets and are typically reviewed every three years. The percentage of aid channelled through government institutions at national and local government level was 68% in 2003, 74% in 2004 and 72% in 2005. Details of 2003 and 2004 expenditure,

<sup>34</sup> Includes Republic of South Africa and Zimbabwe that do not have programme country status.

<sup>35</sup> Includes Vietnam, which came on stream in 2005.

which can be directly related to the Department's most recent Annual Consolidated Audit Reports for those years, are shown in Table 31.

**Table 31 - Support Managed by Overseas Offices**

Country	Through National Government Systems € m		Through Local Government Systems € m		Other € m		Total Support Managed by Overseas Offices € m	
	2003	2004	2003	2004	2003	2004	2003	2004
Ethiopia	1.5	8.2	15.2	12.8	9.1	8.3	25.8	29.3
Uganda	25.8	27.2	0.6	.5	7.9	4.6	34.4	32.3
Mozambique	15.6	14.7	5.8	8.1	11.5	7.5	32.9	30.3
Tanzania	14.4	15.2	1.9	3.4	4.4	4.6	20.7	23.2
Zambia	4.9	5.9	2.4	4.0	7.3	7.8	14.6	17.7
Lesotho	8.2	9.1	0.0	0.0	2.6	2.3	10.7	11.4
Timor Leste	1.5	2.0	0.0	0.0	1.4	2.0	2.9	4.0
South Africa	5.3	3.4	1.6	2.5	4.8	4.1	11.7	10.0
Zimbabwe	0.0	0.0	0.0	0.0	0.8	0.8	0.8	0.8
<b>Total</b>	<b>77.2</b>	<b>85.7</b>	<b>27.5</b>	<b>31.3</b>	<b>49.8</b>	<b>42</b>	<b>154.5</b>	<b><sup>36</sup>159</b>

The aid delivered through national government involves a range of aid instruments the majority of which relate to moneys that are clearly earmarked for specific purposes e.g. health, education, agriculture, water and sanitation, or specific projects. In Tanzania and Mozambique some of this funding is delivered as general budget support to the Treasury.

The balance of Irish Aid programme money, not delivered via national or local government, includes administration, support to NGOs, UN and other multilateral agencies and moneys spent directly by Irish Aid on behalf of various programmes and partners.

I undertook an examination of Irish Aid audit and evaluation procedures with particular emphasis on projects funded through bilateral assistance in the programme and other countries in 2003 and 2004 as these are the most recent years for which consolidated results of the evaluation procedures used are available.

## Examination Findings

### Financial Control and Accountability

All assistance budgets are submitted annually, in advance, for approval by an interdepartmental committee, set up by Government decision, on which the Department of Finance and other Departments with an involvement in development co-operation are represented.

<sup>36</sup> This figure includes the Subhead A costs of Overseas Offices, which exceeded €9m in 2004.

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This interdepartmental committee, acting as the Programme Appraisal and Evaluation Group (PAEG) under the authority of the same Government decision, approves all new expenditure proposals. The group is assisted by external consultants who evaluate the proposals before submission for consideration.

Both direct and indirect aid expenditure are extensively audited. The audit of indirect expenditure relies increasingly on the work of auditors external to the Department. The Auditors General of partner governments account for the largest proportion of other auditors on whom Irish Aid relies, with the larger audit firms contributing most of the remainder. Irish Aid works closely with the Auditors General to strengthen their capacity (e.g. funding of training initiatives, development of IT audit and equipment purchases).

In the eight programme countries in receipt of bilateral assistance, Ireland's aid programmes, are subject to annual external audit by

- The Department's Evaluation and Audit Unit (EAU) or
- Professional auditors commissioned by Irish Aid, or jointly with other aid donors or independently by development partners or
- Other countries' Auditors General.

Area-based programmes (programmes which operate in specific local authority districts) and sector support programmes (which cover specific sectors such as health or education) in these programme countries are also subject to annual audit.

There are accounting staff in all of the Overseas Offices in the African programme countries.

## Evaluation and Audit Unit

The EAU is an independent unit within the Department. Its mission is to provide an efficient, effective, relevant and independent evaluation and audit function and to contribute to policy development within the overall assistance programme. The unit is currently staffed by a head of unit, three auditors<sup>37</sup> two evaluators and three support staff based in headquarters and six auditors based locally in the Department's Overseas Offices in programme countries.

The work of the EAU is carried out in accordance with an annual work plan and the Strategic and Multi-annual Work Plan 2006 to 2008. The plan notes that progress has been achieved recently in strengthening evaluation and audit in Irish Aid but does, however, state that staff shortages limit the unit's ability to deliver adequate coverage across the whole programme.

I enquired as to the EAU's ability to deliver adequate audit coverage across the whole aid programme in light of the staff shortages and the implications of these shortages for the unit's stated mission.

In reply, the Accounting Officer stated that Irish Aid recognises that, as the aid programme grows, the capacity of the EAU will need to be enhanced in order to ensure effective audit and evaluation. He stated that Irish Aid recognises that the EAU has experienced some limitations due to staffing, particularly in developing a programme of value for money audits, and on providing audit support to other sections of Irish Aid. The EAU had at all times aimed to deploy available resources efficiently and effectively with a particular focus on the overseas offices and to maximise assurance by reliance on the work of others and through the use of consultants.

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<sup>37</sup> Two additional posts have been sanctioned.

In relation to staff numbers, he stated that identifying and retaining staff for this highly skilled area presented a challenge to Irish Aid. In the programme countries 3 additional local staff have been recruited since 2003 bringing the total to 6 local audit staff.

He further stated that the implication of staff shortages had been delays in feeding back to and supporting line management in the interpretation of partners' audit reports. However, this had to be considered in the context that support is available immediately from the 6 internal auditors in the programme countries and via the in-country management structures in Irish Aid and other donors in the field.

The Accounting Officer also stated that the EAU utilises audits commissioned by various partners, where these audits include Irish funds. The largest proportion of these audits consists of audits carried out by national Auditors General and audits carried out by recognised audit firms. This practice of reliance on the audit work of others in relation to grants to development partners assisted Irish Aid to fulfil its requirements under the Rome Declaration on Harmonisation.

## **Annual Consolidated Audit Report**

The EAU produces an annual Consolidated Audit Report, which covers direct expenditure by Irish Aid and the disbursement of grants to development partners. The reports for 2003 and 2004 summarise all the audit activity completed in respect of expenditure in those years. They are intended to inform line management, support the Audit Committee in its oversight of the audit and evaluation function and assist the annual audit by my Office.

The objectives of the Consolidated Audit Report are to

- Identify gaps in audit assurance by detailing what expenditure has not been audited or for which audit reports have not been received
- Summarise the findings of the large number of audits and management letters to identify key deficiencies in accounting procedures and internal control
- Show the status of recommendations arising from previous years' audits
- Highlight whether financial statements give a true and fair view of the financial position of the entity or programme being audited.

## **Overall Audit Coverage 2003 and 2004**

The 2004 Consolidated Audit Report, which was completed in March 2006, included an update of the original 2003 report completed in October 2005. This showed that the audit coverage of expenditure had increased from 78% to 85% (this had increased again to 89% by mid-July 2006) for 2003. The audit coverage for 2004, as at April 2006, was 63%. This had increased to 84% by mid-July 2006. The Department's policy is that the level of audit coverage should aim to be greater than 85% each year. The audit coverage of 2003 and 2004 expenditure as at mid-July 2006 is outlined Table 32.

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**Table 32 Audit Coverage**

Country	2003			2004		
	Amount Audited €	Amount Unaudited €	% Unaudited	Amount Audited €	Amount Unaudited €	% Unaudited
Ethiopia	18,994,084	6,785,836	26	23,775,744	5,533,305	19
Lesotho	10,573,256	109,525	1	11,474,867	-	0
Mozambique	28,583,553	4,351,987	13	20,278,900	10,005,227	33
South Africa	9,782,614	1,961,627	17	9,186,856	886,920	9
Tanzania	20,359,075	357,025	2	19,283,474	3,940,000	17
Timor Leste	2,485,743	450,420	15	3,915,727	9,900	0
Uganda	33,448,892	878,779	3	30,424,011	1,848,152	6
Zambia	12,188,710	2,460,231	17	14,941,533	2,712,642	15
Zimbabwe	368,195	394,313	52	275,704	482,475	64
<b>Total</b>	<b>136,784,122</b>	<b>17,749,743</b>	<b>11</b>	<b>133,556,816</b>	<b>25,418,621</b>	<b>16</b>
<b>Total for Year</b>	<b>€154,533,865</b>			<b>€158,975,437</b>		

As audit reports had not been received at the time of my examination in respect of 37% (this had improved to 16% at 30 June 2006) of 2004 expenditure, I enquired as to the total number of reports receivable for 2003 and 2004 and how many of these were currently outstanding. I also enquired as to the limitations on the Department's scope to take effective action in respect of material adverse findings or significant audit recommendations as a result of delayed receipt of audit reports. I further enquired as to how the Department ensured that the stated mission of EAU to maintain an efficient, effective, and relevant evaluation and audit function is achieved and how the risks to public funds from irregularities or misappropriations remaining undetected, due to delays in receiving reports, are minimised.

The Accounting Officer stated that Irish Aid's overseas office audit policy emphasises that audit coverage is a tool and does not, in itself, give complete assurance. The policy outlines 85% as a guide figure only and the specific circumstances in each country must also be taken into account. There are many additional processes and tools in place that inform Irish Aid's assurance. These include partner Governments' own public expenditure reviews, tracking studies, work by other donors, internationally conducted national assessments (typically led by IMF/World Bank), day to day monitoring and discussions by line management based in the overseas offices.

### Audit Reports and Opinions Received

Over 450 audit reports were received in respect of 2003 and 2004 expenditure. The Accounting Officer pointed out that these fell into two distinct categories: internal audits relating to Irish Aid and audits relating to the use of grants by the Department's development partners. The 355 audit reports relating to the use of grants by development partners are analysed in Table 33, which shows, by country, the percentage of reports, which contained a qualification or disclaimer. The Accounting Officer said that it was important to note that none of the qualified reports related to Irish Aid's direct expenditure.

Table 33 Analysis of Audit Opinions received in 2003 and 2004

	2003 <sup>38</sup> Audit reports			2004 Audit reports		
	Received	Qualified or Disclaimer Opinions	% Qualified or Disclaimer	Received	Qualified or Disclaimer Opinions	% Qualified or Disclaimer
Ethiopia	13	2	15	31	2	6
Lesotho	25	5	20	20	4	20
Mozambique	33	12	36	29	13	45
South Africa <sup>39</sup>	22	12	55	12	9	75
Tanzania	25	10	40	20	14	70
Timor Leste	2	0	0	2	0	0
Uganda	11	3	27	24	1	4
Zambia	33	2	6	43	3	7
Zimbabwe <sup>40</sup>	6	5	83	4	3	75
<b>Total</b>	<b>170</b>	<b>51</b>	<b>30</b>	<b>185</b>	<b>49</b>	<b>26</b>

Regarding 2003, the Accounting Officer stated that two audit reports were outstanding at 1 June 2006. These reports were due from an Auditor General and the delay was due to local factors. The office of the Auditor General concerned had not yet completed all audits in relation to the financial year ended 7 July 2004, which includes Irish Aid grants issued after 7 July 2003. The outstanding audits were currently in progress.

In regard to the risk to public funds, he informed me that development activities by their nature take place in a high-risk environment. There are delays in receiving certain types of partners' audit reports, but the effect of timing on the risk of misappropriation or irregularities is lower than might initially appear. Irish Aid line management is usually aware of the issues raised by an audit before the field work is fully completed.

He also stated that risk is minimised by the extensive management systems in place in Irish Aid to manage the aid programme. However, he stated that it must be acknowledged that on occasion delay does affect Irish Aid's reaction to audit issues and the ability to follow-up. Irish Aid responds in a number of ways

- Working with partners' line management to agree a programme of remedial action
- Withdrawing funding or temporarily withholding funding or part funding pending the implementation of reforms, including staff changes
- Working with partners to conduct detailed investigations.

<sup>38</sup> The source of these figures is the 2003 report. The 2004 report updated this coverage. Disclaimers are generally issued in situations where the auditee has failed to keep full and complete books of account.

<sup>39</sup> Most qualifications in South Africa reports (9 in 2003, 8 in 2004) are in respect of income. As the organisations derive their income from voluntary donations, the income cannot be verified before it is entered in the accounting records. As this is the nature of the operation of such organisations, this qualification is not, in itself, a major concern to Irish Aid.

<sup>40</sup> A number of auditors issued disclaimer opinions due to the hyperinflationary situation in Zimbabwe. These fully account for two of the adverse opinions in 2003 and for all three in 2004

## Consolidated Audit Report - Audit Findings

Audit findings are classified by EAU according to the level of seriousness

- Category A findings relate to major weaknesses in financial controls or a recurring issue that it is considered must be urgently addressed.
- Category B findings are important matters that will significantly improve the control environment, the accounting system or the operations of the entity but are not so serious or prevalent as to be considered major weaknesses.
- Category C are minor or isolated weaknesses that should nevertheless be addressed to improve the control environment, the accounting system or the operations of the entity.

Many findings are in respect of projects/programmes that are co-funded by Ireland with other donors.

Table 34 analyses the number of audit reports received and the related number of Category A findings by each aid supported country.

**Table 34 Analysis of Audit findings as classified within management letters (including internal audit reports and VFM studies)**

Country	2003		2004	
	No. of Reports Received	No. of Category A Findings	No. of Reports Received	No. of Category A Findings
Ethiopia	12	16	28	7
Lesotho	37	32	23	36
Mozambique	30	46	36	51
Tanzania	28	62	34	64
Timor Leste	2	4	2	1
Uganda	9	16	27	16
Zambia	53	24	74	38
South Africa	24	9	14	2
Zimbabwe	6	2	5	3
<b>Total<sup>41</sup></b>	<b>201</b>	<b>211</b>	<b>243</b>	<b>218</b>

In regard to the nature of the Category A findings, the following are examples of some of the more common themes noted

- Lack of supporting documentation for expenditure
- No tendering for contracts or comparative quotations for purchases

<sup>41</sup> These overall totals are greater than those shown in Table 4 because they include Internal Audit Reports and VFM Studies in addition to audit opinions.

- Expenditure not always authorised
- Use of funds for other than intended purposes
- Weak internal controls
- Long outstanding unsettled advances
- Stores discrepancies.

I enquired what the Department's approach was to the management of Category A findings disclosed in the audit reports and as to how the Department can ensure that the appropriate action in these cases is timely and relevant given the delays in the Department becoming aware of them.

In reply, the Accounting Officer stated that the follow-up to partners' audit reports is about addressing issues arising in third parties that have received Irish funding and funds from other donors, and this affects the nature of that follow-up. He stated that all of the programmes are implemented in partnership with developing countries and other donor countries and follow-up is conducted in this context. Follow-up with partners is aimed at the strategic level, with the intention of improving the overall financial management and accountability of the partners.

He also stated that working with other donors to support the implementation of ongoing public sector financial management and administrative reform processes is the key to rectifying many of the issues identified in audit reports. In addition, the joint donor/government coordination committees that exist in programme countries are also a platform for follow-up actions to audit and other programme issues. In non-governmental partners, the follow-up is usually via discussion between Irish Aid and the partners' senior management. All audit reports on partners commissioned by Irish Aid and the reports of most Auditors General include follow-up on the issues raised in the previous year's audits.

He informed me that Irish Aid's approach to the Category A issues arising in the programme varies depending on the particular structure and type of programme and the level of influence Irish Aid can bring to bear. The ranking system was introduced so that Category A issues could be clearly identified and could be emphasised by line management in follow-up. This is particularly important when the line managers do not have a financial background. The intention of the ranking is to assist them to identify the key areas to focus their follow-up efforts. The ranking should assist line managers to check that they have already identified the key issues arising from the underlying individual audit reports that would have been available to line management for some time.

He further stated that, in many cases, Ireland is a contributor to programmes along with many other donors who share information and work closely together. In such programmes, each donor does not conduct individual follow-up, but rather a lead donor is designated to take primary responsibility for the programme. In such cases, it is the lead donor who is responsible for following up on audits on behalf of all donors and sharing information on actions taken.

In this context, the follow-up to each partner's qualified audit reports is different, but influenced by

- The nature of the aid in question and the corresponding donor/government management structures
- The amount of expenditure in the programme from all donors and government
- The strategic importance of the programme/project
- The timeframe of the programme
- The partner's line management's ability to implement a programme of action.

## **Risk Assessment and Value for Money**

I enquired if a risk assessment of overseas projects had been carried out and, if so, what was the outcome in terms of risk identification and management. In reply, the Accounting Officer stated that the PAEG approval process is a comprehensive appraisal system to which all country aid programmes are subjected to test for quality, poverty focus, sustainability and adherence to policy priorities. In addition to the PAEG system, a specific example of the outcome of the introduction of risk assessment methodology in Irish Aid is the inclusion of a section on risks in the quarterly reports submitted by the programme countries to Departmental headquarters.

He also stated that the wider international donor community carries out a wide range of assessments, which include risk analyses, and these studies are utilised by Irish Aid. At a national partner Government level, these assessments are usually led by the IMF/World Bank using formal tools that have gained international acceptance. Most developing country partners do not yet have sophisticated and effective risk management and mitigation systems integrated into their own internal management systems. An important objective of the donor community (including Ireland) in working together with partner Governments through national plans is to develop all aspects of public sector performance, including risk management. He added that progress varies from country to country and significant challenges remain.

Finally, I asked how many value for money reports had been completed or planned since 2003. In reply, the Accounting Officer stated that Irish Aid has completed six value for money studies since 2003, two were currently in progress and at least one is planned for 2007. He also stated that Irish Aid is engaged in value for money studies via the Expenditure Review Initiative of the Department of Finance.