



AKPBSP

FIDUCIARY RISK ASSESSMENT

AGA KHAN PLANNING AND BUILDING SERVICES, PAKISTAN

May 6, 2016



pwc

A·F·FERGUSON & Co. | A member firm of the PwC network

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1. List of acronyms / abbreviations

AKPBSP	Aga Khan Planning and Building Services, Pakistan
AKDN	Aga Khan Development Network
AKES	Aga Khan Education Services
ASP	Assessment and Strengthening Program
CBS	Community Based School
CHIP	Community Health Improvement Program
GBC	Gilgit Baltistan Council
HR	Human Resource
IA	Internal Audit
IIA	Institute of Internal Auditors
IT	Information Technology
JCVF	Japanese Country Value Fund
KM	Knowledge Management
M&E	Monitoring and Evaluation
NUPAS	Non-US Organisation Pre-Award Survey
PCF	Petty Cash Fund
RSPN	Rural Support Programmes Network
SHIP	School Health Improvement Program
USAID	United States Agency for International Development
WHIP	Water and Hygiene Improvement Project

2. Summary of assessment results

2.1 Objectives

The primary objective of this assessment is to confirm that Aga Khan Planning and Building Services, Pakistan (AKPBSP) has acceptable organisational and management structures, accounting, financial management systems and other systems of internal controls, quality assurance capabilities, as well as acceptable policies, procedures, practices. In addition, the assessment will determine if AKPBSP:

- can adequately safeguard, monitor and efficiently utilise resources;
- can obtain, maintain, and fairly disclose reliable data and information;
- has the institutional framework for accurate and reliable reporting, and;
- can comply with applicable laws and regulations.

Other objectives of the assessment are:

- compliance with the rules and regulations;
- to evaluate organization's capacity for receiving the increased assistance based on a comprehensive absorptive capacity analysis;
- to ensure that management leadership, organisational strengths, quality of staff and quality of processes and procedures are adequate to support the management of a USAID funded award;
- to assess the organizational capacity to manage USAID advance funding mechanism per USAID regulations; and
- to test on sample basis the financial and procurement systems.

2.2 Procedures performed

The following procedures were performed:

- reviewed policies and procedures established by the entity to confirm that the same are adequate;
- inquired the management about practices followed to ensure the program objectives are met;
- reviewed reports prepared by the management to ensure financial information is adequately captured and disclosed to senior management and donors;
- obtained list of employees to assess strength of department;
- reviewed correspondence with donors to assess the working relationship with the entity;
- reviewed cooperative agreement with the donor to assess whether the management's current capability is adequate to meet the conditions agreed therein;
- reviewed the personal files of key process owners to verify that they possess adequate qualifications and experience to enable effective performance of the requisite tasks; and
- verified transactions on a sample basis for compliance with established policy and procedures.

2.3 Summary of assessment results

We have made a review and evaluation of the managerial capacity and internal control systems of AKPBSP using those criteria established by USAID / Pakistan. Our review included tests of compliance with the organization's stated procedures to the extent that such testing was deemed necessary and feasible. Our review is not an audit of any financial statement(s) prepared by AKPBSP.

The management of AKPBSB is responsible for establishing and maintaining systems of internal controls and financial management. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable, but not absolute assurance that assets are safeguarded against loss from unauthorised use or disposition, and that transactions are executed in accordance with management's authorisation and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. We understand that the objective of those financial management and internal control procedures comprehended in USAID's criteria is to provide similar assurance.

Based on this knowledge and the review and evaluation conducted by our firm, we believe AKPBSB's current policies procedures are sufficient for USAID / Pakistan's purposes, assuming satisfactory compliance, except for the conditions described in section 6 of this report which we believe would be material weaknesses. The level of risk identified as a result our assessment is considered to be low to moderate risk.

Further, nothing came to our attention that would cause us to believe that AKPBSB does not have the managerial, technical, administrative and financial capabilities to carry out the proposed USAID funded activities except for the effect, if any, of the matters included in section 6 of this report.

3. Executive summary

3.1 Introduction

We have been engaged by Assessment and Strengthening Program – Rural Support Programmes Network (ASP-RSPN), a USAID funded project, for fiduciary risk assessment of AKP BSP for Water and Hygiene Improvement Project (WHIP), jointly funded by USAID and AKP BSP.

This report sets out the findings and assessment recommendations based on our review of AKP BSP in accordance with the terms and conditions as set out in Task Order ASP-CPO/A&C/Ass-A/01-2016 dated March 9, 2016. In this respect, we have performed a fiduciary risk assessment using the Non-US Organisation Pre-Award Survey (NUPAS) checklist in accordance with the scope of our work as set forth in section 5 of this report.

3.2 Scoring of areas

The scoring, based on the criteria stipulated in NUPAS checklist, is as follows:

No.	Criterion	Average score
1	Legal structure	3.80
2	Financial management and internal control systems	3.44
3	Procurement systems	3.67
4	Human resources systems	3.50
5	Project performance management	4.00
6	Organization sustainability	3.00
	Overall score	3.57

The scoring and assessment of capacity are determined using risk scoring and analysis detailed in section 5 of this report.

3.3 Summary of findings

Our findings are summarised below:

Risk areas reviewed	Observations and findings	Score	Para ref.
1. Legal structure			6.1
1.1 Local organisation definition	None	4.00	N/A
1.2 Legal requirements	None	4.00	N/A
1.3 Organizational structure	Absence of region and project wise organisational chart.	3.00	6.1.1
1.4 Governance	None	4.00	N/A
1.5 Control environment	None	4.00	N/A
2. Financial management and internal control systems			6.2
2.1 Banking relationship and accounts	Date and approval not appearing on the bank reconciliation statements.	3.67	6.2.1
2.2 Accounting / bookkeeping system	Delays in posting of transactions into the system.	3.00	6.2.2
2.3 Chart of accounts, General Ledger and Financial Statements	None	4.00	N/A

Risk areas reviewed	Observations and findings	Score	Para ref.
2.4 Variance analysis (budget to actual costs)	The financial and procurement policy does not cover variance analysis for projects.	3.00	6.2.3
2.5 Allowable and unallowable cost	The financial and procurement policy does not cover allowable and unallowable cost.	3.00	6.2.4
2.6 Direct and indirect costs	None	4.00	N/A
2.7 Payments – segregation of duties	Non-compliance of ‘financial and procurement policy’ with regards to petty cash.	3.50	6.2.5
2.8 Accounting cycle	None	4.00	N/A
2.9 Financial records management	Absence of policies and procedures in respect of record retention and Information Technology.	2.00	6.2.6
2.10 Sources of funding	None	4.00	N/A
2.11 Financial reporting	Absence of practice with regards to preparation of monthly financial statements.	3.00	6.2.7
2.12 Audit and review of Financial Statements	<ul style="list-style-type: none"> The Internal Audit plan provided to us did not mention the indicative timeline for internal audit work. A formal risk assessment exercise was not conducted to assess inherent risk and strength of control environment. The responses from management on the IA findings do not include the responsible authority and the due date for implementation of action plan. 	3.00	6.2.8
2.13 Financial management personnel	None	4.00	N/A
2.14 Cash flow management	None	4.00	N/A
3. Procurement systems			6.3
3.1 Procurement policies, procedures and practices	The financial and procurement policy does not cover dispute resolution and claims made by vendor.	3.50	6.3.1
3.2 Compliance with policies and procedures – reasonableness of price	• Weak controls over review of payments to vendors.	3.50	6.3.2
	• Absence of a formal tenancy agreement for use of office premises.		6.3.3
3.3 Procurement and sub-awards	None	4.00	N/A
4. Human resources systems			6.4
4.1 Overall HR policies and procedures	• Hired employee not meeting the required qualification criteria.	2.50	6.4.1
	• Incomplete records in personal file maintained by HR department.		6.4.2
	• Periodic review of HR manual to incorporate changes in practice not carried out.		6.4.3
4.2 Staff time management	None	4.00	N/A

Risk areas reviewed	Observations and findings	Score	Para ref.
4.3 Payroll system	Absence of documented policy on compensation.	3.00	6.4.4
4.4 Travel policies and procedures	None	4.00	N/A
5. Project performance management			6.5
5.1 Technical evaluation criteria	None	4.00	N/A
5.2 Project management Capacity	Inability to meet the completion deadline agreed in the contract.	4.00	6.5.1
6. Organisational sustainability			6.6
6.1 Absorptive capacity	<ul style="list-style-type: none"> Internal Audit Department needs to be strengthened. 	3.00	6.6.1
	<ul style="list-style-type: none"> Absence of documented policy and procedures with regards to preparation of cashflow forecast for projects. 		6.6.2

The NUPAS checklist is provided in the Annexure / Appendix section to this report

4. Description of the entity and program

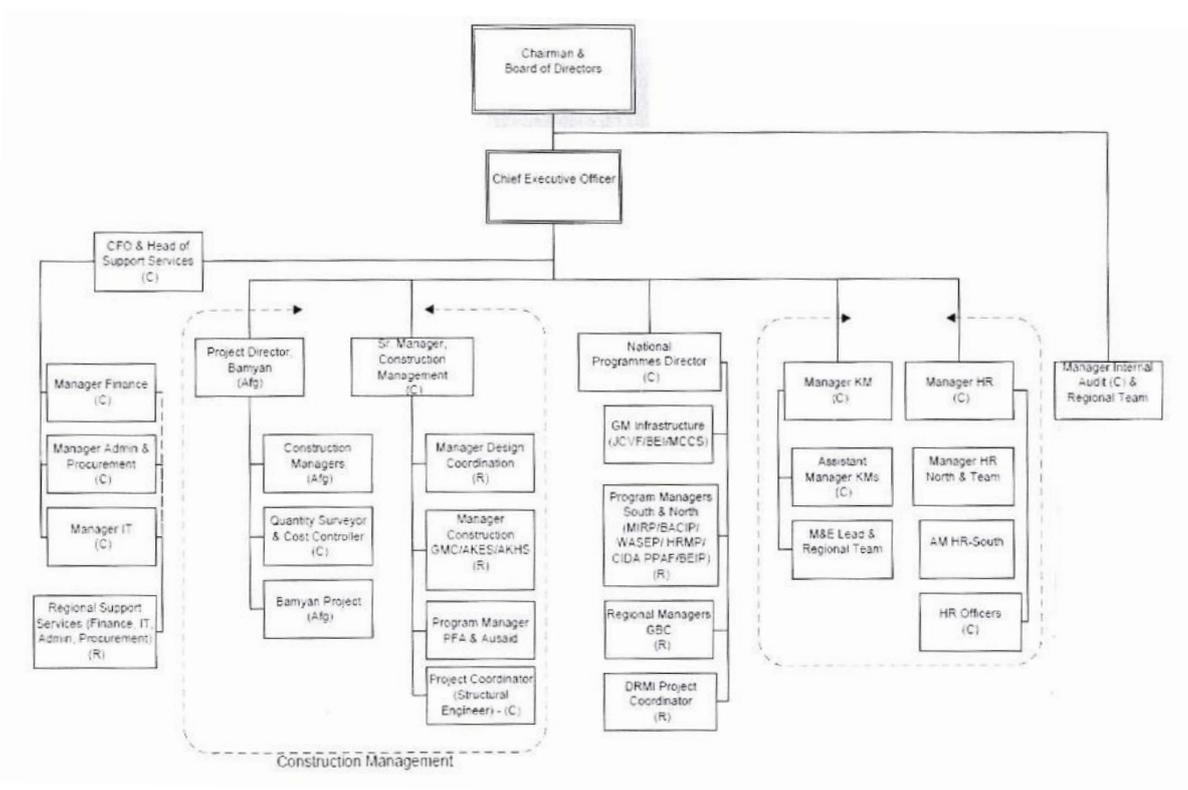
AKPBSP was established in 1980 and is an independent executive body with the objective to plan and implement infrastructure and technology related development initiatives to improve living conditions. AKPBSP is mandated to assist local communities within various provinces and regions for the purpose of development program areas such as habitat risk reduction, energy efficient building and construction improvement, water supply and sanitation, and natural resources conservation.

Financial strength:

The extract of statement of comprehensive income detailing the amount of grant utilised for the year 2014 and 2013 is summarised below:

Statement Of Comprehensive Income	2014			2013		
	Unrestricted Funds	Restricted Funds	Total	Unrestricted Funds	Restricted Funds	Total
(In Rs)						
Income						
Funds through community through voluntary contribution	20,809,306	-	20,809,306	22,864,924	-	22,864,924
Restricted Fund Utilized		627,075,324	627,075,324	-	619,686,759	619,686,759
Deferred Capital Grant realized	646,374	20,613,523	21,259,897	373,812	23,064,061	23,437,873
Other Income	7,790,853		7,790,853	3,172,618		3,172,618
Total Income	29,246,533	647,688,847	676,935,380	26,411,354	642,750,820	669,162,174

The organogram of the entity is provided below:



Total number of employees: 171

The iScala ERP system has been installed at entity’s offices to capture financial information. The said software includes modules for general ledger, account receivable, accounts payable, purchase order and inventory control. The management at central office obtains daily back up of the data stored at all regional offices and uses the same to update central records with regards to entity’s operations at all regions.

WHIP is a jointly funded project which is being implemented by AKPBSP. This project is governed by Cooperative Agreement no. **AID-391-A-15-00007** between AKPBSP and USAID signed on August 21, 2015.

The overall mission envisaged under the Project is to create an enabling environment for the people of Murtazaabad, including school children and teachers through the provision of clean and safe drinking water, health and hygiene.

The aforementioned objective is planned to be achieved through the following activities:

- enhanced social cohesion and increased community participation, especially of women in the installation, administration, operation and maintenance of safe drinking water supply infrastructure and health & hygiene promotion and adoption in Murtazaabad through social mobilization and formation and training of Water and Sanitation Committee;
- sustainable infrastructure for provision of clean and safe drinking water from provision of household and communal water infrastructure in Murtazaabad; and
- increased awareness of hygiene appropriate behavior change through Community Health Improvement Program (CHIP) sessions and School Health Improvement Program (SHIP) sessions.

AKPBSP is responsible for undertaking the delivery and implementation of the Project in accordance with the Cooperative Agreement.

The WHIP is a USD 496,727 project to be funded jointly by USAID and by AKPBSP. The funding has been allocated as follows:

Cost Category	USAID contribution	AKPBSP cost share	Total project cost
	(In US Dollars)		
Salary and wages	132,225	69,611	201,837
Fringe benefits	10,085	-	10,085
Consultants	785	-	785
Travel, transportation per diem	5,457	-	5,457
Procurement, equipment & supplies	141,512	12,662	154,174
Training	72,932	-	72,932
Other direct costs	38,971	12,485	51,456
Total estimated cost	401,967	94,758	496,726

The selected location of the project is Murtazaabad village comprising a total 430 households, five schools and other communal buildings such as mosques. The entity has a dedicated bank account at Habib Bank Limited bearing account number 1783-79004606-01 in respect of receipt of and payment from USAID funds.

5. Scope and methodology of the assessment

Composition of assessment team

Composition of the A. F. Ferguson & Co. (AFF) team for the fiduciary risk assessment:

Name	Designation	Role
Khurshid Hasan Sabzwari	Partner	Khurshid was responsible for the overall supervision of the project as the engagement leader.
Muhammad Humair	Associate Director	Humair worked in the capacity of the project manager, giving on field manager direct guidance throughout the assessment. Further, he was also responsible for conducting meeting with higher level management at AKP BSP.
Asad Ahmed Ali	Assistant Manager	Asad worked in the capacity of on field manager throughout the assessment. He served as the link between the project manager and the team members to coordinate efforts, conducting meetings with the departmental heads and was responsible for the overall supervision of on field team members.

Scope and methodology

The fiduciary risk assessment was conducted using the NUPAS checklist developed by USAID. The assessment was performed for following fiduciary risk areas:

- Legal structure;
- Financial management and internal controls systems;
- Procurement systems;
- Human resources system;
- Project performance management; and
- Organisational sustainability.

In order to address the requirements of the NUPAS checklist, meetings and interview sessions were held with those responsible for relevant areas covered in the checklist. The necessary documentation, references, policies and by-laws were tested and confirmed with the designated process owners. We conducted walkthrough procedures on sample basis to cover the existence and completeness of documentation, required approvals, progress follow up, and supervision of the processes. Further, the cooperative agreement for the WHIP project was reviewed to assess whether the management’s current capability is adequate to meet the conditions agreed therein. Furthermore, the cooperative agreement for the WHIP project was reviewed to assess whether the management’s current capability is adequate to meet the agreed conditions therein.

The risks identified are included in this report along with suggested recommendations.

Our assessment and findings are based on current and previous projects undertaken by AKPBSP to determine whether AKPBSP has sufficient financial management, organisational, and management capacity to manage USAID funds in accordance with U.S. Government and USAID requirements. Our findings are based mainly on the review of the following projects of AKPBSP:

Project	Donor
Water and Hygiene Improvement Project	USAID
Construction of new classrooms in Community Based Services, Sujawal, Sindh, Pakistan	Aga Khan Education Services
Construction of first floor on existing building at Model School, Oshikhandass, Gilgit Baltistan, Pakistan	Aga Khan Education Services
Environmental Health Project*	Japanese Country Value Fund
Ensuring Social inclusion through accessible water and sanitation	Sightsavers

* The records of Environmental Health Project, Japanese Country Value Fund for the year 2015 were under custody of Auditor General for annual audit purposes. Hence, our procedures with respect to the said project were restricted to records for the period from January to March 2016.

Risk scoring and analysis

The risk scoring ranges between 1 - 4 and is based on the adequacy of managerial and financial capacity of the non-U.S organization to manage USAID funds. The scoring has been used to drive the appropriate level of treatment to mitigate each identified risk. The individual scoring has been determined using Table 4.1.

Capacity Risk	
Inadequate capacity	1.00-1.50
Weak capacity	1.51-2.50
Adequate capacity	2.51-3.50
Strong capacity	3.51-4.00

Table 4.1 : Capacity rating

The assessment of capacity is based on the following table:

Capacity	Assessment rationale
Inadequate capacity 	Significant control weaknesses which could expose the organisation to significant financial or other loss or otherwise significantly impair its ability to manage USAID funds. (Key deficiencies and significant weakness that are not remediable before the award, or high risk)
Weak capacity 	Significant control weaknesses could expose the organization to unacceptable/inadequate levels of unmanaged risk. (Some deficiencies and significant weakness that are not easily remediable before the award, or moderate to high risk.)
Adequate capacity 	Although a control weakness was noted, compensating controls and other factors exist to reduce the residual risk within the organization to acceptable levels. (No deficiencies, significant weakness, if any, are remediable before the award, or low to moderate risk.)
Strong capacity 	Overall, a strong control framework is in place given the inherent business risks. Some improvements may be recommended to routine detailed control activities. (No deficiencies or significant risk or low risk.)

The observations identified are set forth in section 6 of this report.

6. Risks identified

6.1 Legal structure

6.1 Legal structure

6.1.1	Absence of region and project wise organisational chart.	NUPAS checklist Ref. 1.3
<p>Criteria:</p> <p><i>The organisation should have a strong organizational structure relevant to its mission and goals, with well defined and highly appropriate lines of communication between departments / functions.</i></p> <p>Condition:</p> <p>The entity has an organogram for central office covering various departments including managers and leaders of regional teams while defining their reporting lines to board of directors.</p> <p>However, the entity does not have a comprehensive organisational chart covering different positions at regional offices and projects.</p> <p>Cause:</p> <p>Lack of management capacity to timely update the regional and project-wise organisational chart based on status of projects and the resulting staffing strategy (employee rotation, hiring and / or redundancy).</p>		
<p>Effect:</p> <p>Different functions and reporting lines within regional / project teams may not be optimally structured to achieve goals and objectives.</p>		<p>Recommendation:</p> <p>We recommend that:</p> <ul style="list-style-type: none"> • region and project-wise organisational chart should be prepared; and • organisational charts should be timely updated to reflect any change of structure due to status of projects.
<p>Management comments:</p> <p>Organisation chart covering all the core positions has been shared. This covers the position in the core programmes/departments. However, this does not cover the positions in the project of short duration (e.g. 6 moths). For such projects list of staff mentioning their positions is available in Excel Sheet.</p>		

6.2 Financial management and internal control systems

6.2 Financial management and internal control systems

6.2.1	Date and approval not appearing on the Bank reconciliation Statements	NUPAS checklist Ref. 2.1
<p>Criteria:</p> <p>The ‘financial and procurement policy’ interalia states that:</p> <p style="padding-left: 40px;"><i>“All bank reconciliation statements should be approved by the designated personnel from Finance Department by 15th of the following month”</i> - Section 3.2.3, ‘financial and procurement policy’</p> <p style="padding-left: 40px;"><i>“Ensure that the reconciliation statement is signed by persons preparing, checking and approving the statement.”</i> - Section 3.2.13, ‘financial and procurement policy’</p> <p>Condition:</p> <p>During our review of selected bank reconciliation statements, we have observed the following:</p> <ul style="list-style-type: none"> • the preparation and review dates were not mentioned on the bank reconciliation statement; and • the standard format for bank reconciliation statement as prescribed by the manual contains fields for signature of person preparing and reviewing the statement. However, the format does not contain any field for signature of the approving authority. <p>Cause:</p> <p>Lack of understanding with regards to established policies and procedures.</p>		
<p>Effect:</p> <p>Non-compliance with ‘financial and procurement policy’ may lead to ineffective controls over banking reconciliation process.</p>		<p>Recommendation:</p> <p>We recommend that the dates of preparation, review and approval should be mentioned on the bank reconciliation statements. Further, all bank reconciliation statements should be approved by designated authorised personnel.</p>
<p>Management comments:</p> <ul style="list-style-type: none"> • Agreed. Will ensure compliance in future. • Agreed. As per the recommendation, the signature field on statement has been inserted. However, all bank reconciliation statements were thoroughly reviewed by the relevant authority, including the external auditors. 		

6.2.2	Delays in posting of transactions into the system	<i>NUPAS checklist Ref. 2.2</i>										
<p>Criteria:</p> <p>Financial information should be timely captured and recorded so that accurate and complete records are available at any given point of time.</p> <p>Condition:</p> <p>A debit note is raised for settlement of funds between regional and central offices.</p> <p>During the course of our review of intra-office fund settlements, we noted that a debit note was raised for settlement of funds with regards to purchase of laptop by central office on behalf of Gilgit office.</p> <p>However, the management at Gilgit office recorded the asset in the fixed asset module after delay of 53 days. The chronological details of the instance noted is mentioned below:</p> <table border="1" data-bbox="331 831 1485 1010" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: center;">Purchase order date</th> <th style="text-align: center;">Cheque date</th> <th style="text-align: center;">Debit note date</th> <th style="text-align: center;">Payment voucher date</th> <th style="text-align: center;">Asset recording date in fixed asset module</th> </tr> </thead> <tbody> <tr> <td style="text-align: center;">December 28, 2015</td> <td style="text-align: center;">February 4, 2016</td> <td style="text-align: center;">February 4, 2016</td> <td style="text-align: center;">February 15, 2016</td> <td style="text-align: center;">March 28, 2016</td> </tr> </tbody> </table> <p>Further, we have also noted instances at Karachi office where parked entries were not timely posted in the system.</p> <p>Cause:</p> <p>The said delay is due to:</p> <ul style="list-style-type: none"> • staff's involvement in annual audit and public holidays; and • practice of posting any parked entry during the monthly financial closing process. 			Purchase order date	Cheque date	Debit note date	Payment voucher date	Asset recording date in fixed asset module	December 28, 2015	February 4, 2016	February 4, 2016	February 15, 2016	March 28, 2016
Purchase order date	Cheque date	Debit note date	Payment voucher date	Asset recording date in fixed asset module								
December 28, 2015	February 4, 2016	February 4, 2016	February 15, 2016	March 28, 2016								
<p>Effect:</p> <p>The aforesaid conditions expose the entity to the following risks:</p> <ul style="list-style-type: none"> • delays in posting of entries may result in inaccurate accounting records at cut off / reporting date; and • delays in posting of parked entries reflect absence of timely review and approval of transactions. 		<p>Recommendation:</p> <p>We recommend that the management should timely record and post the transactions in the system.</p>										
<p>Management comments:</p> <p>As per International Accounting Standards (IASs), all assets (revenue of counterparty) are recorded on the basis of risk and reward transfers and other eligibility criteria mentioned in the accounting standards. In this particular case, asset was not recorded on timely basis due to the pending subsequent transfer of the asset in the region. We second your recommendation.</p>												

6.2.3	The financial and procurement policy does not cover variance analysis for projects	NUPAS checklist Ref. 2.4
<p>Criteria: Policies and procedures provide the framework within which an organisation operates and is a direct link between an organisation’s vision and its day-to-day operations.</p> <p>Condition: The ‘financial and procurement policy’ does not cover variance analysis of projects.</p> <p>Cause: The management relies on guidance provided by donor via workshops and meetings where a comprehensive manual for an individual project is not provided.</p>		
<p>Effect: In the absence of aforementioned policy, key functions and activities of the entity may not be streamlined to meet its objectives.</p>		<p>Recommendation: We recommend that the management should update the ‘financial and procurement policy’ so as to include procedures for variance analysis of projects.</p>
<p>Management comments: The recommendation has been already been accounted for in the revised policy document – as one of the initiatives in upcoming incorporation of new entity, Aga Khan Agency for Habitat.</p>		

6.2.4	The financial and procurement policy does not cover allowable and unallowable cost	NUPAS checklist Ref. 2.5
<p>Criteria:</p> <p>Policies and procedures provide the framework within which an organisation operates and is a direct link between an organisation’s vision and its day-to-day operations.</p> <p>Condition:</p> <p>The ‘financial and procurement policy’ does not cover allowable and unallowable cost for project budgeting.</p> <p>Cause:</p> <p>The management relies on guidance provided by donor via workshops and meetings where a comprehensive manual for an individual project is not provided.</p>		
<p>Effect:</p> <p>In the absence of aforementioned policies and procedures, key functions and activities of the entity may not be streamlined to meet its objectives.</p>		<p>Recommendation:</p> <p>We recommend that the management should prepare a checklist for each project to document the donor guidance on allowable and unallowable costs.</p> <p>Further, the ‘financial and procurement policy’ should be updated to include a clause for preparation of the said checklist.</p>
<p>Management comments:</p> <p>The recommendation has been already been accounted for in the revised policy document – as one of the initiatives in upcoming incorporation of new entity, Aga Khan Agency for Habitat.</p>		

6.2.5	Non-compliance of ‘financial and procurement policy’ with regards to petty cash	<i>NUPAS checklist Ref.</i> 2.7																																												
<p>Criteria:</p> <p>The ‘financial and procurement policy’ states that: <i>“5.1 Upon consumption of one third PCF balance or at the end of the month whichever is earlier, the custodian should:</i> 6.2.1 <i>fill the ‘Petty cash replenishment form’ completely;</i> 6.2.2 <i>attach all ‘Petty cash payment vouchers’ (along with supports) with the ‘Reimbursement Claim Form’,</i> 6.2.3 <i>attach copy of all outstanding ‘Petty Cash Advance Request Form’ (IOUs) with the ‘Reimbursement Claim Form’;</i> 6.2.4 <i>have the ‘Reimbursement Claim Form’ checked by the Supervisor and approved as per the Department’s Authority Matrix.</i> 6.2.5 <i>send the entire set to Finance department for further processing;</i> 6.2.6 <i>It should be kept in mind that the reimbursement of funds would require about 5 working days after the disbursement statement is received in the Finance office.”</i></p> <p>Condition:</p> <p>However, we have noted the following conditions at Gilgit office:</p> <ul style="list-style-type: none"> the management does not have a practice of preparing reimbursement claim form to process petty cash replenishment; and instances were noted where the cash in hand was less than the threshold of Rs 26,667 at the time of replenishment. The details of such instances are set forth below: <table border="1" data-bbox="379 1081 1457 1603"> <thead> <tr> <th>Month</th> <th>Petty cash limit</th> <th>Cash in hand at the time of replenishment (In Rs)</th> <th>Cash obtained as replenishment</th> </tr> </thead> <tbody> <tr> <td>January 2015</td> <td>40,000</td> <td>78</td> <td>39,922</td> </tr> <tr> <td>February 2015</td> <td>40,000</td> <td>-</td> <td>40,000</td> </tr> <tr> <td rowspan="2">March 2015</td> <td>40,000</td> <td>4,050</td> <td>35,950</td> </tr> <tr> <td>40,000</td> <td>3,513</td> <td>36,487</td> </tr> <tr> <td rowspan="2">April 2015</td> <td>40,000</td> <td>1,438</td> <td>38,562</td> </tr> <tr> <td>40,000</td> <td>649</td> <td>39,351</td> </tr> <tr> <td rowspan="2">May 2015</td> <td>40,000</td> <td>3,044</td> <td>36,956</td> </tr> <tr> <td>40,000</td> <td>430</td> <td>39,570</td> </tr> <tr> <td rowspan="2">June 2015</td> <td>40,000</td> <td>3,680</td> <td>36,320</td> </tr> <tr> <td>40,000</td> <td>5,418</td> <td>34,582</td> </tr> <tr> <td>December 2015</td> <td>40,000</td> <td>3,151</td> <td>36,849</td> </tr> </tbody> </table> <p>Cause:</p> <p>Lack of understanding by the management with regards to established policies and procedures.</p>			Month	Petty cash limit	Cash in hand at the time of replenishment (In Rs)	Cash obtained as replenishment	January 2015	40,000	78	39,922	February 2015	40,000	-	40,000	March 2015	40,000	4,050	35,950	40,000	3,513	36,487	April 2015	40,000	1,438	38,562	40,000	649	39,351	May 2015	40,000	3,044	36,956	40,000	430	39,570	June 2015	40,000	3,680	36,320	40,000	5,418	34,582	December 2015	40,000	3,151	36,849
Month	Petty cash limit	Cash in hand at the time of replenishment (In Rs)	Cash obtained as replenishment																																											
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April 2015	40,000	1,438	38,562																																											
	40,000	649	39,351																																											
May 2015	40,000	3,044	36,956																																											
	40,000	430	39,570																																											
June 2015	40,000	3,680	36,320																																											
	40,000	5,418	34,582																																											
December 2015	40,000	3,151	36,849																																											
<p>Effect:</p> <p>Non-compliance with ‘financial and procurement policy’ may lead to ineffective controls over petty cash management.</p>		<p>Recommendation:</p> <p>We recommend that the ‘financial and procurement policy’ should be complied with.</p>																																												
<p>Management comments:</p> <p>We will ensure hundred percent compliance in future.</p>																																														

6.2.6	Absence of policies and procedures in respect of record retention and Information Technology	NUPAS checklist Ref. 2.9
<p>Criteria:</p> <p>Policies and procedures provide the framework within which an organisation operates and is a direct link between an organisation’s vision and its day-to-day operations.</p> <p>Condition:</p> <p>We have noted that policies and procedures have not been designed for the following key areas:</p> <ul style="list-style-type: none"> • record retention; and • information technology including disaster recovery and backup. <p>Cause:</p> <p>Lack of understanding by the management with regards to the significance of the aforesaid key areas.</p>		
<p>Effect:</p> <p>In the absence of aforementioned policies and procedures, key functions and activities of the entity may not be streamlined to meet its objectives.</p>		<p>Recommendation:</p> <p>We recommend that the management should formulate policies with regards to record retention and information technology.</p>
<p>Management comments:</p> <p>These recommendations have already been accounted for in the revised policy document – as one of the initiatives in upcoming incorporation of new entity, Aga Khan Agency for Habitat.</p>		

6.2.7	Absence of practice with regards to preparation of monthly financial statements	NUPAS checklist Ref. 2.11
<p>Criteria: Preparation and review of monthly financial statements enables strong oversight over financial affairs and position of the entity.</p> <p>Condition: The management does not have a practice of preparing monthly financial statement for internal reporting purposes.</p> <p>Cause: Lack of understanding by the management relating to benefits from monthly financial statements.</p>		
<p>Effect: The management may not be able to identify potential problems linked with financial affairs and position of the entity.</p>		<p>Recommendation: We recommend that the management should prepare monthly financial statements.</p>
<p>Management comments: For internal purposes, financial statements of all the projects are developed on quarterly basis. Apart from these reports monthly reports are also developed if there is a donor requirement, e. g USAID funded WHIP Project. (Such reports have already been submitted to USAID). Monthly financial reports are also developed depending on the need of the project manager.</p>		

6.2.8	Functioning of Internal Audit department	NUPAS checklist Ref. 2.12
<p>Criteria:</p> <p>The attribute standards established by Institute of Internal Auditors (IIA) interalia states:</p> <p><i>2010.A1- The internal audit activity's plan of engagements must be based on a documented risk assessment, undertaken at least annually. The input of senior management and the board must be considered in this process.</i></p> <p><i>2030 - Resource Management: The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.</i></p> <p>Condition:</p> <p>The internal audit department performs fieldwork in accordance with the Internal Audit plan approved in the Audit Committee meeting.</p> <p>We have noted the following deviations from best practices with regards to the Internal Audit (IA) function established at the entity:</p> <ul style="list-style-type: none"> • the IA plan provided to us did not mention the indicative timeline for internal audit work. • a formal risk assessment exercise was not conducted to assess inherent risk and strength of control environment in determining the auditable units to be included in the internal audit plan. Hence we were not able to ascertain the justification for the 19 audit units covered in the IA plan for the year 2016 while only 8 audit units covered in the IA plan for the year 2015; and • the responses from management on the IA findings do not include the responsible authority and the due date for implementation of action plan. <p>Cause:</p> <p>Lack of attention to improve capacity of IA function.</p>		
<p>Effect:</p> <p>Effectiveness of internal audit function may be compromised.</p>		<p>Recommendation:</p> <p>We recommend that the internal audit department should address the conditions noted keeping in view the best practices.</p> <p>Further, management should invest in capacity building of its employee base to ensure effective functioning of all departments.</p>
<p>Management comments:</p> <p>The internal audit has an approved charter – basis for conducting all internal audits, including the work scope and timelines/plans. Over time, the capacity and scope of the audit department has been strengthened considerably – a continuous process to be followed in future as well.</p>		

6.3 Procurement systems

6.3 Procurement systems

6.3.1	<i>The financial and procurement policy does not cover dispute resolution and claims made by vendor.</i>	NUPAS checklist Ref. 3.1
<p>Criteria:</p> <p>Policies and procedures provide the framework within which an organisation operates and is a direct link between an organisation’s vision and its day-to-day operations.</p> <p>Condition:</p> <p>We have noted that the ‘financial and procurement policy’ does not cover dispute resolution measures with vendors.</p> <p>Cause:</p> <p>Lack of understanding with regards to the significance of dispute resolution.</p>		
<p>Effect:</p> <p>In the absence of aforementioned policy and procedures, key functions and activities of the entity may not be streamlined to meet its objectives.</p>		<p>Recommendation:</p> <p>We recommend that the management should update the ‘financial and procurement policy’ so as to cover dispute resolution measures.</p>
<p>Management comments:</p> <p>These all recommendations have already been accounted for in the revised policy document – as one of the initiatives in upcoming incorporation of new entity, Aga Khan Agency for Habitat.</p>		

6.3.2	Weak controls over review of payments to vendors.	<i>NUPAS checklist Ref.</i> <i>3.2</i>
<p>Criteria:</p> <p>Section 1.1 of Financial and procurement policy interalia states:</p> <p style="padding-left: 40px;"><i>“Authority levels must be vested high enough in the organization such that effective review take place and disapproval of improper or undesirable decisions or transaction must be reasonably assured.”</i></p> <p>Condition:</p> <p>During the course of our review at Gilgit office, we observed that payments were made to Rescue Security Service (Private) Limited for the months of December 2015, January and February 2016, however, the invoices received for the aforementioned 3 months were photocopies of the invoice issued in November 2015, bearing the same invoice number and invoice date.</p> <p>Cause:</p> <p>Ineffective coordination between the management and vendor.</p>		
<p>Effect:</p> <p>The said condition may cast doubt over effectiveness of management’s controls with regards to timely identification and prevention of payments against unauthentic invoices.</p>		<p>Recommendation:</p> <p>We recommend that the management should properly review the supporting documentation to ensure payments are only made against authentic invoices.</p>
<p>Management comments:</p> <p>The Financial and Procurement policy of the Institution is strictly adhered to at all times, that include all supporting documentation and authentic invoices. In this particular one off case, the vendor used to provide the photocopy of the invoice in our Gilgit office, with original one subsequently submitted to our finance department through their Karachi office. We used to oblige due to the nature of services offered in a risk prone region. From now on, the payments are and will only be processed upon receiving their original invoice from vendor’s head office.</p>		

6.3.3	Absence of a formal tenancy agreement for use of office premises	NUPAS checklist Ref. 3.2
<p>Criteria: A formal agreement with vendor determines rights and obligations of parties in order to deliver the agreed performance objectives.</p> <p>Condition: We have observed that the entity has not entered into formal agreement with the landlord with respect to the tenancy of plot situated near helicopter chowk, Jutial, Gilgit for its office premises.</p> <p>Cause: Lack of follow-up by the management with regards to tenancy agreement with landlord.</p>		
<p>Effect: In the absence of a formal agreement, the entity may not be able to exercise legal rights in case of disputes.</p>		<p>Recommendation: We recommend that the entity should make arrangements to enter into a formal contract with the landlord for use of the aforementioned office premises.</p>
<p>Management comments: The agreement was signed originally in the landlord’s presence. Subsequently, he has been out of town whereby agreements have been made with him verbally and via emails. All payments have been made via cross cheque and deposited in his designated bank account to ensure compliance and security of the transaction. Further, he has been told to either get the formal written agreement signed via courier or authorize someone to do this on his behalf in future.</p>		

6.4 Human resource systems

6.4 Human resource systems

6.4.1	Hired employee did not meet the required qualification criteria	NUPAS checklist Ref. 4.1
<p>Criteria:</p> <p>The job description form and the job advertisement available in the personnel file of Assistant Inventory Officer defined the following requirements for the position:</p> <p style="text-align: center;"><i>“The ideal candidate should be a commerce graduate with 2-3 years’ experience in inventory management.”</i></p> <p>Condition:</p> <p>We have noted that the candidate hired for the said position at Gilgit office on July 1, 2015 held certificates in short term courses and diploma in Information Technology; however, the personal file of the candidate did not contain any document supporting the required graduate qualification.</p> <p>Cause:</p> <p>Lack of management’s initiative to ensure completeness of personal files in all respects and applying alternate methods of employee information verification.</p>		
<p>Effect:</p> <p>The management may not be recruiting staff with ideal skill set to discharge the duties of the position.</p>		<p>Recommendation:</p> <p>The management should ensure that only the candidates who meet the job specifications for the position in terms of qualification and experience; and apply alternative methods to check personal information of employees.</p>
<p>Management comments:</p> <p>Preference is always given to the graduates as per job specifications and hiring criteria. The candidate in this case had misplaced his certificate, providing us with the receipt of re-application from the concerned authority – document available in his personnel file.</p> <p>On a separate note, as there are some cases of the preferred candidates’ offer withdrawals at the last moment, the next best available alternative is always selected. We always ensure that the personnel files are updated with such information.</p>		

6.4.2	Incomplete records in personal file maintained by HR department	NUPAS checklist Ref. 4.1
<p>Criteria:</p> <p>An up-to-date and complete personal file documents the history and status of the entire employment relationship with an individual employee thus allowing effective decision making with regards to employee selection, promotion, training needs and discipline.</p> <p>Condition:</p> <p>During our review of selected employee personal files, we have noted following conditions:</p> <ul style="list-style-type: none"> instances were noted where the job description form was not completed in respect of authorisation of approving authority and the date of such approval; instances were noted where the employee requisition forms were either missing from the personal files or were incomplete; and certain educational certificates were missing from the personal file of the Head of the Accounting Department. <p>Cause:</p> <p>The aforesaid conditions are due to lack of effective coordination between regional office; and absence of centralised maintenance of HR records.</p>		
<p>Effect:</p> <p>In the absence of maintaining complete documentation in the personal files, there is lack of documentary evidence to ascertain compliance with the HR policies and procedures.</p>		<p>Recommendation:</p> <p>We recommend that complete records should be maintained in the personal files. Further, the entity should maintain centralised HR records at its head office.</p>
<p>Management comments:</p> <ul style="list-style-type: none"> Point 1&2 noted and will be rectified. Record has now been updated as per requirements. 		

6.4.3	Periodic review of HR manual to incorporate changes in practice not carried out		<i>NUPAS checklist Ref. 4.1</i>
<p>Criteria: As per the best practices, policies and procedures should be atleast annually reviewed for changes in practice.</p> <p>Condition: We have observed that a memorandum dated January 1, 2014 was issued to revise the entitlement limit for Medical Outpatient benefit of employees. However, the said change was not incorporated in the relevant HR policy since then.</p> <p>Cause: Absence of practice to periodically review the HR manual.</p>			
<p>Effect: It cannot be ensured that policies documented in the HR manual are up to date.</p>		<p>Recommendation: We recommend that the management should periodically review the policies and procedures documented in the manual and update the same with regards to changes.</p>	
<p>Management comments: Revision in medical allowance has been communicated to all staff via internal memorandum. Since organisation is going through major structural improvements, revised/enhanced HR policy manual will be implemented by the mid of this year.</p>			

6.4.4	Absence of documented policy on compensation.	<p>NUPAS checklist Ref. 4.3</p>
<p>Criteria: Policies and procedures provide the framework within which an organisation operates and is a direct link between an organisation’s vision and its day-to-day operations.</p> <p>Condition: We have noted that the HR manual does not cover compensation plan.</p> <p>Cause: Deficiency in established policy and procedures.</p>		
<p>Effect: In the absence of aforementioned policy, key functions and activities of the entity may not be streamlined to meet its objectives.</p>		<p>Recommendation: We recommend that the management should formulate policy with regards to compensation plan.</p>
<p>Management comments: The recommendation has already been accounted for in the revised policy document – as one of the initiatives in upcoming incorporation of new entity, Aga Khan Agency for Habitat.</p>		

6.5 Project performance management

6.5 Project performance management

6.5.1	<i>Inability to meet the completion deadline agreed in the contract</i>	NUPAS checklist Ref. 5.2
<p>Criteria:</p> <p>The entity has entered into a contract with Aga Khan Education Service for construction of six class rooms at Community based School (CBS) Sujawal, Sindh. The said contract includes the following clause:</p> <p style="text-align: center;"><i>“The assignment will be completed in all respects by September 30, 2015”</i></p> <p>Condition:</p> <p>However, the project’s progress report dated February 29, 2016 revealed that the project is only 75% complete with an expected completion date of April 15, 2016; hence leading to a delay of more than 6 months from the agreed completion date as per contract.</p> <p>Cause:</p> <p>The progress report cites the following reasons for the delay:</p> <ul style="list-style-type: none"> • Interference by local activists; • Losing of contractor’s mixer machine at project site; and • Certain additional work as per consultant’s advice. 		
<p>Effect:</p> <p>Failure to meet the agreed deadlines for projects may expose the entity to the risk of penalty / fine being levied upon the entity and may adversely affect entity’s reputation.</p>		<p>Recommendation:</p> <p>We recommend that steps should be taken to ensure that the projects are completed by the date agreed in the contract.</p>
<p>Management comments:</p> <p>AKPBS,P has been successfully providing construction management and execution services to AKDN institutions since inception. These projects are designed to maintain up-to-date engineering and architectural standards and ensure seismic resistance, proper lighting and ventilation. Over 1.2 million square feet of construction have been completed, with 25 large-scale institutional buildings, over 1,000 schoolrooms and 50 health facilities in over 200 villages. School facilities have been completed in Tajikistan and Kyrgyzstan while the Bamyan Provincial Hospital is currently under construction in Afghanistan.</p> <p>Considering the nature and remote locations of our activities, cost escalations in construction and its susceptibility to the general economic / political / legal and regulatory environment, there are some uncontrollable factors and circumstances that results in delays, such as contractor underperformance – prime factor in this case. Nevertheless, the client / our partner is always taken on board in such instances, with mutual agreement through revisions in out Memorandum of Understanding (MOUs).</p>		

6.6 Organisational sustainability

6.6 Organisational sustainability

6.6.1	Internal Audit Department needs to be strengthened	NUPAS checklist Ref. 6.1
<p>Criteria:</p> <p>The attribute standards established by Institute of Internal Auditors (IIA) interalia states:</p> <p><i>2030 - Resource Management: The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.</i></p> <p>Condition:</p> <p>The entire IA department consists of two persons including the Chief Audit Executive who are entrusted with checking the design and operating effectiveness of controls implemented on projects at all regions.</p> <p>Cause:</p> <p>The aforesaid condition is due to staff turnover.</p>		
<p>Effect:</p> <p>Effectiveness of internal audit function may be compromised.</p>		<p>Recommendation:</p> <p>We recommend that the management should invest in capacity building via trainings for development of advocacy skills, training/speaking abilities, technical skills of its employees to ensure effective functioning of all departments.</p>
<p>Management comments:</p> <p>The internal audit has an approved charter – basis for conducting all internal audits, including the work scope and timelines/plans. Over time, the capacity and scope of the audit department has been strengthened considerably – a continuous process to be followed in future as well.</p>		

6.6.2	Absence of documented policy and procedures with regards to preparation of cashflow forecast for projects.	NUPAS checklist Ref. 6.2
<p>Criteria:</p> <p>Policies and procedures provide the framework within which an organisation operates and is a direct link between an organisation’s vision and its day-to-day operations.</p> <p>Condition:</p> <p>We have noted that the established policy and procedures do not cover preparation of cashflow forecast for projects.</p> <p>Cause:</p> <p>The management only prepares cash flow forecast for a project in an event where the donor for the project specifically stipulates such a requirement or where the project is deemed material.</p>		
<p>Effect:</p> <p>In the absence of aforementioned policies and procedures, key functions and activities of the entity may not be streamlined to meet its objectives.</p>		<p>Recommendation:</p> <p>We recommend that the management should: update the ‘financial and procurement policy’ to include:</p> <ul style="list-style-type: none"> • guidance on preparation of cashflow forecast for projects; and • threshold for materiality of a project above which cash forecast shall be prepared
<p>Management comments:</p> <p>The recommendations have been already been accounted for in the revised policy document – as one of the initiatives in upcoming incorporation of new entity, Aga Khan Agency for Habitat.</p>		

7. Conclusion

Overview

The purpose of this analysis is to assess the current managerial capacity and the future expected capacity keeping in view the pathway of managerial development, in handling the fiduciary risks including those that affect the capability to manage advance funding mechanism. In this regard, we have analysed how operational capability and performance could better align the organisation in delivering value to stakeholders in accordance with their expectations.

Expectations of stakeholders

In order to assess the current management capacity of entity, it is important to understand the expectations of the key stakeholders of the water and hygiene improvement program and the extent to which the current managerial capability would be able to meet the expectations.

Donors (USAID)

- The control structures being the foundation of financial management system must be sufficiently robust to minimize the fiduciary risks associated with the use of donor funds at the current levels.
- Managerial ability to administer cash flow planning to minimize fiduciary risks.
- Completion of the project with all the envisioned objectives to be met on a timely basis.

Society

The society expects from the organisation to create an enabling environment for the people of rural areas of Pakistan through the provision of clean and safe drinking water and health and hygiene education.



Operational capability

Capacity building of departments

Considering the fact that the entity is currently engaged in more than 40 projects, there is an inadequate number of staff for the internal audit to cover each of these projects located at different regions. Consequently, the objective of internal audit to evaluate and improve the effectiveness of risk management, control, and governance processes may be compromised. In response to this threat, the management should consider capacity building of internal audit function or alternatively hire and train new staff, to enable effective risk management.

Revisit the policies and procedures

Since the entity’s staff is on contractual basis, the entity should be vary of potential risk exposure from resignation of key personnel. In this regard, the management should revisit the established Standard operating procedures / policies and ensure that documented procedures are available to assist any potential new staff particularly with regards to project budgeting and cashflow forecasting.

Performance

Developing foresight for improved financial management

As is the case with other donors, USAID should stipulate certain reporting requirements for monitoring of project specific funds and proper oversight of the project. These reporting requirements should not be limited to periodic financial report and progress report but should also extend to preparation and monitoring of annual cash forecast setting out monthly cash inflow and outflow to offer useful foresight to the management. Further, monthly reports should be prepared for monitoring against the said cashflow forecast to enable better understanding of uncertainties and strategies to counter the same, all of which may increase confidence in achieving goals and objectives.

Stakeholder value alignment

The NUPAS checklist was used for the purpose of our assessment and to determine whether the entity has sufficient financial and managerial capacity to manage donor funds. The average rating of 3.57 suggests that the entity has more than adequate capacity to manage the funds in accordance with requirements. Further, advance funding mechanism is already a popular choice for several other donors engaged with the entity and a mechanism with which the entity’s management is thoroughly familiar. However, the deficiencies noted in section 6 of this report together with potential capacity building opportunities as above, should be addressed for improved alignment with stakeholder expectations.

The table below summarises the average score for areas covered by the NUPAS checklist:

Areas	Average Score
Legal structure	3.80
Financial management and internal controls systems	3.44
Procurement systems	3.67
Human resources system	3.50
Project performance management	4.00
Organisational sustainability	3.00
Average	3.57



For our fiduciary risk assessment of organizational, management, accounting, internal controls, financial management systems and quality assurance capabilities at AKP BSP, we acknowledge the management's cooperation for assisting the team throughout the assignment for scheduling the meetings and arrangement of documents. We appreciate the management's extended efforts for assisting the team from understanding of the entity practices to initiating approvals for access to documents.

Annexure / Appendix