INTERNAL AUDIT REPORT

TREASURY - RELEASE OF CASH PAYMENTS ('VALUE EXITS')

November 2015

Gavi
The Vaccine Alliance

Summary

Conclusion

Our audit procedures were designed to provide assurance to management and the Gavi Board about the design and operating effectiveness of the key controls in the release of cash payments ('value exits').

Through our audit procedures, we have confirmed that the risks associated with release of cash payments are well understood and are being effectively managed. The internal controls are robust and well enforced. We have identified one area where there is potential improvement opportunity in operational efficiency/effectiveness.

Internal Audit Issue Summary

Issue Description	Rating	Ref	Page
Maintenance of Average Monthly Balances in Excess of Collateral Requirements for Foreign Exchange Hedges & Not Investing the Collateral in Short term Instruments.	L	2015-03.01	3

Summary Performance Ratings on Areas Reviewed

For ease of follow up and to enable management to focus effectively in addressing the issues in our report, we have classified the issues arising from our review in order of significance: High, Medium and Low.
In ranking the issues between 'High', 'Medium' and 'Low', we have considered the relative importance of each matter, taken in the context of both quantitative and qualitative factors, such as relative magnitude, the nature and effect on the subject matter. This is in accordance with the Committee of Sponsoring Organisations of the Treadway Committee (COSO) guidance and the Institute of Internal Auditors standards.

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

Contents & Distribution

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Distribution

Title
Managing Director, Finance and Operations
Senior Director, Finance and Chief Accounting Officer
Senior Manager Treasury

For Information

Title
Chief Executive Officer
Deputy Chief Executive Officer
Managing Director, Audit & Investigations
Executive Team
Head Risk

Summary of Findings

Audit Objective

Our audit assessed the design and operating effectiveness of the key internal controls in the processes related to release of cash payments ('value exits').

Audit Scope and Approach

We adopted a risk-based audit approach informed by our assessment of the system of accounting and internal controls and tested where necessary a sample of cash payments released through the e-banking portals to validate the proper operation of these controls.

This audit was designed to assess the:

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

The scope of this audit covered treasury activities from 1 January 2014 to 30 June 2015. In particular, the audit covered the following key processes:

- Release of cash payments (funds transfers) for vaccines programme, investment cases, cash payments to partner countries, business plan expenses and internal funds transfer;
- Maintenance of third party bank information of partner countries and vendors in AX2012;
- Treasury reconciliations;
- Signatory authority and limits;
- Bank change requests and ;
- Contingency planning.

Background

The Treasury function contributes to Gavi's mission by optimising the use of funds raised through financial management of programme grants and active management of business plan expenditure. Gavi's annual forecast for programmes (vaccines and cash) expenditure is 87% and business plan (Secretariat and Partners) expenditure is 13%. The total outflow from 1 January 2014 to 30 June 2015 was $2.32 billion.

Payments are initiated in Microsoft Dynamics Axapta 2012 and transfer of funds effected in e-banking portals of Gavi's bankers. Once approval for the transfer of funds has been received, the Senior Manager Treasury initiates the transfer of funds through the e-banking portals upon validating all supporting documentation after which the second authorised signatory releases the payment. Approximately 3348 transfers were made between January 2014 and June 2015.

Conclusion

Our audit procedures were designed to provide assurance to management and the Gavi Board about the design and operating effectiveness of key controls in the operational processes related to release of cash payments ('value exits').

In the course of the audit, we reviewed operating account balances, bank rights reviews, bank access reports, signatory and viewing rights, funds transfers, changes to the master data of vendors bank details, treasury reconciliations, signatory authority and limits.

Through our audit procedures, we have confirmed that the risks associated with the release of cash payments ('value exits') are well understood and are being effectively managed. We have identified one low risk area where there is potential improvement opportunity in operational efficiency/effectiveness.

Summary of Issues Arising

Our audit identified one low rated issue. A summary of the issue identified along with the agreed management action is provided below.

Maintenance of Average Monthly Balances in Excess of Collateral Requirements for Foreign Exchange Hedges & Not Investing the Collateral in Short term Instruments.

According to section 1.7 of GAVI Accounting Procedures on operating account balances, "aggregate average monthly non-interest balances for all disbursement accounts should be kept below US $ 1 Million. Non-interest

Summary of Findings

bearing bank accounts are normally used for GAVI's short term disbursements.
However, the Treasury Manager may maintain balances above the US $ 1 Million to meet specific needs of the business such as collateral for forex hedges".

Through our audit procedures we established that Gavi maintained a total average monthly balance of US$73.7 Million in non-interest bearing bank accounts (US $ 24.2 Million and US $ 49.4 Million in the US $ and Euro operating accounts respectively) from January 2015 to June 2015. During the same period, Gavi had foreign exchange hedges of US$ 196-623 Million and was required to maintain collateral of between US $ 15 and US $ 40 Million. However, the average aggregate monthly balance in these bank accounts was in excess of the collateral requirements by an average of US $ 34-70 Million over the same period.

In addition, management had the option to invest the collateral in short term instruments such as the money market funds but did not (the collateral maintained with two other banks was invested in a short term money market fund).

In 2014, Gavi maintained aggregate average monthly balances for the two accounts of US $40.4 Million and US $41.2 Million respectively. There were no foreign exchange hedges with the main bankers in 2014 (average interest earned on the US $ account was 0.3% while on the Euro account was 0.1%).

Other issues identified were considered to be very low risk, below a threshold for reporting and have been communicated to management. A detailed analysis of the issue raised above has been provided to those responsible for implementing the recommended actions and can be provided on request.

We will continue to work with management to ensure that the audit issue is adequately addressed and the required actions are undertaken.

We take this opportunity to thank the Finance team for their assistance during this audit.

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Chrysantus Nyongesa,
Head of Internal Audit

Appendix 1: Detailed Finding and Recommendation

Issue No.	Issue Rating	Issue Description	Risk/Implication	Recommended Actions	Management Comments	ET Member/ Action Owner	Target Completion Date	Status
2015-03.01	Low	**Maintenance of Average Monthly Balances in Excess of Collateral Requirements for Foreign Exchange Hedges & Failure to Invest the Collateral in Short term Instruments**		It is recommended that Management:		**MD, Fin & Ops**	30 June 2016	Open
		According to section 1.7 of GAVI Accounting Procedures on operating account balances, "aggregate average monthly non-interest balances for all disbursement accounts should be kept below US $ 1 Million. Non-interest bearing bank accounts are normally used for GAVI's short term disbursements. However, the Treasury Manager may maintain balances above the US $ 1 Million to meet specific needs of the business such as collateral for forex hedges". 1. Through our audit testing, we established that between January 2015 and June 2015, GAVI maintained a total average monthly balance of US$73.7 Million in non-interest bearing bank accounts. The US $ and Euro operating accounts at the main bankers had aggregate average monthly balances of US $ 24.2 Million and US $ 49.5 Million respectively from January 2015 to June 2015. During the same period, Gavi had aggregate foreign exchange hedges of between US $ 196.2 Million and US$ 623 Million with collateral requirements of between US $ 15 and US $ 40 Million respectively as illustrated in table 1 and 2 below. This implies that the average aggregate monthly balance in these bank accounts was in excess of the collateral requirements by an average of US $ 34-70 Million over the same period. 2. In addition, management had the option to invest the collateral in short term instruments such as the money market fund but did not (note that collateral of US$61 Million with two different banks for foreign exchange hedges was invested in short term Money Market Fund and earned interest).	1. GAVI is incurring an opportunity cost in the form of interest foregone as a result of maintaining balances in excess of collateral requirements in non-interest bearing accounts. 2. GAVI is likely to be charged negative interest on deposits that exceed the deposit limit set by the bank.	1. Invests in short term instruments such as money market funds any amounts that are in excess of collateral requirements. In addition, management should invest the collateral in short term instruments such as the money market funds	Gavi looks to mitigate its foreign exchange currency exposure by entering into forward contracts and options with banks that meet the necessary criteria as determined by the Board-approved policies on currency hedging. All banks require that collateral is posted against these currency forward contracts. With the level of non-USD being received at Gavi having increased significantly over the past couple of years, Gavi was faced in 2015 with one bank having to hold a larger amount in collateral non-interest bearing accounts (due to changes in market interest rates) than was foreseen when the Investment Policy was adopted. In seeking to address this issue, the Gavi Secretariat has worked with the relevant bank to put in place arrangements that allow interest to be credited to Gavi on monies held on collateralised deposits. This became effective on 1	Senior Director, Finance & Chief Accounting Officer Treasury Manager		

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<tr><th>Issue No.</th><th>Issue Rating</th><th>Issue Description</th><th>Risk/Implication</th><th>Recommended Actions</th><th>Management Comments</th><th>ET Member/ Action Owner</th><th>Target Completion Date</th><th>Status</th></tr>
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Table 1 shows the average (Av.) balances of the US $ and EUR* accounts and the required collateral balance for Foreign Exchange (FX) hedge.
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<tr><th>Month</th><th>Jan</th><th>Feb</th><th>Mar</th><th>Apr</th><th>May</th><th>June</th><th>Av.</th></tr>
<tr><td>Collateral (US$ M)</td><td>15</td><td>15</td><td>15</td><td>20</td><td>20</td><td>40</td><td>20.8</td></tr>
<tr><td>Total – Acc.</td><td>62</td><td>71</td><td>49</td><td>72</td><td>78</td><td>110</td><td>73.7</td></tr>
<tr><td>Excess</td><td>47</td><td>56</td><td>34</td><td>52</td><td>58</td><td>70</td><td>52.9</td></tr>
<tr><td>Acc. bal.- 6860L(US$ M)</td><td>13</td><td>23</td><td>3</td><td>25</td><td>31</td><td>50</td><td>24.2</td></tr>
<tr><td>Acc. bal.- 6870D*(US$ M)</td><td>49</td><td>48</td><td>46</td><td>47</td><td>47</td><td>60</td><td>49.5</td></tr>
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(*) The figure is from the Bank Account Values Report from Treasury, converted from EUR to USD using the monthly historical exchange rate sourced from OANDA.
Table 2 shows the required collateral and the cumulative foreign exchange hedges between January and June 2015
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<tr><th>Month</th><th>Jan</th><th>Feb</th><th>Mar</th><th>Apr</th><th>May</th><th>June</th></tr>
<tr><td>Collateral (US$ M)</td><td>15</td><td>15</td><td>15</td><td>20</td><td>20</td><td>40</td></tr>
<tr><td>FX Hedges</td><td></td><td>196.2</td><td></td><td>258.9</td><td>320.9</td><td>623</td></tr>
</table>
In 2014, the aggregate average monthly balance for the two operating accounts was US $ 40.1 Million and US $41.2 Million respectively and there was no foreign exchange hedge. However during this period, the two accounts earned average interest of 0.3% and 0.1% respectively.
</td><td></td><td></td><td>January 2016. The new arrangement with the bank means that Gavi will be within the limit of cash held set by the Investment Policy. The Gavi Secretariat is also exploring other options to reduce the need to deposit collateral with this bank, such as the establishment of an International Swaps and Derivatives Agreement which is already in place with other banks that Gavi works with.</td><td></td><td></td><td></td></tr>
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