



ADAPTATION FUND

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Ethics and Finance Committee  
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Agenda Item 4

## **STREAMLINED ACCREDITATION PROCESS**

## **Background**

1. At its twenty-third meeting held 20-21 March 2014, the Adaptation Fund Board decided to continue its consideration of approval for accreditation of Small National Implementing Entities (SNIEs or applicants) on the basis of a “Streamlined Accreditation Process” (Decision B.23/17). This process would entail no changes to the fiduciary standards, but it would institute appropriate mitigating measures and controls needed for SNIEs to demonstrate their required competencies. Specifically, the mitigating measures and controls would reflect the institution’s characteristics. As a result, the Accreditation Panel (Panel) could specifically recommend to the Board that the SNIE be accredited to manage projects with conditions, if needed, that reflect the type of entity, its size and risk profile.

2. The proposed process is based on the update from the Panel based on its experience gained in operationalizing the Streamlined Accreditation Process and on advising two SNIEs on viable alternatives to address the requirements of the fiduciary standards as written in Annex II of the Panel’s 17<sup>th</sup> Report to the Board (AFB/B.24/4). The Board in Decision (B.24/22) encouraged the Panel to:

- (a) Finalize its work on the two cases considered applicable for a streamlined approach; and
- (b) Present a standardized streamlined accreditation process for SNIEs for consideration by the Board at its 25th meeting.

3. The following document presents a proposed streamlined accreditation process for SNIEs as it relates to the fiduciary standards. As the above decision indicates there were two case studies to test the streamlined process, but one entity put all the requirements of the fiduciary standards in place and no longer needs to be considered under the streamlined approach. The second case is being recommended for accreditation under the streamlined approach through the Accreditation Panel’s 18<sup>th</sup> (AP18) report to the Board (AFB/25/4). The AP18 report includes an annex with a summary of how the entity meets the requirements through the streamlined process for small entities.

4. Under the streamlined process there would be no mitigating controls for the environmental and social standards.

## **The streamlined accreditation process**

5. The Panel together with the secretariat are proposing a streamlined accreditation process to assess accreditation applications of smaller entities. It takes into consideration compensating measures, controls, and practices normally found in smaller entities to determine whether or not an entity meets the fiduciary requirements without exposing the Fund to significant additional risks.

6. The process is based on the following five areas:
- (a) An assessment of the potential risks that the Adaptation Fund would take by funding a project based on the capacity and nature of an SNIE,
  - (b) A greater emphasis on identifying alternate ways to meet the requirements of the fiduciary standards,
  - (c) Added flexibility for an applicant to show how it uses mitigating measures to meet the spirit of the fiduciary standards,
  - (d) Reduced time and effort for the applicants to go through the accreditation process, and
  - (e) Alignment where possible with the fit-for-purpose approach of the Green Climate Fund

7. It should be noted that the proposed streamlined process entails no changes to the fiduciary standards but instead opens up possibilities for a smaller entity to demonstrate its competence and capacity to meet acceptable requirements. However, the requirements for demonstrating the fiduciary standards would be commensurate with the type, size, and risk profile of the institution.

8. The suggested approach for the accreditation process is to rely where possible on credible and independent reviews or due diligence done of the applicant. These types of reviews may well have considered many of the same areas as those covered by the accreditation application and can therefore be used when this is the case. This reliance is an opportunity to align the accreditation process further with the Paris Declaration on Development Effectiveness, the Accra Agenda for Action and subsequent development conferences.

### **Characteristic of an SNIE applicant applying under streamlined process<sup>1</sup>**

9. It is proposed to have this modality available to applicants currently executing or implementing projects up to USD 1 million per project or programme, having up to 25 professional staff working on implementing or executing projects and having annual administrative expenses of up to USD 1 million. It is important to note that the characteristics are provided to give a general parameter and are not intended to be rigidly applied. Applicants falling outside of these ranges could be considered under the streamlined approach based on other considerations such as their characteristics or type of business. From past experience some of the regional implementing entities share similar characteristics and the streamlined approach should be equally available to them.

10. There are a number of characteristics that are commonly found in SNIEs. When these are noted by the Panel; the Panel should consider the possible risk mitigating procedures that would be available such as those in the examples given below.

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<sup>1</sup> A lesson learned from the first case study is that the initial characteristics proposed by the Panel for SNIEs who are eligible for the streamlined accreditation process was too restrictive and that a better alignment with the Operational Guidelines would be useful.

- (a) Less formal internal controls than those of large entities including the possibility for management to override existing controls. The lack of formal internal controls is not an indicator of fraud or error. Nevertheless, any management override of controls is and may have a significant adverse effect on the control environment and lead to an increased risk of fraud.
- **Risk mitigation:** An active Board of Directors or another oversight body which regularly reviews day-to-day operations as well as the results from independent audits and the financial statements might contribute to mitigate this type of exposure. Full documentation of key financial and operating processes and procedures also minimizes this risk.
- (b) Limited extent to which segregation of duties in some areas is practicable due to the size of the applicant and its limited number of employees.
- **Risk mitigation:** Active management supervision of staff in day-to-day operations serves as a compensatory internal control that counters the risk associated with the limited segregation of duties.
- (c) Limited ability to withstand adverse conditions and sustain operations.
- **Risk mitigation:** The SNIE would need to demonstrate sustainability of its financing in the medium and long term before any recommendation for accreditation could be made.
- (d) Turnover of key staff or insufficient investment in staff in terms of training and exposure. A high turnover rate and staff with an inadequate ability could have a negative effect on the SNIE's sustainability, ability to deliver quality projects, etc.
- **Risk mitigation:** Although there might be external factors that contribute to the turnover, the SNIE would need to demonstrate that key positions in the organization that are necessary for delivery of grant-funded projects are fully staffed with qualified individuals on a sustainable basis.

11. An applicant can apply directly under the streamlined process however would not have to stipulate upfront that it is applying as a small entity. After an initial review by the Panel where they have analyzed areas where risk mitigation measures could be necessary for a SNIE to meet the fiduciary standards, the Panel would discuss the possibility with the applicant during the accreditation process. An applicant would need to agree to undergo the streamlined process with the understanding that (i) the process would likely take less time (ii) the upfront costs would be reduced (iii) the applicant could be accredited using its own systems (i.e. without having to make changes to meet standards intended for larger organizations); and (iv) the applicant would be accredited with a monetary limitation to the size of projects it can apply for.

12. Given the last point above, if a nominated NIE is accredited as an SNIE a country would have the option of nominating a second organization to serve as an NIE.

13. Annex I provides a flow diagram of the SNIE proposed process.

## **Conditionality**

14. As is the case under a regular accreditation an entity under the streamlined procedures is accredited for five years at which time it can apply for reaccreditation, either under the streamlined or regular reaccreditation process.

15. A condition can be placed on an accreditation if the applicant cannot meet the full requirements of the fiduciary standards due to its limited size or restrictions caused by its geographical location or ability or resources available within the country. If the applicant successfully demonstrates fulfillment of the standards but if the Panel recognizes that based on the organization's capacity and past experience the applicant can only manage limited amounts of money, then the Panel would recommend to the Board a restricted project size in terms of disbursement limits, etc. The rationale for any conditions placed on the applicant needs to be well documented by the Panel and shared with the applicant so that the applicant is informed prior to the recommendation to the Board. Any conditionality should be clearly communicated on the Adaptation Fund website listing the accredited implementing entities.

16. An entity, accredited under the streamlined approach which carries conditions, can request at any time during its accreditation to have the conditions re-evaluated by the Panel for the remainder of the five year period based on its development of policies and procedures or the additional experience acquired since the accreditation. This would avoid that conditions become fixed over a long period of time which may make it impossible to bring about a much needed adaptation project for a particular country.

## **General efficiencies introduced**

17. Based on five years of experience and having processed close to a hundred applications the Panel has identified a number of areas within the accreditation process and the application form itself that can be improved to give it greater clarity, introduce efficiencies and focus more on the applicants capacity to perform the project implementation tasks. This section explains the proposed improvements to be achieved by the streamlined approach which should facilitate the accreditation process for the applicants and shorten the time required for the accreditation process.

### *Well understood procedures and practices*

18. The streamlined approach recognizes that smaller entities do not have a full set of documents and manuals that contain all the policies and procedures. It accepts a description of implicit policies and practices provided these are commonly understood and used. An exception relates to anti-fraud procedures and the grievance mechanism for the Environmental and Social Policy because they need to be publically available to external parties. This practice reflects the approach taken by the Panel when it examined the first wave of accreditation applications for national and regional implementing entities five years ago.

*Experience as an implementing or executing entity*

19. From experience we know that donors and multilateral institutions usually work closely together with the type of applicants that would come under the streamlined process. This would relate to the areas of project identification, project appraisal, monitoring and evaluation as well as project closure. The Panel should recognize these efforts and the related capabilities that an applicant would therefore have when it is evaluating the capacity of SNIEs under the streamlined process.

*Using established project cycle management systems*

20. The type of applicants that would come under the streamlined approach are in many cases quite adept at adjusting their procedures to the requirements of their donors and multilateral institutions and they understand these procedures quite well. When implementing projects on their own without donor requirements applicants may use one of the project management cycle systems from a donor or a multilateral institution that they are familiar and make only minimal adjustments thereto. This would be acceptable from an accreditation perspective provided the applicant can demonstrate a good understanding of those procedures and show how it fits with its own characteristics. In these cases the Panel would not insist on the applicant to design its own system.

21. The next section outlines the key mitigating controls of the fiduciary standards that are proposed for the streamlined process. A summary matrix of these controls is included as Annex II.

**Mitigating controls for the streamlined process***Financial statements*

22. The fiduciary statements require that an applicant's financial statements are prepared in accordance with internationally recognized accounting standards. There are two sets of accounting standards: those for the private sector and standards for the public sector referred to as IPSAS. The latter was recently adopted by the United Nations organizations and is the basis of accounting for many county governments.

23. In smaller organizations an accounting methodology based on cash disbursements is frequently used. While such a method is not the preferred method under international accounting standards, it can be accepted provided that there is a clear indication of the rules used and provided that the external auditor agrees that such stated rules are applied. The cash accounting method may be more practical for smaller organizations and they do not lead to a risk of incorrectly accounting for any funding provided by the Fund. Neither will the cash accounting method create a risk that cash transferred would not be used for the purpose intended namely, to finance a project. Under the streamlined approach such method can be accepted.

24. For applicants that are government entities an annual expenditure statement, even if unaudited, would be permissible provided that the same figures are in the accounts of the government as a whole and it is clear that all funds allocated to an entity are accounted for. Common costs such as rent, utilities that are paid directly by the government would normally not be part of such statements and that is acceptable.

#### *External Audit*

25. The requirement to have the applicants accounts audited in accordance with recognized international auditing standards would be satisfied if an audit is done in accordance with national auditing standards. This modification means that the auditor can use the rules set out in their national legislation and language. This would be applicable to the streamlined and the regular accreditations.

26. The external audit for applicants that are government entities is normally done by the Supreme Audit Institution (SAI) of the country which go by names such as Office of the Auditor General or Court of Accounts. The SAI may have specific audit reports relating to the applicant but in most cases would not. In cases where there is no specific report the Panel needs to evaluate whether the overall government control framework has sufficient checks and balances to safeguard any monies provided by Fund. If the Panel concludes that there are sufficient safeguards then it would not insist on a specific external audit report on the entity itself. Nevertheless, the Panel may review the government-wide financial report of the SAI to get a sense of the overall controls of the government and their specific application to the entity.

#### *Audit Committee*

27. Applicants are expected to have an audit committee. Such a committee is made up from members of the governing body or external experts that would meet several times per year to advise the Chief Executive Officer and the Board on areas of governance including:

- The adequacy of the annual financial statements and the audit thereof,
- The adequacy of the governance systems, internal controls and risk management,
- The adequacy of internal audit and investigations, and could also include
- The adequacy of the project management cycle including evaluations.

28. The Panel provides guidance that can be used to formulate terms of reference for such a committee. Smaller entities seldom have such a committee. However, they can benefit from establishing an audit committee because it forces the entity to reflect periodically on its ongoing control and governance activities. For small entities applying under the streamlined approach an additional degree of flexibility would be appropriate. For example, an existing committee such as a finance committee or another Board sub-committee could take on the audit committee responsibility.

29. For Government operating under the Commonwealth system the equivalent of an audit committee would be their Public Accounts Committee that is made up of Parliamentarians and is usually chaired by a member of the opposition. However, such a committee may be dealing at a too high a level to impact the operations of an applicant under the streamlined process. A mitigating control was recently discussed with an applicant. The applicant used a Project Management Committee made up of the heads of various government departments to monitor its projects including the review of significant project procurement decisions. The Terms of Reference of the Project Management Committee were expanded to also include the typical tasks of an audit committee.

#### *Accounting Package*

30. Five years of accreditation experience has taught the Panel that all applicants use software packages for their accounting. All, except a few large applicants, have purchased these accounting packages and the description thereof is available on the vendors' websites. This gives the applicants the option to provide a reference to the vendor's website rather than submitting a full description of the software. This is a simple efficiency measure that also results in more accurate information for the Panel. In the case of government applicants the same accounting package is normally used throughout the government. This would be acceptable for accreditation unless there is information that would give concern to the Panel.

#### *Internal Audit*

31. The International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors is the golden standard applicable world-wide. These standards are translated in many languages. Training, related practice forums and practitioner meetings are available throughout the world. Many related professional network gatherings are available at a low cost to the participants. These international standards place significant emphasis on having sufficient resources, annual planning, being accountable for the plan and following-up on implementation of audit recommendations.

32. Large organizations would have an in-house internal audit staff but this is an unnecessary burden for smaller organizations that are closely controlled and scrutinized through a tight budgetary process and by a Board of Directors or another governance structure. The approach applicable to small entities applying under the streamlined process would therefore be to ask for an annual independent review of the operation of its key internal controls done by an audit firm or consultant.

33. Internal audit reports provide detailed and independent confirmation of the state of the applicant's controls, capabilities and the strength of its management. This is particularly true for applicants that qualify under the streamlined approach. The Panel therefore insists to review at least one recent internal audit report or equivalent under the streamlined process. If no satisfactory internal audit report or equivalent is available an internal audit review or equivalent would have to be commissioned during the accreditation process. .



### *Internal Control Framework*

34. An internal control framework entails all the governance systems, policies, procedures and practices to ensure that the objectives of an organization will be met and applies to every part of the organization. A few larger organizations have a document that codifies its systems and procedures into a framework and may have used the COSO<sup>2</sup> methodology to do so. However, such frameworks are often restricted to specific processes such as the issuance of financial statements. In general they are not mature enough to enable the Panel to use them as a benchmark when judging the quality of the internal control framework of small applicants. Therefore a more practical approach is taken.

35. First it is expected that the governance roles and responsibilities are set out in a document. This can usually be found in the legislation or documents establishing the applicants' organization. Second, it is recognized that if the fiduciary standards and the requirements of the application are met, it would constitute an adequate internal control framework that covers the areas of risk associated to any funding by the Fund. Hence if an applicant meets the requirements set out in the application then it can be concluded that it has an adequate internal control framework to execute projects funded by the Fund.

36. Nevertheless, it is important that the Chief Executive and Chief Accountant take their responsibility and accountability for operating within a framework of adequate internal controls. Therefore, the Panel has insisted that applicants issue an annual statement identifying the significant governance controls with a statement that these were effective during the year and back up such a statement with a periodic and systematic review of the critical controls. Such statement would usually be issued at the same time as the financial statements. This requirement is maintained and the Panel provides guidance to an applicants that do not have a tradition to prepare such a statement.

37. Under the streamlined approach this requirement for an annual public accountability statement remains but would possibly be signed by the Chairman of the Board given their usual active role in the operation of smaller entities. For government entities applying under the streamlined approach the greatest risk relates to project execution. The annual accountability statement would therefore relate more to the project cycle as opposed to the financial objectives.

### *Business Plans and Budgets*

38. The fiduciary required capability is for the "*production of long term business plans/financial projections demonstrating financial solvency*". For government entities applying under the streamlined process the financial solvency depends more on the government overall commitment to applicant than the budget process itself and the Panel recognizes this in its accreditation process.

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<sup>2</sup> Committee of Sponsoring Organizations of the Treadway Commission (COSO)

### *Procurement*

39. The fiduciary standards require a competency in procurement that relates to the acquisition of goods, works, services and consultancies for projects. The emphasis of the accreditation process is on the ability of an applicant to control the procurement of the executing entities through a non-objection or a similar mechanism. However, if an applicant has limited experience with controlling the procurement of its executing entities then the Panel would review the applicant's own project procurement and will ask applicant how it will execute the procurement control function.

### *Project Approval and Appraisal*

40. The panel evaluates the following areas related to the creation and approval of a projects:

- (a) The identification and the design of a project
- (b) The appraisal activities
- (c) Incorporation of technical, financial, economic, environmental, social and legal aspects, and
- (d) Undertaking the required risks assessments and incorporating mitigating actions.

41. The approach towards project identification and appraisal activities depends on the nature of the applicant. A development bank will have policies in place and generally relies on implementing entities to manage the full design and appraisal activities. A multilateral organization that provides grants will rely on either an implementing entity or an executing entity to do these activities but it will be more involved to finalize the documentation into a standard format.

42. The system of donors and financial institutions imply that applicants applying under the streamlined approach are generally extensively involved in the identification and appraisal activities but tend to follow the structures of the organizations they deal with. They may or may not have their own methodology. From an accreditation perspective all these activities need to be done well and be complete irrespective of which approach is taken.

43. The overall risk related to the stages up to and including project approval under this approach is not extensive because of the controls exercised by Fund when during the identification, design and approval phases of a project. Other controls of the Fund that reduce the overall risk is the provision of grants for preparing projects and the rigorous validation process at both the secretariat and the Board level to ensure the quality of projects that are approved.

44. There are efficiencies that can be introduced in the accreditation process related to project identification and evaluation as part of the streamlined process. In the current application form there are different documents required for the activities related to project identification, appraisal

and risk assessment. Under the streamlined process applicants can use one document to demonstrate more than one capability.

45. Applicants under the streamlined approach have a tendency to rely upon services of the government, universities and civil society to identify and appraise projects including considerations of technical, financial, economic, environmental, social and legal aspects. This means that an accreditation recommendation can be made if an applicant has the required government controls that it can call upon provided it can manage these national stakeholders to produce the required project concepts and appraisals.

#### *Project Monitoring and Evaluation during implementation*

46. The greatest risks for the Fund related to the direct access modality is during the project execution stage. The Fund receives reports on an annual basis and all the day to day project implementation controls reside with the applicant. Therefore, the project oversight procedures need to be well understood and followed. The supporting documentation that should be provided with the application includes detailed procedures and formats used for monitoring and evaluation during project implementation. These consist of progress reports and budgets, field visits, activities requiring specific clearances or non-objection activities, and a review of the environmental and social risks.

47. Under the streamlined approach and in particular for counties with smaller projects lower cost alternatives to travel are acceptable. This is particularly true where it is expensive and difficult to travel such as in Small Island Development States or SIDS. Alternatives include extensive use of email to: obtain information on project progress and budgets, provide non-objections to procurement and other aspects and receive frequent project reporting including photographs. The use of internet will make it possible to have projects funded by the Adaptation Fund in remote parts of the world where it would otherwise not be economically or physically feasible due to the high travel cost.

#### *Project Closure and Final Evaluation*

48. The closure of a project including the final accounting of the project expenditures is a requirement for all implementing entities and it is not justified to streamline or reduce this aspect.

49. Applicants making use of the streamlined approach would normally engage external consultants to do the final project evaluation. In such instances the Panel would examine the ability of an applicant to: develop adequate terms of reference for outsourcing the evaluation; to support the consultants during the evaluation; and to be able to react to the lessons learned and recommendations of the evaluation report.

*Policies and Framework to deal with fraud, corruption and other forms of malpractices*

50. Under the streamlined approach the Panel would insist that the anti-fraud and corruption policy be in place but would allow the investigative function to be outsourced. This was done by one regional entity that contracted the investigation review out to its external auditors and clearly announced this on its website. For government entities, it can be the government-wide system provided it an accessible, transparent, fair and effective system. The Panel provides guidance to applicants that explains what is required.

**Recommendation**

51. The Ethics and Finance Committee may recommend the Board decide to:
- (a) Approve the streamlined process as outlined in the current document; and
  - (b) Ask the secretariat to work with the Accreditation Panel to develop a fact sheet for applicants about the process and its implications.

**ANNEX I: FLOW CHART SNIE ACCREDITATION PROCESS**

