

Third-party review of effectiveness of the UNOPS oversight mechanisms for Sustainable Investments in Infrastructure and Innovation (S3i)

UN Office for Project Services

KPMG Oy Ab

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1 Key Findings

Scope

In August 2022, the United Nations Office for Project Services (UNOPS) commissioned two independent external advisory reviews at the request of the Executive Board. The third-party reviews stem from concerns raised by reported irregularities, potential financial losses, and alleged misconduct linked to the Sustainable Infrastructure Investments and Innovation Initiative (S3i) investments. The first review focuses on identifying the root causes and institutional vulnerabilities within UNOPS that led to the failures associated with S3i. The second forward-looking review focuses on UNOPS' mandate, governance, risk management and internal control systems, performance management and accountability, and includes an assessment of the portfolio and cost structures. The two reviews have separate but inter-related Terms of References (ToRs).

KPMG Finland (KPMG) was selected as the independent external party to conduct the reviews and has consequently prepared two review reports. This report is the backward-looking review on S3i and should be read in conjunction with the second, forward-looking, review report. This report is prepared for the purposes noted above and defined in the ToR and is not suitable for any other purposes.

A draft Preliminary Key Findings document and later a draft report were submitted for factual checking to UNOPS management and the Working Group of the Executive Board simultaneously, and the comments received have been incorporated into this report. This report was submitted to UNOPS and the Working Group of the Executive Board in November 2022. The key findings should be read in conjunction with the full reports. UNOPS management, staff and stakeholders participated in the review with an open and supportive attitude.

Methodology and Approach

KPMG's methodology for the assignment focused on obtaining a comprehensive view of the process and events related to S3i and investments made under the initiative. This was conducted through the review of a significant amount of documentation, including meeting minutes and supporting documentation, manuals and guidelines, internal and external reports, accounting and payment documentation, emails, legal contracts, due diligence materials, publicly available information, and etc. that was made available by UNOPS for our review. The desk review was supported by close to 100 interviews conducted with current and previous UNOPS personnel and the Working Group and representatives of the Executive Board. The assignment was carried out during a relatively short time frame in September – November 2022.

The management of UNOPS has gathered a "timeline" summarising key decisions, communications, investigations and relevant information and documents in relation to S3i that was made available for our review.

The assignment was not a forensic investigation and KPMG's review procedures are limited to the scope outlined above as defined in the ToR and we do not accept any responsibility relating to adequacy of areas included in the ToR or the adequacy of the report for the purposes of the recipients of the report. We have performed the procedures based on the material available and are not able to assess the completeness and



accuracy of the documentation. We have not tested the documents to exclude the possibility of manipulations or to confirm the authenticity of those or any third party documents. KPMG had an interview with representatives of the Office of Internal Oversight Services (OIOS) during the assignment. However, an investigation report of S3i by the OIOS, which has been publicly mentioned, has not been shared with KPMG.

The procedures that we have performed do not constitute an audit or a review made in accordance with any generally accepted standards on auditing or any generally accepted standards on review engagements and, consequently, no assurance will be expressed. Had we performed an audit, other matters might have come to light that would have been reported.

The interpretation of legal consequences of our findings is solely a responsibility of UNOPS and the Executive Board. Our review was not performed in order to investigate the acts of individuals but rather to review UNOPS procedures and controls, and the roles and responsibilities in relation to the S3i process. The report may not be disclosed, copied, quoted or referred to in whole or in part for the purposes of disciplinary proceedings without our prior written consent. It should be noted that our final written report shall take precedence over any draft, and that no reliance should be placed by UNOPS or the Executive Board on any draft other than at their own risk.

Background

UNOPS is a United Nations agency dedicated to implementing infrastructure and procurement projects for the United Nations System, international financial institutions, governments and other partners around the world. UNOPS total revenue in 2021 was USD 1.2 billion with a total volume of operations of USD 3.4 billion (delivery). UNOPS is headquartered in Copenhagen, Denmark. Established in 1973 as part of UNDP, it became an independent subsidiary organ of the General Assembly, fully separating from UNDP, in 1995. UNOPS concentrates its support in the areas of infrastructure, procurement, project management, human resources and financial management services.

Over the last 10 years, UNOPS and its portfolio of operations have grown rapidly. UNOPS has attempted to manage this growth by expanding its staff base, establishing a policy framework and internal control environment supported by financial and project management systems, and adjusting the organisational structure, job descriptions and roles. UNOPS has also made revisions to its risk management, oversight and accountability frameworks in response to a UN High Level Committee on Management decision to endorse and effectively implement the three lines of defense model.

A new Executive Director (ED) was appointed to UNOPS in 2014. At that time, UNOPS was generally considered to be a highly relevant agency contributing to development efforts in difficult operational settings and providing support to UN Agencies and governments. However, due to its role providing operational support services, it was also a “hidden” agency that did not have as high a public profile as some of the other UN Agencies. The new ED, together with the Deputy Executive Director (DED), wanted to reposition the fairly unknown UN agency and increase its standing within the development cooperation space. This led the agency towards impact investing and other new initiatives, with the goal of achieving more with less by leveraging the resources of the private sector. As part of its profile-raising efforts, UNOPS also partnered with We



Are the Oceans (WATO) in February 2017 through a grant as a vehicle for public relations and awareness raising.

Mandate and Strategy

The new impact investing activities required revisions to the UNOPS mandate. The agency's management made gradual changes that were presented in updates to the Executive Board of UNOPS over the period of 2015 to 2021. The development of impact investing was encouraged by the Executive Board on different occasions, based on presentations by UNOPS management. In mid-2016, the Executive Board approved "the creation of a seed capital fund aimed at utilising a portion of UNOPS operational reserves to make targeted contributions to early-stage investment projects in UNOPS mandated areas". The UNOPS Strategic Plan for 2018-2021 still concentrated on the core mandate for infrastructure, procurement, project management, human resources, and financial management services. However, UNOPS top management moved forward with financing activities as a key objective although this can be viewed as an "extension" of the mandate.

To enable impact investing, UNOPS accelerated efforts to grow its business and accumulate operational reserves. UNOPS was successful in growing its reserves (i.e. net assets), which expanded from USD 159 million in 2017 to USD 360 million in 2021 (126% increase in four years). However, part of the growth of the reserves was done at the expense of investing in the organisation in terms of systems and staff. The accumulated reserves enabled the agency to take initial steps towards achieving its objective of becoming an impact investor.

Management

At the time of the new ED appointment (2014), the DED had an exceptionally strong role in UNOPS due to his recognised contribution and track record in the agency's financial turnaround prior to 2014. In parallel with the evolving mandate, changes in the management structures were implemented. The changes included a smaller top management team and less participation in decision-making from the Regional Groups. The reporting structures of top management were also reorganised. As a result, most of the key management functions, with the exception of internal audit, ethics, and communications, reported directly to the DED, who in turn reported to the ED. The new management structure, combined with significant delegated authorities to the DED, as the only Assistant Secretary-General (ASG) in the agency, and the ED, as the only Under Secretary-General (USG), led to high concentration of decision-making power at UNOPS.

Based on interviews, UNOPS management culture started to develop into a strong top-down approach with a high focus on growing the business and reserves. Increased revenues were prioritised even if it meant venturing further from the original mandate of UNOPS and taking on more risk. UNOPS top management, especially the ED and the DED, focused on developing and initiating impact investing. These changes in management focus were combined with what appears to be a systematic approach to reduce transparent sharing of information and undermine the key management team members ability to challenge decisions such as by referring to "lack of understanding the business and private sector way of working". Interviews indicate there was a noticeable fear of career consequences in case decisions or management agenda were challenged.



This developed elements of a culture of fear in the organisation, which came to influence the decision-making processes.

Investment Process and Decisions

The first concept and operational models for impact investing were developed together with external support as early as 2015. The early efforts in formulating the concept looked at the sectors of innovative finance, public-private partnerships and social investments. The model for UNOPS' impact investing continued to be developed in 2016 and more detailed operational guidelines and frameworks were prepared in 2017, with the support of an external consultant. Some aspects of the initial concepts and models were taken into use, but many critical oversight and segregation of duty elements were not implemented. This led to a situation where investment decisions of S3i were done without an investment policy framework in place and processes established.

Based on interviews, the DED was actively reaching out to stakeholders in the investment space, including investors, foundations and project developers, during this time. However, the broader management (including the Corporate Operations Group) and staff had a minor role in this engagement and limited information was shared within UNOPS. The geographical expertise and technical capabilities of UNOPS were also not being effectively utilised in the impact investment formulation and screening. At this point, there were limited concrete results from the planning efforts and consultations with investment stakeholders. UNOPS management in-charge of driving forward S3i had not been able to identify clear added value or complementarity that the agency could bring to the investment market.

The plans for impact investing highlighted that UNOPS needed to strengthen its organisational capacity before venturing into this sector. However, limited investments in people or processes were made prior to making the first significant investment decisions. The envisioned objectives were ambitious compared to UNOPS track record and capability to deliver on investments. Due to this limited capacity and experience in similar investment arrangements, it appears that the management did not fully take into account the risks involved. The lack of experience led to limited due diligence and vetting procedures performed in relation to the S3i investments. As an example, based on meeting material available for our review, the Engagement Acceptance Committee + (EAC+) did not receive appropriate documents related to the financial model nor review the financial model for the housing projects that comprised USD 35 million of the investments made.

By the time an S3i office was opened in Helsinki, in January 2021, all S3i investment decisions had already been made. The Helsinki-based team, mainly comprising new hires to UNOPS, had a limited role in the management of the initial investments.

Based on our review, there was a limited transparency from the top management in relation to selection of partners and limited financial and technical due diligence to support the evaluation process was found available for our review. UNOPS has a full set of administrative and financial rules for its regular operations, but the selection of S3i partners did not follow all of these procedures. One of the main reasons for the selection of Sustainable Housing Solutions (SHS) Holdings as a key partner for S3i, as presented by the DED to the Senior Leadership Team (SLT), was a unique and affordable new technology. Limited documentation on technical due diligence was available for our review and it appears that a complete technical due diligence on the technology or



feasibility studies by designated expert teams over the concepts were not conducted, despite UNOPS' strong expertise in infrastructure.

UNOPS took financial and reputational risks with the commitments of sustainable housing, although the concept was merely at piloting stage. Together with the governments of several partner countries, UNOPS committed to constructing 760,000 houses in five countries (with financing contracts signed), which would have required total investments in the scale of USD 20 - 50 billion. (The investment value is based on an average cost of USD 25,000 – 50,000 presented in the submission documentation, which has not been verified or thoroughly vetted by UNOPS.) With an average household size of five people, the projects would have created houses for 3.8 million people. Publicly UNOPS had committed to sustainable housing in seven countries with a total of 1.3 million houses.

Decision-Making

To support S3i decision-making, the ED convened meetings with members of the Corporate Operations Group (COG) and named them EAC+. The aim of the EAC+ was to function as a review panel on S3i investments. However, no official terms of reference or mandate for the EAC+ were established. The members of EAC+, as noted above, consisted of selected members of COG (later on SLT), and the DED and ED. All members of EAC+ reported to the DED, except for the ED. No technical experts or investment professionals were included in this committee. The ED had the decision-making authority on the investments. There was limited segregation of duties in the decision-making process of the S3i investments. The DED, who had led the development of the investment projects, also presented the projects to the EAC+, was a member of the EAC+ and in the final stage signed the financing contracts after the ED approval. A perception of urgency was created around the preparation and presentation of investment cases and the investment decision process. Combined with the described culture of fear and lack of an investment framework, this contributed to a weakened environment for decision-making.

The first investment within S3i, valued at USD 8.8 million, was made in August 2018 to a wind project in Mexico through an SHS related company (World Wide Renewable Energy, WWRE). Before the financing decision, an advance payment of USD 0.9 million was paid to the company for due diligence and preparatory procedures. In the January and March 2019 EAC+ meetings, S3i investments of USD 30 million in the form of loan facilities were endorsed. This included USD 15 million in total for social housing projects in Kenya, Ghana, India, and Antigua and Barbuda, and USD 15 million for renewable energy portfolio. Another loan facility to SHS was agreed in October 2019 when EAC+ endorsed USD 20 million to a housing project in Pakistan. As UNOPS has recognised all loan facilities were approved by the ED based on her authority. All of the loan facilities in 2018 and 2019 were made to companies with direct or indirect ownership interest associated with a British businessman. At this point, investments and grant funding had been provided to various sectors (oceans awareness campaign, renewable energy and affordable housing) but ultimately associated with a single British family. The idea of diversifying the risk by investing in different countries through a platform, as presented by the ED and DED in the EAC+ meetings, ultimately led to pooling of risks to a single group of associated entities. In total USD 59.7 million was disbursed from UNOPS to



SHS and its related and/or affiliated entities through the S3i investments, and USD 3.3 million through the WATO/Oceans Generation grant. It should be noted that SHS and its related/affiliated entities have repaid USD 6.2 million to UNOPS at the time of this reporting.

Red Flags and Risk Alerts

Prior to investments being made, gaps, risks and red flags had been identified and alerted. The red flags were brought to the attention of the EAC+, including the ED and DED (especially prior to the investments in 2019), and to a certain extent to the oversight functions. Risks were also highlighted by the EAC+ members, but ultimately decisions to proceed with the investments presented by the DED were endorsed by the EAC+ and approved by the ED based on her mandate. Based on the review, it appears that UNOPS management and oversight functions did not effectively respond on these risk signals. We describe the key red flags below.

A whistleblower complaint was made in early 2019 on the S3i arrangements. The complaint highlighted many of the risks in relation to the investment decision making, including investing in one partner without any competitive vetting process, and limited due diligence.

One red flag that was observed early on is that members of the same family were associated with both SHS and WATO. WATO had received a USD 5.0 million grant from UNOPS in February 2017, of which USD 3.0 million was disbursed in a single payment after the Memorandum of Agreement (MoA) was signed. A new MoA was prepared with Oceans Generation in November 2018 continuing the grant implementation activities of WATO, and the remaining grant of USD 2.0 million was transferred to the new MoA. Only USD 0.3 million of that grant was utilised and in 2019 Oceans Generation terminated the MoA and returned unused funds. UNOPS observed challenges in the early stages of the WATO grant implementation, including what UNOPS has referred to as an unexpected need to create a new entity, Oceans Generation, to continue the implementation of the grant activities in 2018.

The Internal Audit and Investigation Group (IAIG) of UNOPS identified related party transactions in relation to the use of the WATO grant during a review in early 2019 which was alerted to the ED and circulated to the DED and some of the EAC+ members. The IAIG investigation that was conducted in 2021 concluded the same.

UNOPS did not require WATO to provide complete audited financial statements including income statement, balance sheet and notes. It can be noted that UNOPS, as part of the financial monitoring activities, accepted an audited statement of receipt and disbursements of WATO as of December 31, 2017, not containing any notes.

Based on the EAC+ meeting minutes, the members were aware of the family relationship associated with WATO and SHS prior to the SHS investment decisions in March 2019, but decided to progress with the financing arrangement.

The reputational due diligence procedures that were conducted for the SHS housing projects in Antigua and St. Lucia highlighted risk areas for further investigation (with reference to media reports from 2014 and 2016) and that the selection method of sole-sourcing with SHS required particular attention from UNOPS.



As noted above, the EAC+ members raised risks in the S3i investments, including concerns related to significant exposure to one partner, limited due diligence on commercial potential, operational capacity of the partner, no collateral on the loans, reputational risks, UNOPS lack of capacity in implementing projects in four countries simultaneously, and possible challenges with the allocated land (provided by the local governments).

Based on material available and our procedures, it seems that these red flags were disregarded without comprehensive mitigation measures and final decisions were made on 22 March 2019 to invest USD 30 million in the form of loans into five projects (with a commitment of up to USD 50 million). The full amount of USD 30 million was disbursed to the companies shortly after the SHS financing contracts had been signed.

Oversight

The inefficiency of oversight mechanisms at different levels contributed to making the investments possible despite the red flags and risks highlighted earlier. The Audit Advisory Committee (AAC) was not performing an oversight role and instead had a mandate and role in practice to advise, rather than monitor, the ED. The EAC+ members perceived their role as advisory and did not feel accountable for the endorsements the committee made. This was a result of the limited segregation of duties, the DED and ED driving the process, and limited mitigation measures taken as part of the investment preparation despite the risks highlighted by the EAC+ members. Interviews indicate that the personal motivation among EAC+ members to effectively influence decisions was reduced as a result of the lack of mandate in the decision-making process, management structures and culture.

OIOS received a whistleblowing complaint in relation to S3i in early 2019 (the complaint noted above), prior to approval of the most significant SHS investments. OIOS transferred the responsibility to investigate the complaint to the IAIG. The complaint also referred to the UNOPS DED. However, IAIG was not mandated to investigate matters concerning the ED or the DED, who was in an ASG position. Thus, the complaint was not investigated at that time by IAIG or OIOS.

As risk signals in relation to the S3i investments started to accumulate, IAIG opened investigations into WATO and SHS. However, the investigations were only completed in August and October 2021, two and a half years after the initial complaints. There is indication that IAIG was not in a position to perform its duties independently, as noted by the Joint Inspection Unit (JIU) and self-assessed by IAIG in 2022.

Interviews indicate that the whistleblowing mechanism was not functioning effectively due to a lack of trust in confidentiality during the processing of complaints and fears of retaliation among staff.

The reporting on S3i activities was not fully transparent in addressing and disclosing risks that were already known to management in 2019 and understood more clearly in 2020. The Executive Board, based on the information presented by UNOPS management, approved the growth and innovation fund from the reserves, which was used to create the S3i initiative and encourage the development of impact investing. The Executive Board was not able to provide effective oversight as a result of the structural challenges, lack of comprehensive information related to risks in the reporting and limited time resources allocated for oversight.



With regards to operational oversight, we identified weaknesses in the financial management procedures in relation to UNOPS' monitoring of S3i activities and financing contracts. This was combined with the fact that the contracts did not include some available tools for protection of financial interest for UNOPS; they had no collateral terms, included a high level of advance payment considering the early stage of activities, and UNOPS limited control over funding flow after the initial disbursements.

UNOPS has administrative and financial rules and procedures, but the S3i initiative was to a far extent operating outside this framework, and the agency's risk management, legal, technical and financial due diligence principles were not followed to the extent expected and required by UNOPS policies in investments of the scale UNOPS made. There were deficiencies in the independence structures of the oversight bodies which affected their ability to effectively monitor the S3i related activities.

Conclusion

Our review was conducted in a situation where many of the negative consequences arising from the S3i related activities have been discussed in the public and with some time elapsed since key decisions were made. Despite this hindrance, the overall view we gained from the material available and the interviews conducted shows that a combination of technical, operational, oversight and governance deficiencies, choices in risk taking and elements of a culture of fear created an environment that was vulnerable to management override of controls. The review interviews indicate a broad perception that the top management took improper advantage of their position and authority in S3i preparation and decision-making reflecting elements that can be associated with abuse power. UNOPS has a full set of administrative and financial rules for its regular operations, but the selection of S3i partners did not follow all of these procedures.

The background for the independent reviews stems from the concern expressed by the UNOPS Executive Board in June 2022 of reported irregularities, potential financial losses, and alleged misconduct linked to S3i. Our review was not a forensic assignment and our objective was not to provide an opinion on whether irregularities or alleged misconduct have taken place. The procedures of our review are as described in the approach and methodology.

Based on our review procedures, we note that UNOPS has identified a number of red flags as part of the S3i investment timeline. The red flags in relation to the S3i activities were identified and reported at different times and at different organisational levels by UNOPS and its oversight bodies. UNOPS top management's disregard for these early risk signals, in combination with weaknesses in the control environment and management culture, were identified in our review as root causes and institutional vulnerabilities within UNOPS that contributed to failures associated with S3i. At the time of our reporting, the financing contracts between UNOPS and SHS are under legal review. Summarized root causes and institutional vulnerabilities in relation to the S3i reported failures are illustrated in Figure 1 below.

The observations of this report indicate that UNOPS needs to implement significant changes and improvements in order to return to a well-functioning organisation with a strengthened control environment and more open and participatory culture. Immediate actions are already in progress but, considering the negative consequences arising from the S3i related activities and the time needed to change an organisational culture,

UNOPS and its management have initiated a transformation process. We outline our recommendations for UNOPS in the forward-looking report.

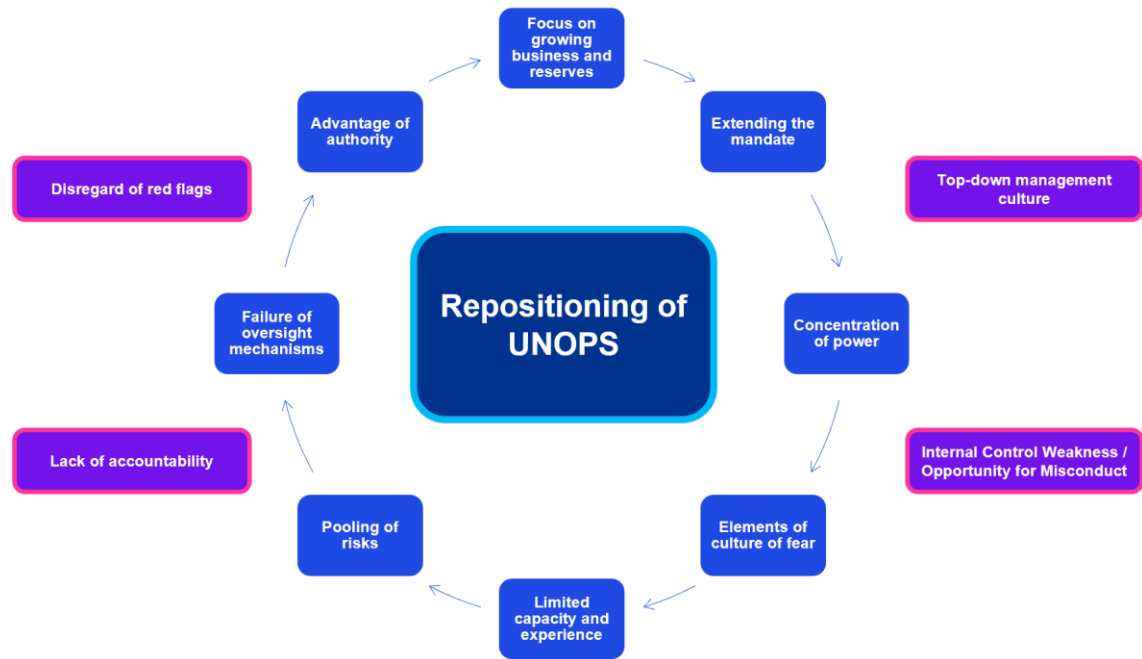


Figure 1: Root Causes and Institutional Vulnerabilities Associated with S3i Reported Failures



Contact us

Anders Lundin

Partner

T +358 20 760 3000

E anders.lundin@kpmg.fi

Lauri Tuomaala

Partner

T +358 20 760 3000

E lauri.tuomaala@kpmg.fi

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