

Term of Reference for External Audit services for DKH financed project

The purpose of this letter is to set out the basis on which the auditors will act as “Auditors of the Project Holder” and to stipulate the respective areas of responsibility of the auditors and project managers.

1. SCOPE OF THE AUDIT

The Auditor designs and carries out the audit in accordance with the objective and scope of this engagement and the procedures. The Auditor may apply techniques such as inquiry and analysis, (re)computation, comparison, other clerical accuracy checks, observation, inspection of records and documents, inspection of assets, obtaining confirmations or any others deemed necessary in carrying out these procedures.

Special attention shall be given to the fact that income through funds from DKH and other aid agencies are earmarked funds. This earmarking is based on the objectives/goals and measures defined in the project as well as on the approved expenditure budget and finance plan. The balances of earmarked funds (project balances) shall be shown as liabilities at the end of the accounting period. In addition the auditors shall analyse the economical and sparing use of funds in accordance with the established local price structures and the contracting practices for placing orders/procurements.

The auditor obtains sufficient appropriate verification evidence from these procedures to be able to draw up a report of factual findings.

The audit of the project will include such tests and auditing procedures as the auditor will consider necessary under the circumstances. Special attention should be paid by the auditor as to whether:

- a) all applicable relevant) rules and regulations of Diakonie Katastrophenhilfe (DKH) and the contractual engagements have been adhered to. These include the:
 - Cooperation Agreement;
 - Administrative and Procurement Procedures;
 - DKH Standards for reporting;
 - Approved budget (cost Plan);
 - International Standards on Auditing;
- b) Funds have been provided and used in accordance with the relevant financing agreements and the relevant donor regulations from DKH, with due attention to economy and efficiency, and only for the purposes for which they were provided;
- c) Goods, works and services financed have been procured in accordance with the relevant financing agreements, including specific provisions of the donor and their procurement Policies and Procedures based on Cooperation Agreement terms;

- d) All necessary supporting documents, records, and accounts have been maintained in respect of all project activities, including expenditures reported using Statements of Expenditure (SOE). The auditor is expected to verify that respective reports issued during the period agree with the underlying books of account;
- e) Designated Accounts have been maintained in accordance with the provisions of the relevant financing agreements and funds disbursed out of the Accounts were used within the required timeframe and only for the purpose intended in the financing agreement;
- f) National laws and regulations have been complied with, and that the financial and accounting procedures approved for the project (e.g. financial procedures manual, etc.) were followed and used;
- g) Assets procured from project funds exist and there is verifiable ownership by the partner office.

In complying with International Standards on Auditing, the auditor is expected to pay particular attention to the following matters:

- a) **Fraud and Corruption:** Consider the risks of material misstatements in the financial statements due to fraud as required by ISA 240: The Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements. The auditor is required to identify and assess these risks (of material misstatement of the financial statements) due to fraud, obtain sufficient appropriate audit evidence about the assessed risks; and respond appropriately to identified or suspected fraud;
- b) **Laws and Regulations:** In designing and performing audit procedures, evaluating and reporting the results, consider that noncompliance by the Partner abroad with laws and regulations may materially affect the financial statements as required by ISA 250: Consideration of Laws and Regulations in an Audit of Financial Statements;
- c) **Governance:** Communicate audit matters of governance interest arising from the audit of financial statements with those charged with governance of an entity as required by ISA 260: Communication of Audit Matters with those Charged with Governance;
- d) **Risks:** In order to reduce audit risk to an acceptable low level, determine the overall responses to assessed risks at the financial statement level, and design and perform further audit procedures to respond to assessed risks at the assertion level as required by ISA 330: the Auditor's Procedures in Response to Assessed Risks.

2. PROJECT FINANCIAL STATEMENTS (PFSs)

The auditor should verify that PFSs have been prepared in accordance with the international accounting standards and give a true and fair view of the financial position of the project at the relevant date and of resources and expenditures for the financial year ended on that date

The Project Financial Statements (PFSs) should include:

- a) A statement of funds received, showing funds received from the DKH Head Office in local and foreign currencies;
- b) A statement of Expenditures (SOEs);

- c) A cash flow statement;
- d) A summary of the principal accounting policies that have been adopted, and other explanatory notes;
- e) A list of material assets acquired or procured to date with project funds.

As an Annex to the PFSs, the auditor should prepare a reconciliation of the amounts as “received by the Project”, with those shown as being disbursed by the Bank (Balance at Hand).

3. STATEMENT OF EXPENDITURES (SOEs) / JOURNAL LISTING

- a) The appropriate exchange rates are used, based FIFO Method;
- b) The Exchange Rates Table includes the organization's calculation methods for exchange rates;
- c) The exchange rates in the Exchange Rates Table are the same as those used in the journal listing;
- d) The columns in the voucher lists are filled with all the necessary details required;
- e) In principle, all inspected documents have to be the original copies. Especially, proofs of payments are to be checked;
- f) The items registered as capital assets correspond to those recorded in the inventory listing;
- g) Examine, on a test basis, that there is supporting documentation related to reported expenditure. The size of the test shall be based on the auditor's risk analysis, which should be stated in the report. The auditor shall report the identified amount in case there is any missing supporting documentation;
- h) Follow up whether salary costs debited to the project correspond to the agreed percentages and are recorded throughout the duration of the year in a systemized way and examine whether the salary costs can be verified by sufficient supporting documentation;
- i) Examine partner compliance with rules and regulations with regard to applicable local taxes and social security fees;
- j) Examine partner compliance with all relevant rules and regulations of DKH and the expenditure deadlines per disbursement;
- k) The total withdrawals under the SOE should be part of the overall reconciliation of Bank disbursements;
- l) The auditor should examine the eligibility of financial transactions during the period under examination and fund balances at the end of such a period;
- m) The adequacy of internal controls for this type of disbursement mechanism;
- n) The operation and use of the designated fund in accordance with the financing agreement;

4. DESIGNATED ACCOUNT

In conjunction with the audit of the Project PFSs, the auditor is also required to review the activities of the designated account associated with the project. The Designated Account usually comprises:

- a) Income received from DKH Head office;
- b) Interest that may have been earned on the accounts;
- c) Withdrawals related to project expenditures;
- d) Transfers from and to other projects
- e) Account balances at the end of such a period.

5. AUDIT REPORT

The auditor will issue an opinion on the project financial reports (PFSs). The annual audit report of the project accounts should include a separate paragraph highlighting key internal control weaknesses and non-compliance with the financing agreement terms.

The addressee of the audit report is the authorized representative of the project holder as well as the country representative of DKH.

The following documents have to be delivered by the auditors:

- Auditor's report/opinion including a compliance statement in respect of the DKH funds;
- Audited financial statement(s) of the project(s) under consideration (income and expenditure account of the project holder, receipt and payment account; list of transactions/ cash flow statement of the project including opening and closing balances of funds and a plan-actual comparison / variance report with the approved budget);
- Management Letter (including comments on the implementation of previous year's recommendations and new recommendations);
- Notes to the accounts (if relevant in the given context of the project):
 - a) list of income/receipts according to origin/source;
 - b) List of transactions;
 - c) foreign currency transactions (incl. examination of exchange transactions and used exchange rates);
 - d) list of all bank accounts of the partner in the country;
 - e) statement on assets, procured by the partner by the project funds;
 - f) Unspent balance per audited project

6. MANAGEMENT LETTER

In addition to the audit report, the auditor will prepare, if the auditor deems it necessary, a management letter, in which the auditor will:

- a) Give comments and observations on the accounting records, systems and controls that were examined during the course of the audit;
- b) Identify specific deficiencies or areas of weakness in systems and controls, and make recommendations for their improvement;
- c) Report on the degree of compliance in the financing agreement and give comments, if any, on internal and external matters affecting such compliance;

- d) Communicate matters that have come to his/her attention during the audit which might have a significant impact on the implementation of the project;
- e) Bring to the recipient's attention any other matters that the auditor considers pertinent.

Ideally, the management letter should also include responses from the partner abroad to the issues highlighted by the auditor.

7. Time frame & Audit Deliverables

- The financial report and accounting records of the project under consideration must be made available by the partner and the DKH representative to the auditors _____
- The auditing process shall be completed within _____ weeks after this date.
- Two copies of the audited financial statements including the audit report, management letter and management response should be received by the audited partner no later than one week after completion of the audit.
- If there is any reason for a delay, this has to be communicated directly to the audited partner by either party (with copies of the correspondence to the other concerned party).

8. Desired Profile of the Auditor(s)

- Audit firm with a Regional presence in the Project Implementation country or with permit to operate in the abovementioned country.
- The audit firm must be registered and has a license from a national or regional professional Accountancy Body.
- The firm should have relevant experience (having in its staff at least 5 certified professionals: ACCA/CPA/National A certificate of auditing) in accounting and auditing of humanitarian projects, especially donor-funded operations.

9. Language

Audit report, Management letter, other communication shall be in English language

The Auditing Firm::

***The Authorized Representative
of the Project Holder::***

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Date / Signature

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Date / Signature