

SUMMARY REPORT ON MAIN RISK AREAS RAISED IN
THE REPORT OF THE BOARD OF AUDITORS ON THE ACCOUNTS FOR 2008

I. INTRODUCTION

1. Since the 37th meeting of the Standing Committee in September 2006, each year¹ UNHCR has presented a summary report on key issues raised in the recommendations of the Board of Auditors on the accounts for the previous year. This conference room paper comments on the main issues raised in respect of the accounts for 2008.

2. The total number of recommendations issued by the Board of Auditors in its 2008 report was 19, including 13 main recommendations. It should be noted that the majority of the recommendations relate to issues and subjects previously raised. Nearly all of the recommendations have been accepted by UNHCR and are in the process of being implemented. The detailed report, *Measures taken or proposed in response to the recommendations of the Board of Auditors for the year ended 31 December 2008*, is contained in document A/AC.96/1067/Add.1. An update on follow-up action and implementation of the recommendations from previous years will be presented in a conference room paper to the Standing Committee at its March 2010 meeting. Details on the status of all outstanding recommendations are available on UNHCR's website at www.unhcr.org/excom.

3. Following the issuance of the report on UNHCR's accounts for the year 2008, in consultation with the Board of Auditors four high risk areas were identified as the focus for reporting by UNHCR namely: implementing partner audit certification; asset management, including both non-expendable and expendable property; accounting for contributions; and end-of-service and post-retirement benefits liabilities. This document reviews the recommendations made by the Board of Auditors for the four high risk areas, including an analysis of each area, and outlines how UNHCR plans to address the identified risks.

II. RISK AREAS

A. Implementing partner audit certification

4. In its report on the 2008 accounts, the Board of Auditors reiterates its previous recommendations regarding the implementing partner audit certification process, while also

¹ No paper was provided in 2007 as the Report of the Board of Auditors was released late, on the eve of the 40th meeting of the Standing Committee.

noting the efforts and improvements made by UNHCR to enhance the process. The Board recommends that UNHCR “intensify its efforts to obtain audit certificates from implementing partners (IPs) by 30 April each year,” and “intensify its efforts to conduct an in-depth analysis of audit certificates in order to make potential adjustments to prior year expenditure in the financial statements.”

5. UNHCR implements its mandate through a vast array of partners. In 2008, 840 partners were entrusted with 1,745 sub-projects representing over \$531.5 million, i.e. 32.6 per cent of UNHCR’s overall expenditure of \$1,628 million. Given the significant amount of funds channelled to its beneficiaries through IPs, there is a potential risk that some of the funds are not disbursed for the purposes intended, or not in accordance with UNHCR’s rules.

6. To mitigate this risk, over a number of years, UNHCR has elaborated a comprehensive internal control framework with regard to programme monitoring. The internal control framework consists of a three-layered approach. The first layer involves ongoing monitoring undertaken in the Field by UNHCR programme staff through meetings, guidance and on-site field visits. The second layer is the requirement for IPs to complete narrative and financial monitoring reports, outlining that the funds received have indeed been utilized in accordance with the agreement and in compliance with UNHCR’s rules. The third layer consists of an audit of the project, a measure that UNHCR has introduced to ensure, through independent assessments, that the funds disbursed via IPs have indeed been spent correctly. The audits should therefore not be seen in isolation, but as part of a comprehensive control framework.

7. Notwithstanding the above, UNHCR is striving to streamline the audit process to improve the compliance rate and to address issues raised in qualified audit reports. As part of this process, a standard set of terms of reference for external audits of UNHCR’s IPs will be used as part of the audit process of the 2009 accounts. In 2007, the Division of External Relations and the Division of Financial and Administrative Management established a working group to develop practical tools to improve the selection and risk management of IPs. In January 2009, a memo was sent to all offices in the Field containing a checklist to be used in assessing the suitability of an IP, upon initial selection or as part of the ongoing monitoring. The memo also contained suggested actions that could be taken based on the assessment of risks. The impact of this guidance will only be observable next year.,

8. As noted in the report of the Board of Auditors, at the end of June 2009 the compliance rate for 2008 audit certificates was 58 per cent; whereas the comparable compliance rate in 2008 for 2007 audit certificates was 57 per cent. This reflects an improvement, particularly considering that an additional value of US\$ 190 million was subject to audit, requiring 158 additional audit certificates for 2008 sub-projects. As of 3 August 2009, UNHCR had received audit certificates covering 83 per cent of the instalments paid to IPs in 2008.

9. UNHCR implements projects through three main categories of partners: international non-governmental organizations (NGOs), local NGOs, and governments. The compliance rate varies between the categories. In addition, UNHCR often fails to convince some governments to open up their accounts for external inspection, because they have their own internal oversight systems. As of July 2009, audit certificates from two governments implementing six projects made up the bulk of the remaining 16 per cent of the value of 2007 sub-projects still requiring an

audit. Also as of July, 48 per cent of the audit certificates due from governments for 2008 projects were still outstanding. It could be argued that UNHCR should cease cooperation with these partners unless they agree to comply with the audit process. However, in many operations, government entities may be the only option available to UNHCR to implement certain projects.

10. In some operations, UNHCR faces other difficulties in obtaining audit certificates. For example, some IPs have had their records confiscated and been asked to leave the country. In other operations, no audit certificates could be produced due to the security situation. In one particular case, UNHCR was satisfied with the financial monitoring reports covering the total amount disbursed by IPs, however, the audit was deferred for security and logistical reasons, and as a result an amount of US\$ 11 million is still awaiting audit certification and forms part of the statistics of audit reports not received.

11. In accordance with the internal control framework outlined above, UNHCR will pursue its efforts to apply all three measures to its projects, and in time for the external audit of the year-end accounts. Nevertheless, considering the operational context of UNHCR, it is unlikely that complete compliance within a relatively short time frame will ever be feasible. UNHCR acknowledges that, when reliance is placed only on the first layer of monitoring, the organization may be exposed to a financial risk. However, UNHCR does not believe that a lack of audit certificates exposes the organization to undue financial risks, provided that the first two layers of measures have been implemented. In addition, as financial monitoring reports and audit certificates continue to be received and analysed, the financial risks are kept to a minimum. At the time of writing, UNHCR had received reports from IPs for 98 per cent of the 2008 instalments paid, excluding those projects that were extended. UNHCR will continue to further minimize the risks by requiring early compliance with submission of IP financial reports as well as with the audit certification process, where feasible.

12. UNHCR also acknowledges the risks involved in receiving qualified audit opinions on the implementation of UNHCR projects by IPs. The possible outcome of a qualified audit opinion of a partner's accounts depends on the type of qualification, which normally falls into one of the following categories: 1) internal control weaknesses; 2) inability to access the documentary evidence of transactions; and 3) inability to justify payments. An in-depth analysis of the qualified audit opinions for 2007 found that less than 1 per cent of the qualified audit opinions could potentially expose the organization to a financial risk. If the rate for 2007 was applied to the 2008 value of audit certificates received with a qualified audit opinion of US\$ 29 million, the risk would amount to 0.01 per cent of UNHCR's total 2008 expenditures of \$1,628 million. Notwithstanding the relatively minor financial risk involved, UNHCR acknowledges that further efforts must be undertaken to reduce the number of qualified opinions, and will continue to analyse the underlying reason for the qualified opinion so that the identified issues can be promptly addressed.

13. UNHCR recognizes the importance of having an effective, realistic and comprehensive programme monitoring system in place and is committed to ensuring that it more accurately reflects what can be reasonably expected in terms of programme monitoring, given the vast array of IPs involved and the challenging environment in which it operates. In doing so, UNHCR will review its current policy on audit requirements and, in light of its experiences to date and paying

particular attention to the complex operations and known challenges, will consider alternative approaches that are relevant and cost-effective, and which can be realistically implemented. Throughout the process, UNHCR will continue to consult with other United Nations agencies that have a similar field-oriented structure, as well as with internal and external auditors.

B. Asset management

14. UNHCR acknowledges the need to have an effective asset management system in place. Inadequate asset management poses certain risks, including loss, theft and diluted accountability. UNHCR is therefore committed to a significant improvement in its asset management practices, as it works towards full compliance with the International Public Sector Accounting Standards (IPSAS) in 2010.

Non-expendable property

15. In its report, the Board of Auditors makes two recommendations with regard to non-expendable property: 1) UNHCR should review the control deficiencies identified in the recording of non-expendable property; and 2) UNHCR should continue the effort undertaken to clean up its database for non-expendable property, and establish a monitoring system for tracing all corrections made in the database during a financial year.

16. The current control deficiencies will be adequately addressed as part of the IPSAS-compliance implementation. UNHCR has adopted and implemented a revised policy that establishes a threshold for the recognition of assets, in line with IPSAS policies and the practice of other United Nations agencies.

17. Ensuring the accuracy and completeness of assets in the database is an ongoing process, and UNHCR is currently coordinating a full review of non-expendable property for every country. As of July 2009, some 90 per cent of the clean-up work of the database of non-expendable property has been done and the task is expected to be completed by the end of the year.

18. Measures that have already been undertaken to address control deficiencies include: monitoring of all purchases to assure correct entry of non-expendable property into the asset database; detailed monitoring of all asset verifications performed at Headquarters and in the Field; and the recording and monitoring of all Local Asset Management Board cases in the Field. In September 2009, UNHCR's Asset Management Unit will introduce a system to monitor all disposals by verifying that they have been correctly processed through the relevant Asset Management Boards. Furthermore, as part of the IPSAS implementation, UNHCR will limit corrections that can be made to the database by field offices.

Expendable property

19. In its report, the Board of Auditors reiterates its recommendation that UNHCR disclose in its future financial statements the value of expendable property unused at the end of the year, in order to provide a more complete and accurate account of its assets.

20. The clean-up of the expendable property database has been initiated and a policy document on the subject of inventory (i.e. expendable goods that UNHCR procures or receives that are intended for distribution to refugees,) was issued in January 2009. The clean-up will be completed by the end of 2009. The business requirements have been defined to disclose and account for inventory, in accordance with IPSAS, and efforts are being pursued to complete the system and the procedural changes necessary to start accounting for inventory in 2010.

C. Accounting for contributions

21. In its report, the Board of Auditors recommends that UNHCR: 1) ensure that contributions received are subject to timely accounting processing by clearing the suspense accounts; 2) implement appropriate internal control procedures to prevent entry errors for contributions and to ensure the reliability of the income recording system; and 3) review its policy concerning non-recoverable voluntary contributions, in order to ensure compliance with paragraph 34 of the United Nations System Accounting Standards.

22. Since the ceiling for expenditure is linked to the level of income, UNHCR acknowledges that inaccurate accounting for contributions could potentially result in taking inefficient or even incorrect resource allocation decisions. Overstatement of accounts receivable due to the incorrect application of receipts for pledges could also lead to misinformation regarding the status of donor contributions. UNHCR therefore takes these recommendations very seriously and aims to address them within the shortest possible timeframe.

23. Effective coordination between the Financial Control Section (FCS) and the Donor Relations and Resource Mobilization Service (DRRM) is important in terms of correct accounting for contributions and receipts. To this end, FCS, the Treasury Section and DRRM have reviewed the processes of recording contributions and applying receipts to identify and address the weaknesses in the current process. The following measures have already been put into place: a) a biweekly comparison and follow-up of all unidentified deposits recorded in contributions suspense accounts; b) immediate follow-up with DRRM to obtain information when deposits are received from donors and the corresponding pledge cannot be identified; and c) immediate confirmation with DRRM to ensure that a payment has been matched to the correct pledge.

24. To further improve the timeliness of information and to minimize errors in recording contributions, the update process that records contributions in the accounts is being run more frequently and numerous controls have been put in place to ensure data integrity. In addition, a new procedure, which will be introduced in August 2009, will improve the accuracy and timeliness of the accounting entries associated with receipts and considerably reduce the number of deposits that are made into suspense accounts. These measures are expected to fully resolve the problems that caused the errors in the 2008 accounts and eliminate the risks that were identified.

25. As regards uncollectible contributions receivables, UNHCR's experience has proven that receivables are collected and a provision is not deemed necessary; however, UNHCR will review its policy within the context of IPSAS implementation.

D. End-of-service and post-retirement benefits liabilities

26. The Board reiterates its recommendation that UNHCR set up specific funding for its accrued end-of-service and post-retirement liabilities, notably the latter.

27. UNHCR acknowledges the risk of carrying forward liabilities that the organization may be unable to fund when they fall due. To manage this risk, UNHCR is committed to elaborating and implementing a plan of action to address the situation. In the progress report (EC/60/SC/CRP.16) presented to the Standing Committee at its 45th meeting in June 2009, UNHCR outlined the background, some possible funding approaches, the amount of the funding gap, and the Office's proposed funding strategy, with regard to end-of-service and post-retirement liabilities. UNHCR is now seeking feedback from Member States in the form of bilateral discussions.

28. Within the next few months, UNHCR expects to be informed of the strategy being adopted by the United Nations at the central level and will then be in a position to formally submit a funding proposal to the Standing Committee in June 2010, for application in the budget of the next biennium.

III. CONCLUSION

29. UNHCR gratefully acknowledges the assistance of the Board of Auditors in identifying the enterprise-level risks to which the organization is exposed. The root causes of the errors in recording contributions have been identified and solutions have been put in place to avoid recurrence in the future. The weaknesses observed in the management of property plant and equipment are expected to be addressed as part of the IPSAS implementation in 2010, and a solution to fund the end-of-service and post-retirement liabilities is expected to be submitted to the Executive Committee in October 2010.

30. During 2007, 2008 and 2009, UNHCR has made extensive and protracted efforts to resolve the problem of non-compliance with the audit certification process and to follow up on qualified audit opinions. Although progress has been achieved, the risks have not been entirely eliminated. Unfortunately, many of these risks are inherent in the very nature of UNHCR's operations, and the Office is fully aware that some measure of risk is unavoidable in order to efficiently carry out its mandated responsibilities. It is a challenge for UNHCR to strike the appropriate balance between maximizing its operational effectiveness and minimizing the financial risks the organization exposes itself to by not having complete compliance to its internal control framework. UNHCR is nevertheless committed to reviewing this framework to ensure that it provides the right balance of cost, effort and risk.
