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RESOURCE MANAGEMENT

(b) Accounts and audit: accounts for the first calendar year of the twenty-second financial period and transfers within the 2002 budget

Corrigendum

Note by the Secretary-General

Please replace pages 13-16 of Annex 1 of C 90/17(b)/Add.2. with the attached, which corrects an omission of paragraphs 88-90 and repeated text of paragraphs 86-87.

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system of classification to regulate the recording of expenditure and obligation in the programme budget accounts.

Audit Objective and Scope:

86. In the previous biennium 2000-01, we had highlighted the incidence of '*Net*' basis of budgeting as compared to the '*Gross*' basis of budgeting prescribed in the Financial Regulations. It was also pointed out that as a close corollary to this practice, budgets of Income were not being presented fairly by the IMO Secretariat before the Assembly, thereby providing a cushion for extra expenditure.
87. An audit was carried out in the current audit year to examine whether the budgetary practices and guidelines, program formulation and accounting processes, in IMO, were in accordance with the Financial Regulations and whether the same were in the best interest of member states. We felt it was particularly relevant to carry out a review of the existing budgetary practices as IMO is currently embarking on a transition to *zero based budgeting* with effect from the biennium 2004-05. Incidentally, in the wider UN system, programme budgeting has been replaced by results based budgeting for some years and there are already Joint Inspection Unit (JIU) critiques of the results based budgeting process available for guidance.

Audit Findings and Recommendations

88. IMO switched over to Programme Budgeting in 1998, that is, with effect from the Work Programme and Budget relating to the Biennium 1998-99. Prior to 1998-99, IMO was preparing its budget on the basis of object-of-expenditure. As a preparation for this transition, the Financial Regulations of the organisation were revised to include the requirements of programme budgeting and programme accounts.
89. A natural corollary to this transition would have been the framing of detailed financial rules in accordance with FR 10.1 and Financial Rules 111.3 to establish a uniform system of programme budgets and classification to regulate the recording of expenditure and obligation in the programme budget accounts. The Chart of Accounts was reviewed and revised with effect from 1st January 1998 to capture classification of expenditure details in accordance with the revised budgetary process. However there was ambiguity in the definition of Programme Codes *relating to Publishing Services, IT services and procurement of goods and services*. Moreover, there was no reference to sub-programmes.
90. At the time of the audit, apart from the General Fund and Working Capital Fund, five other funds existed, viz., Printing Fund, Technical Cooperation Fund, Headquarters Capital Fund, Termination Benefit Fund and Training & Development Fund. The audit observed that Expenditure from these five funds was not subjected to the rigour and discipline of the Work Programme and Budget, except for expenditure from the Printing Fund, which followed procedures, albeit inadequately. Assembly approves the transfers into these Funds at each Assembly session. However, the actual allocation is approved by the Council.
91. Financial Rule 101.1.2 categorically states that the Financial Rules are applicable to all officials and, irrespective of the source of funds, to all financial transactions of the organization. Flowing from this provision, the Financial Rule 103.1.5 applies to the all the Funds, which *inter alia*, states that a statement of the estimated expenditure shall be provided under each Major Programme and Programme; for purpose of comparison, the

appropriations for the current financial period shall be indicated alongside the estimates for the ensuing financial period.

92. *The Secretary General has stated that the management recognizes the need to present the activities under these funds in a programme structure and intends to build these developments into the Work Programme and Budget for the biennium 2004-2005.*
93. *The Secretary General has also stated in his reply that it is also planned that the relevant schedules of appropriations against the out-turn level under each fund will be included in the final accounts although timing will depend upon the prospective acquisition and implementation of new financial planning and accounting system.*
94. The Secretary General has stated that these five funds were established directly by the Assembly and form part of the General Fund and are administered within the scope of Organisation's Financial Regulations and Rules. The Secretary General has also stated that scope and limits of the funds is defined in the Assembly Resolutions establishing the various funds. The audit, however, observed that although the Technical Cooperation Fund has formal rules of operation, none of the other four funds (PF, HQCF, TBF and TDF) have formal rules of operation attached to them.
95. *Considering that the separate funds have been created through Assembly Resolutions, I recommend that formal Rules of Operation be framed for the Printing Fund, Headquarters Capital Fund, Termination Benefit Fund and Training & Development Fund.*
96. The audit observed that IMO does not have any Budget Manual to regulate the preparation of the Work Programme and Budget in a consistent manner. A written guidance in the form of a duly documented Manual is an essential precondition for financial administration of the budget, as it permits the definition of important components like programme, sub-programme, output etc and the identification and development of control objectives for each operational segment so that the same are appropriate, reasonable, comprehensive and integrated into the overall organisational objectives. Audit also felt that the definition of important concepts needed to be introduced in the Manual so that arbitrariness in interpreting them could be avoided.
97. *The Secretary General has agreed to the formulation of Budget Manual by the end of 2003 and a glossary of terms would be included in the Budget Manual*
98. The concept of direct and indirect costs was introduced into the programme budget by showing direct costs on staff in the General Fund and by showing indirect costs under the five other Funds, which have been created by transfers of resources from the General Fund. While the Direct Costs follow the rigour and regimen of the Work Programme and Budget, the indirect costs are being excluded from the same. Rule 3.017 of the UN Finance Manual permits for purpose of information, the apportionment of common costs across all substantial programmes. This could be undertaken separately for the purpose of management information with respect to the sub-programme 'General operating expenses and headquarters premises' and the apportionment of such overheads to all major programmes.
99. The management in its reply has stated that the process of apportionment has not been possible largely because of the weak functionality of the Organization's current accounting system as the apportionment and distribution of indirect costs would require a more agile accounting system. *The management has stated that it is envisaged that the prospective new financial planning and accounting system would provide the necessary functionality.*

100. In response to the audit observation on non-compliance with disclosure requirements under UNSAS 8 while reporting in the financial statements, the Secretary General has replied that a detailed commentary on budgeted expenditure and out-turn for the Printing Fund and Headquarters Capital Fund is in the Financial Report of the Secretary General.
101. *Since the information is already available with the management of IMO, I recommend that the same could be made a part of the Financial Statements of IMO instead of the Financial Report of the Secretary General. In addition, the expenditure details from the Training & Development Fund and Termination Benefit Fund should also be disclosed in accordance with UNSAS 8.*
102. Under the provision 6(c)(iii) of the Additional terms of reference governing the External Audit, the External Auditor should bring to the notice of the Assembly expenditure likely to commit the Organisation to further outlay on a large scale. *This issue was raised with the Management for the year 2001 in relation to MANNET Recommendations. The issue was, however not brought before the Council in the year 2001.* In the current year, as several matters raised by Audit are expected to be resolved by the Secretary-General's 'Change Management Programme' consequent upon the MANNET and Deloitte & Touche reviews and also considering that a replacement of the existing EDP systems by a more modern and robust EDP system is an integral component of such changes, we are of the opinion that these measures are likely to entail substantial expenditure, and should be brought within the due process of financial administration set out in the Financial Regulations. Presently this expenditure is being variously met from the Headquarters Fund and the Training and Development Fund, and is kept outside the formal process of Work Programme and Budget.
103. *I accordingly recommend that the management may consider including the 'Change Management Programme' as a distinct Work Programme with clear sub-programmes in the Budget for the biennium 2004-2005.*

Performance Reviews of Technical Cooperation Division and Printing & Publishing Activities of IMO

Printing and Publishing Activities

104. The major areas of concern, which were addressed in the performance review of Printing & Publishing Activities, were costing of publications, pricing policy, cost-effectiveness of in-house printing and the non-maintenance of Trading and Profit & Loss accounts on a commercial basis. In the absence of any recent evaluations regarding the performance of Printing & Publishing Activities of IMO, some reliance was placed on the report of a study conducted in 1997 by an external consultant, which had suggested that there were some serious problems with the Division. Management is of the view that since the report was now six years old and pre-dates radical changes implemented in the working practices of the Organization's printing and binding unit, the report was not an appropriate reference point for the Publishing Services' activities in 2003.

Technical Cooperation Division

105. The major areas of concern, which were addressed in the performance review of Technical Cooperation Division, were stewardship of the ITCP, reliability and fairness

of reporting to the legislature, financial administration of the TC fund, definition of target groups, areas at risk and programme delivery.

106. The performance audits were conducted during the course of the external audit and audit observations and recommendations were issued to the management as a part of the Draft Management Letter.
107. The Secretary General has stated that the research of the external audit had not taken full account of the 'work in progress' consequent upon the MANNET and Deloitte and Touché reviews. Considering the comments of the management, I propose to study further the Technical Cooperation Division and Printing & Publishing Activities of IMO during the course of the year, taking into account the 'work in progress'.

Frauds and Presumptive Frauds

108. The Secretary General in his Letter of Representation has stated that there were no cases of fraud and presumptive fraud in the year 2002 in IMO.
109. In my audit report for the financial year 2001, I had recommended that suitable procedures be introduced so that a reasonable assurance is available on these matters to the governing legislative bodies and external agencies. In response, IMO management have stated in their compliance report that a fraud-risk assessment will be incorporated into the IOS work programme.

Acknowledgement

110. I gratefully acknowledge the assistance rendered to my audit team by the Management.

(Vijayendra N. Kaul)
Comptroller and Auditor General of India
External Auditor