COUNCIL
89th session
Agenda item 19(b)

C 89/19(b)/Add.1
1 November 2002
Original: ENGLISH

RESOURCE MANAGEMENT

(b) Review of the final accounts and audits for the twenty-first financial period, including the report of the Working Group

Note by the Secretary-General

SUMMARY

Executive summary:	This document reports on the outcome of the work of the Council Intersessional Working Group on Accounts and Audit, convened by the Council at its eighty-eighth session.
Action to be taken:	Paragraph 4
Related documents:	C 88/18(b), C 88/18(b)/Add.1; C/ES.21/13; C/ES.21/13/Add.1

Introduction

1 The Council will recall that at its eighty-eighth session, it decided to reconvene the Council Intersessional Working Group on Accounts and Audit to consider the Report of the External Auditor on the Organization's Accounts and Audit for the twenty-first financial period. The Council decided that the Group would have the same terms of reference established for the Group's consideration of the Accounts and Audit for 2000, namely, to give advice to the Council on:

(i) the recommendations contained in the audit reports on the smooth running of the Organization;

(ii) the recommendations contained in the audit reports on the financial administration of the Organization;

(iii) the relevance of certain of the recommendations and the level of the detail of the information contained in the audit reports; and

(iv) the rules and regulations governing the audit,

with the addition of a review of the progress made on the implementation of the recommendations agreed in respect of the 2000 audit.

2 The Group met on 15 October 2002 and the following Member States were represented:

Argentina	Panama
Bahamas	Philippines
Brazil	Singapore
Canada	Spain
Cyprus	Trinidad and Tobago
Germany	Turkey
India	United Kingdom
Italy	United States of America

3 The Secretary-General is pleased to attach the report of the Group's work. The Council will note that the Group reviewed and concluded to its full satisfaction, on each of the recommendations made by the External Auditor.

Action requested of the Council

4 The Council is invited to take note of the report of the Council Intersessional Working Group on Accounts and Audit. The Council is further invited to take note of the Financial Statements, including the notes to the accounts and the External Auditor's Opinion and Report, for the twenty-first financial period 2000-2001 and the IMO/UNDP accounts for the year ended 31 December 2001, and to forward them with its recommendation for approval to the twenty-second session of the Assembly.

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ANNEX 1

Report of the Council Intersessional Working Group on Accounts and Audit (Final Accounts for the twenty-first financial period)

1 The Council Intersessional Working Group on Accounts and Audit met on Tuesday, 15 October 2002 at IMO Headquarters. The following Members of IMO were represented at the session:

Argentina	Panama
Bahamas	Philippines
Brazil	Singapore
Canada	Spain
Cyprus	Trinidad and Tobago
Germany	Turkey
India	United Kingdom
Italy	United States of America

2 Mr. John Mervyn Jones (Bahamas) had been reappointed as Chairman of the Working Group by the Council at its 88th session. The External Auditor was represented at the Group's session on 15 October by Mr. P.K. Brahma (Deputy Comptroller and Auditor General), Mr. A.K. Thakur (Minister (Audit)) and Mr. S. Raman (First Secretary). The Group very much appreciated their attendance.

Background

3 The Group recalled that the Organization's accounting period covered two years. The Accounts and Audit Report before the Group, therefore, comprised the 2001 Final Accounts and the biennium 2000-2001. The Group took note with appreciation, of the Secretary-General's report that the financial accounts showed (Table 1 of C 88/18(b)), after taking account of the supplementary estimates voted by the Assembly at its twenty-second session in November 2001, that the biennium 2000-2001 ended with a surplus of £250,148. This represented 0.6% of the biennium appropriation. The Group also welcomed the Secretary-General's explanations concerning the substantially improved interaction between the Auditor and the Management concerning the management of audit queries. The Secretary-General noted that, for the first time, all Directors had been involved in the audit process. Some 84 audit queries had been raised (some with sub-sets of ten questions). During the audit period, some 40 queries had been resolved and the Auditor's Management Letter had set out 45 queries or observations, of which over half had been resolved. As a consequence, this process had led to the Auditor's report, which included some ten recommendations. The Secretary-General had provided Council with his response to each of these. The Group welcomed the Secretary-General's positive action and expressed its appreciation to the External Auditor for the positive developments.

ITEMS (i) AND (ii) OF THE COUNCIL MANDATE

(i) The recommendations contained in the report on the smooth running of the Organization

(ii) The recommendations contained in the audit reports on the financial administration of the Organization

4 The Group is again pleased to report that it addressed each of the recommendations contained in the audit report on the same basis which the Group adopted at its meetings in 2001. The table attached to this document provides a summary of the Secretary-General's responses and the Group's conclusions. The presentation of the Group's consideration of the recommendations has followed the presentation of the External Auditor's report, namely, to review first the recommendations contained in the audit report on the financial administration of the Organization and second, to review the recommendations contained in the report on the management of the Organization. Accordingly, the attached table provides the Group's response to items (i) and (ii) of the Council's mandate in reverse order.

5 The Group has concluded on each of the recommendations and is therefore pleased to invite the Council to submit the Organization's Final Accounts for the twenty-first financial period 2001-2002 to the twenty-third session of the Assembly with this report for the Assembly's approval, together with the accounts relating to the IMO's activities as a participating and executing agency.

Financial administration

6 The Group noted that there were two main linked issues in the recommendations concerning the financial administration of the Organization. The Group in particular welcomed the Secretary-General's proposal to present the Organization's budget and appropriation on a 'gross' basis rate rather than the present 'net' basis. This change was in line with general UN practice and provided a more transparent basis for expenditure control. An example of the two bases of presentation are shown as an annex to this document.

7 The Working Group noted in this connection that the External Auditors had recommended that the estimation process in respect of the forecast made of miscellaneous income, including forecast income from 'support costs' paid by donors as a contribution to the Organization's overheads from technical co-operation projects, should be reviewed. The Group generally supported the Secretary-General's practice of erring on the side of caution in the estimating process, noting that this could and did lead to budgetary surplus. The Group also noted that such budgetary surpluses added to the Organization's accumulated reserves which would either be returned to the Membership directly or, as was the practice, transferred with the Council and Assembly's approval and endorsement, to the various Funds of the Organization. However, the Group welcomed the Secretary-General's intentions to increase the transparency in the estimating process in respect of Trust Fund income flows and to thereby assist in improving the levels of accuracy so far as practicable. The Group noted that the Secretary-General would take account of these points in presenting the Work Programme and Budget for 2004-2005.

Management

8 The Group noted that only two recommendations had been made relating to Management issues and that one in particular, was of material concern both to the staff and to the Membership which concerned the rising costs of health insurance for the Organization's staff members.

9 The Group recognised the global increase in the costs of healthcare cover and that the Organization's Medical Insurer (Van Breda) had forecast an increase of some 40% in the premium levels, with effect from 1 January 2003. The Group noted the reasons for the increase in premiums and acknowledged that London in particular, attracted high medical costs. The Group generally concluded that Health Care coverage was an essential part of the Organization's 'total benefits' package for staff members and therefore was sympathetic to the representations which had been made by the Staff Association to the Group, and explained by the Director of Administration, that the balance of contribution between the individual staff member and the Membership should be reviewed urgently in view of the significance of the premium increase. The Group invited the Administration to discuss with the Staff, possible options for ameliorating the impact of the prospective increase in the premiums, which could be reviewed by the Council at its forthcoming eighty-ninth session.

Other issues

10 The Group recalled the Secretary General's decision to form an Internal Oversight Section (IOS) in 1998 which the Council had endorsed. The Group welcomed the Secretary-General's proposal to address the functions and responsibilities of the IOS and to specify and strengthen these in the Organization's Financial Regulations and Rules. The Group welcomed the planned submission of detailed proposals to the forthcoming November Council for consideration.

11 The Group welcomed the External Auditor's and the Secretary General's commitment to the achievement of a closer interaction between the two functions in determining and in delivering their respective work programmes so that duplication could be avoided.

12 The Group also noted the External Auditor's recommendation concerning the reporting arrangements for IOS and generally concluded that the IOS should provide the Secretary General with the appropriate assurances concerning Management's compliance with the Organization's Financial Regulations and Rules. The Group did not consider it necessary, at this juncture, to institutionalise the ISWG as an Audit Committee, which remained a function of the Council.

ITEM (iii) OF THE COUNCIL MANDATE

(iii) Review of the relevance of certain of the recommendations and the level of the detail of the information contained in the audit reports

13 The Group recalled that the form and content of the Report was a matter for the External Auditor who was guided by both general standards and International Audit UN practice.

14 The Group welcomed the evident attempt which had been made in the consultation process between the Secretary-General and the External Auditor to reduce the number of apparently unresolved items which was shown by the significant reduction in the issues on which recommendations were made.

15 The Group further noted that the Audit Report, in accordance with general international auditing standards, provided general information to the Council on certain general aspects of the Organization's finances as well as making specific recommendations, in order to help the Council and Assembly discharge their governance responsibilities.

16 The External Auditor noted sympathetically, the Group's suggestion that comments 'for information' and of a general nature could be so annotated in the Audit Report.

ITEM (iv) OF THE COUNCIL MANDATE

(iv) Review of the Rules and Regulations governing the Audit

17 The Group noted that, so far as the External Auditor's terms of reference are concerned, no issues were raised during the course of the 2001 audit and welcomed this. It was noted that the External Auditor's terms of reference were not IMO specific and that the reporting followed international auditing standards.

ADDITIONAL ITEM OF THE COUNCIL MANDATE

Review of the progress made on the implementation of the recommendations agreed in respect of the 2000 accounts

18 The Group noted that the External Auditor had provided a summary in his Audit Report (C 88/18(b)/Add.1(Annex 1)) of the action taken by the Secretary-General to implement those recommendations which had been accepted in respect of the 2000 Accounts. The Group noted, with appreciation, the progress report of action which had been taken to implement those recommendations accepted in respect of the 2000 Final Accounts and looked forward to completion of the 'work-in-progress' issues, in time for them to be reflected in the Accounts for 2002.

Conclusion and recommendations

19 The Group decided that it had concluded to its full satisfaction on each of the recommendations of the External Auditor, taking into account the Secretary-General's response, and had fulfilled its mandate.

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Audit Recommendations	Secretary-General's Response	Working Group Conclusions
Budget and Appropriation **Paragraphs 9-12:** Presentation of Budget inconsistent with Financial Rules 9. According to financial rule 103.1, the budgetary estimate for expenditure and miscellaneous income shall be prepared on gross basis. The Zero Nominal Growth (ZNG) budget for the biennium 2000-2001 was, however, prepared for the net appropriation level of £36,612,200 (after adjusting 'reimbursement of technical support costs') to maintain the Work programme and Programme Budget at the net appropriation level for the biennium 1998-99. Miscellaneous income excluded from the budget 10. The ZNG budget, at the net appropriation level had not projected estimates for receipts to the General Fund like miscellaneous income and transfers from Printing Fund. Thus, even though the budget was claimed to have a zero nominal growth, in effect there was an in-built cushion for extra expenditure due to the exclusion of these items. 11. The Secretary-General stated that in accordance with the recommendation of the Council Intersessional Working Group (CIWG), the UN general practice for support cost income from project activities was reviewed leading to the conclusion that the support cost income should be credited to miscellaneous income	The Auditor made a similar recommendation in 2000 concerning the preparation of estimates on a gross basis. The Secretary-General advised the Council Intersessional Working Group that he would review the Organization's past practice, with particular reference to the United Nations' policy and practice and that of the Specialized Agencies. The Secretary-General has completed that review and can report to the Council that the UN general practice is for support cost income from project activities to be credited to an Organization's miscellaneous income, as a receipt, and not to deduct the income from gross expenditure. The Secretary-General can advise the Council, therefore, that in future presentations of the Work Programme and Budget and the accounts relating thereto, the appropriation will be presented and voted on a gross basis, in conformity with financial rule 103.1. The change will be neutral in assessment terms, although there are transitional consequences in terms of presenting biennium to biennium appropriation changes.	The Group welcomed the Secretary-General's response to this recommendation and its planned implementation in the Work Programme and Budget from 2004-2005.

instead of deducting the income from gross expenditure. It was, however, stated that in future presentations of the Work Programme and Programme Budget and the accounts relating thereto, the appropriation would be presented and voted on a gross basis, in conformity with financial rule 103.1.		
12. I appreciate the Secretary-General's efforts with reference to presentation of support cost income in future, on a gross basis, to be credited to miscellaneous income as per the general practice followed by UN agencies. However, as the miscellaneous income itself is not shown in the Budget, I feel that the issue pointed out by me is yet to be addressed. I recommend that the project miscellaneous income should be included in the Work Programme and Programme Budget.	The recommendation concerning the inclusion of projected miscellaneous income in the Work Programme and Budget is not correct. It is the Organization's long-standing practice to include miscellaneous income in the Work Programme and Budget presentations in order to arrive at the assessment level on the Member States of the Organization.	
Paragraphs 13-15: Underestimation of income leading to over-assessment of contributions from members 13. As reported to and approved by the Assembly, the net appropriation of £36,612,200 for the biennium 2002-2001, which was already reduced by way of 'reimbursement of technical support costs amounting to £44,400' was further reduced by miscellaneous income and transfers from the Printing Fund, estimated at £280,000 and £400,000 respectively to decide the contributions to be assessed from member countries for the biennium. Against the projected income of 'reimbursement of technical support costs' and 'miscellaneous income', the actuals	The Secretary-General has noted the Auditor's recommendation concerning the need to set the level of prospective support cost income at a realistic level. The Secretary-General would recall that the prospective receipts from support costs are less certain than contribution income; they depend on a continued level of donor funding and assumption of delivery level. The Secretary-General has therefore consistently taken a prudent approach, particularly given the Organization's relatively fixed cost structure which would make it difficult to shed costs, if	The Group generally supported the Secretary-General's prudent approach to estimating miscellaneous income and particularly prospective support cost receipts. The Group noted and welcomed the Secretary-General's intention to further increasing the transparency of the Budget from 2004-2005, which will also help towards improved forecasting levels.

were £820,605 and £1,101,765 indicating significant escalation at 83% and 293% over the budget estimates for these two items. I am of the view that as the assessments once made from member countries are not being revised subsequently after obtaining 'actual' figures, contributions from members are being over assessed. 14. The Secretary-General stated that the prospective support costs were less certain than contribution income and they depended on a continued level of donor funding and assumption of programme delivery level. It was further stated that the Organisation's interests were well served by adopting a conservative approach in the estimation process. 15. I recommend a review of the income estimation process in view of the actual receipts being significantly higher than the estimates so that the contribution assessments of the member countries are fair.	support costs fell below the budget levels. In these circumstances, the Secretary-General considers that the Organization's operational interests are best served by erring on the side of caution in the estimating process. The Secretary-General would also note that, since contribution receipts can fluctuate, the Organization's cash flow is additionally vulnerable.	
Paragraph 16: Trust Fund activities excluded from the Budget 16. The net budget appropriation for the twenty-first financial period ended 31 December 2001 was at £36,612,200 for the regular budgetary activities of IMO. The total expenditure incurred on the extra-budgetary activities financed by Trust Funds from donors for the same period was at £14,067,864. Thus, the expenditure on Trust Fund activities was significantly at 38% of the	The Secretary-General will examine the feasibility of incorporating prospective support cost income flow from Trust Funds managed by the Organization, within the scope of the Work Programme and Budget for 2004-2005	The Group noted that Trust Funds are extra budgetary contributions from multi-lateral or bilateral donors who have specific institutional reporting requirements for their accounting and financial purposes. The Group noted that the financial management of Trust Funds is regulated by the Organization's Financial Regulations and Rules. The Group welcomed

budgeted appropriation for the regular budget. For these extra-budgetary activities, as IMO is the monitoring agency and as such activities have contributed significantly to income by way of programme support costs amounting to £82,605 during the biennium 2000-2001, I recommend that the Council may consider the desirability of bringing the Trust Funds under regular budget discipline so that the overall performance of IMO could be monitored and measured with reference to budget projections.		the Secretary-General's response which will represent a further contribution to increasing transparency.
Paragraph 17 **Financial Statements** <u>Representation by the Secretary-General</u> 17. The Management stated that the form and contents of Representation issued by the Secretary-General had been agreed with the previous auditors and was being followed. It was however stated that the additional representation relating to the maintenance of internal controls for ensuring that the financial statements were free of material mis-statements would be included in future Letters of Representation.	The form and content of the Letter of Representation issued to the External Auditor was agreed with the previous External Auditor of the Organization. A Letter of Representation issued in respect of the year 2000 accounts was similar in content and the form and was accepted by the current External Auditor. Therefore, a similar Letter of Representation was issued in respect of the year 2001 accounts. The Secretary-General has taken note of the External Auditor's comments and the new requirements will be included in future Letters of Representation as notified by the External Auditor.	The Group took notice of this item which required no action on its part.

Paragraphs 18-19: Maintenance of property records 18. As per financial rule 110.6.2, property records for all real property, non-expendable and expendable supplies and equipment have to be maintained containing full details. Management has neither produced records relating to maintenance of property nor has it provided us with evidence regarding its physical verification. 19. According to financial rule 110.6.3, an annual physical verification has to take place at 31 December of each year of all assets, supplies and materials in hand and a copy of the same has to be furnished to the External Auditor. The physical verification Report for non-expendable assets at 31 December 2001 has not been produced to audit. The management stated that so far as the value of the fixed assets is concerned, the process of physical verification of fixed assets has not yet been completed and the figures in the accounts have been based on the Statement for 2000, assuming that new investment is writing-off the replacements. It was also stated that a complete evaluation would be taken within the coming weeks so that the full disclosure of the inventory and its value would be provided to the Council at its 89th session.	The process of completing the physical inventory using a new Inventory Management System is in hand. In order to ensure that the Inventory is both comprehensive and valued in accordance with the United Nations Accounting Standards, and updated systematically, the Administrative Division has commissioned Deloitte & Touche to review the current processes as part of the “Interim Solution” for strengthening the Organization’s financial systems. This will ensure that the accounts for 2002 will have a full and transparent record of its capital assets at 31 December 2002 and that there is in place, a dynamic system.	The Group took note that an inventory of the Organization’s assets will be drawn up in accordance with the Organization’s Financial Regulations and Rules for presentation to the External Auditor, as part of the 2002 accounts and which will take account of disposals as well as acquisitions.

Paragraphs 20-21: Accountal of Receipts 20. Financial rule 111.1.3 states that the receipts shall be credited to the accounts of the calendar year in which the remittance is received indicating that the income accrued during the year but received during subsequent financial periods is not accountable during the current year. According to the said rule, the refund of £415,672.42 received from the Valuation Office, United Kingdom during February 2002 is not accountable as received during the year 2001.	The Secretary-General agreed with this observation and agreed to amend financial rule 111.1.3 in line with UN Accounting Standards. As advised in the Secretary-General's reply to the External Auditor's Management Letter, the refund due from the Valuation Office, United Kingdom, was fully disclosed to the IMO Council at its 21st extraordinary session in November 2001 and the Council, at that session, approved the utilisation of this miscellaneous income to meet the supplementary estimates approved by the Council. The refund was shown in the accounts for 2001 as accrued income in accordance with the United Nations Accounting Standards and in accordance with the Organization's long-standing practice, in respect of all the Funds of the Organization, namely the regular budget, Trust Funds and the Printing Fund. However, the Secretary-General has already agreed that the operative financial rule 111.1.3 is not consistent with the Organization's long-standing practice, nor the United Nations Accounting Standards and that he will take steps to make the necessary amendments to the Organization's Financial Rules.	The Group welcomed the Secretary-General's proposed amendment to financial rule 111.1.3 and noted that a draft text had been circulated to the Council's forthcoming 89th session (C 89/22).

Paragraphs 22-23: Disclosure of stores and cash losses 22. Regulation 10.4 of the "Financial Regulations" states "the Secretary-General may, after full investigation, authorise the writing off of losses of cash, stores and other assets, provided that a statement of all such amounts written off shall be submitted to the Auditors with the accounts." Financial rule 111.5.1 (d)(vii) further provides that such losses should be presented in the form of statements indicating how these have been dealt with in the Accounts. 23. For the year 2001, a proposal for writing-off publications having a sale value amounting to £120,870 (production cost of the above items valued at £24,000 approximately) comprising damaged and obsolete stocks amounting to £10,173.50 and £11,069.50, respectively was submitted by the Publishing Service, on 12 March 2002. The proposal was approved by the Secretary-General (March 2002). However, disclosure under note no. 64 of the Accounts regarding a proposal for writing-off did not include damaged stock valued at £10,173.50.	As advised in the reply to the Management Letter, write-off approval by the Secretary-General will be provided to the External Auditor and disclosures will be made in accordance with the Financial Regulations and Rules. The necessary approvals will therefore be obtained in respect of the final accounts for 2002.	The Group took note of and welcomed the Secretary-General's response.
Paragraphs 24-28: 24. The Secretary-General subsequently stated (May 2002) that the write-off approved consisted of a value of obsolete stocks at £235,395, damaged stocks at £9,308 and shortages at £10,858 totalling £255,561.25. It was also stated that action would be taken to provide the	As noted above	As noted above

approval to the write-off to the External Auditor and to place appropriate disclosures in the Notes to the Accounts' in accordance with the Financial Regulations and Rules.		
25. Similarly, for the year 2000, publications valued at £226,016.25 consisting of obsolete, damaged and stock shortage of £219,999, £548.25 and £5,468.50 respectively, were written-off (April 2001). These write-offs of publications, as approved, were not disclosed in the accounts for the financial year 2001.		
26. I recommend that the disclosures for write-off approved by the Secretary-General be made in the accounts of the related year in accordance with the provisions of the Financial Regulations.		The Group took note of and welcomed the Secretary-General's response.
<u>Unliquidated Obligations</u> 27. For one of the projects of the Technical Co-operation Fund under implementation in Samoa (South Pacific Regional Environment Programme (SPREP), vide project TC03RAS/00/320), the expenditure of £18,943 up to December 2001 was not shown as cash expenditure and a lump sum provision at £26,200 was shown in the accounts for the year 2001 on an estimated basis.	The Secretary-General accepted the over-provision of unliquidated obligations and agreed to make necessary adjustment in the accounts of 2002. As advised in the reply to the Management Letter, adjustments for overprovided, unliquidated obligations will be made in the accounts of 2002.	
28. In respect of Trust Fund, DO029, the unliquidated obligation as at 31 December 2001 amounting to $11,511 was raised for the gross amount for web development charges payable for the period 24th September 2001 to 30th		The Group took note of and welcomed the Secretary-General's response.

November 2001 instead of at the net amount after deducting the VAT payable amounting to $2,338.		
Paragraphs 30-31: Contributions 30. The main resources for regular budget activities are mobilised by way of annual contributions from member countries. 31. I appreciate the vigorous steps taken by the Management to achieve a high rate of collection at 98 percent of the assessments made for the year. However, as at 31st December 2001, contributions receivable including arrears pertaining to earlier assessments amounted to £2,145,858.	As reported to the External Auditor, the Council had proposed establishing a Working Group to review Member States' arrears of contributions and, in particular, to assess the prospects of payment by those Member States with long-standing arrears. Since that advice to the External Auditor, the Council decided to defer the matter. In the meantime, three Member States have settled long-standing arrears.	
Paragraphs 32-34: 32. It would be seen from the above that substantial amounts of contributions receivables relate to the period 1988-1999. IMO has in place an incentive scheme to encourage the early receipt of contributions from Member States. The Secretary-General stated that the Council at its 21st extraordinary session decided to establish a working group to review Member States' arrears of contributions and in particular to assess the prospects of payment by those Member States with long standing arrears.		The Group noted that this recommendation was effectively addressed to the Council itself. The Group recalled that the Council, at its forthcoming 89th session in November 2002 would revert to the matter, which was of enduring concern to the Council.

Trust Fund activities 33. There were 43 Trust Funds comprising 72 projects as at 31st December 2001. A review of the closing balance of Trust Funds revealed that there were minus balances in respect of 10 funds. 34. In respect of UNDP projects, the Management stated that the positive balance of $3,560,120 on the main UNDP accounts counter balanced the deficit under these Trust Fund Accounts and these inter fund balances were cleared by transfer entries after finalisation of accounts. For the minus balance in UNEP, the Management stated that the funds release was delayed due to their year-end closure process and the funds were normally received in the beginning of the new financial year to clear any deficit. In the case of World Bank also, it was stated that the remittances, apart from the initial payment follow programme deliveries. In respect of a minus balance in another Fund relating to the United States, the Management stated that they received $15,000 during February 2002 and for the balance, discussions were ongoing. In respect of other minus balances, either the balance was small or action taken subsequently, by the Management. The Management further stated that the project delivery reports, interim accounts and final accounts were submitted to donors and the attention of the donors was drawn to the minus balances to remit funds in accordance with the project agreements.	In his reply to the Management Letter, the Secretary-General fully disclosed the basis for the negative balances. The major negative amount of $3,528,911 posted against the UNDP, represents a book transaction of the UNDP Operating Fund account with respect to the GEF Trust Funds accounts of the Manila (PEMSEA) project. The majority of PEMSEA transactions are made through the UNDP field offices and cleared in UNDP, New York on closure of UNDP Final Accounts. The balances were cleared in the New Year in line with past practice. A remittance of $1.2 million was also received to meet the current year disbursements of PEMSEA and Ballast Water projects. The negative balance of $75, 177 against the UNEP programme was caused by a delay in remitting the funds from the UNEP headquarters, Nairobi. The required funds were received in the New Year after the closure of the final accounts 2001. This practice has arisen in earlier financial periods and occurs during the intervening period of the Organization's year-end closure procedures and the approval process by UNEP of the budget for the next financial year. In the case of the World Bank and UNOPS, remittances are released only after the expenditure has been incurred or after the submission of impress accounts; the final payment is made only after the final report has been filed with the donors by the Organization.	The Group noted that the Auditor's comments on Trust Funds were for information only and that no action was required on its part. The Group noted that the Auditor's comments on Trust Funds were for information only and that no action was required on its part.

	Thus, during the project execution, a negative balance is often shown in the Organization's accounts. In accordance with the contract between IMO and OPEC the final contribution of $25,000 was due upon presentation of the final report and was duly received in February 2002.	
	In respect of the negative balance of $41,080 from the US Government, there were protracted problems with the remittance on account of bank transfer system difficulties in the aftermath of the 11 September events.	The Group noted that this balance had been fully settled.
Paragraphs 35 & 36: Closure of projects 35. During the year 2001, five funds were closed. A multi-donor fund, Review of INF Code, had an unspent balance of $4,165. The Management stated that the balance had been lying dormant for several years and the balance was credited to IMO at the end of the year 2001 as the review was co-financed by IMO. However, prior consent or confirmation for the same from the donors has not been obtained.	The relatively small balance of $4,165 in the Review of INF Code, a multi-donor fund, was credited to IMO without reference to the original donors since the amounts relating to each donor were small and the time elapsed since the completion of the project was rather long.	The Group noted that the Auditor's comments on Project Closure were for information only and that no action was required on its part.
Inactive balances 36. There was no expenditure during the year 2001 in respect of the following : U004-UNDP Sectoral Support, U005-UNDP Sub-contracts, D003-WMU Capital Fund, D010-UNEP Memoranda of Understanding, D027-Denmark and D027-Cyprus.	The largest of the "inactive " balances is £306,316 which represents the assets of the WMU Capital Fund. This account is held in London on behalf of the WMU.	The Group noted that the Auditor's comments on Inactive Balances were for information only and that no action was required on its part.

	The balances of UNDP Sectoral Support, UNDP Sub-contracts and UNEP Memoranda of Understanding will be closed in the current year. The balance of $18,971 funds was earmarked for project PR355 "Development of Port State Control Capability in Black Sea Countries" to be executed during 2002.	
Paragraph 37: 37. The Management stated that action would be taken to close the accounts since the project activities were completed.		
Paragraphs 38-39: Bank Reconciliation statements 38. The Bank Reconciliation Statement as at 31st December 2001 in respect of Barclays Bank, Sterling current account showed that 9 items of expenditure/debit by banks pertaining to periods earlier to March 2001 aggregating to £2,894 were still not recorded in the cash book due to want of details/expenditure authorisation. Similarly, in respect of NatWest Dollar Account, the reconciliation showed that 5 items of receipts amounting to £968 were not recorded in the cash book due to want of details. Some of the items	As reported to the External Auditor, these items will be cleared in the Financial Year 2002 and prompt action will be taken to obtain the necessary information from the banks to resolve these items appearing in the bank statements.	The Group noted that the Auditor's comments on Bank Reconciliations Statement were for information only and that no action was required on its part.

belonged to the financial year 1999 and 2000 also. 39. Management accepted to take action to clear these items in the financial year 2002 and to take prompt action, in future, to obtain necessary information from the banks to clear such items.		
Paragraph 40 Confirmation of balances 40. All the banks except M/s Barclays Bank responded to the request made by us in March 2001 to the banks concerned for independent confirmation of cash balance as at 31st December 2001. The Management has agreed to pursue with the Bank for furnishing the standard reports expeditiously.	Barclays Bank has confirmed that they have responded to the External Auditors directly on this matter.	The Group noted that the Auditor's comments were for information only and that no action was required on its part.
Paragraphs 41-48 Management Issues Leave records As a result of inaccuracies in the maintenance of the leave accounts, the Organization had to pay for an excess of net 151.15 days of leave to the staff in the cases of staff separated from service during the biennium 2000-2001. Management is yet to calculate the financial implication involved to obtain the formal approval of the Secretary-General for the write off of this excess payment in terms of the financial regulations.	The procedures in place for the approval and monitoring of annual, sick and special leave are currently based on a manual recording system. This requires a staff member to obtain the formal approval of his/her supervisor. Where applicable, an absence report is submitted by a divisional focal point if sick leave or special leave is taken. This sick leave report is routed through the Organization's Medical Unit to the Personnel Section. A separate monthly report is compiled, on a Section basis, which shows for	The Group took note of the Secretary-General's response on the matter and concluded that no further action was required on its part. The Secretary-General noted that a future Audit report would provide feedback on the improved levels of accuracy achieved by the new Human Resources system.

42. Management admitted that mistakes had occurred during the maintenance of leave records some of which pertained to periods long ago. It was further stated that the possibility of similar mistakes in the leave records of the other staff members could not be ruled out as such mistakes remained undetected until the file of the staff member was audited on separation from service. Owing to the deficiency in the maintenance of leave records, information about the inaccuracies in the leave records and the related financial implications was incomplete.	each day, absence (and type of absence) or attendance. This form is signed by the Head of Section and Divisional Director, as well as all staff members in the Section. Notwithstanding these checks and balances, clerical errors can arise (mainly arising from changes in the type of leave taken). Experience has shown, however, that the process of reconciling the individual's daily leave record with the monthly returns, on a monthly basis, is highly labour-intensive and of uncertain cost-effectiveness. The level of the error rate, on the basis of the material which was provided to the External Auditor, is less than 0.1%, as was exemplified in the Administration's reply to the External Auditor.	
Paragraphs 43-44: 43. Management stated that there was some constraint in having a periodic check over leave accounts. Management added that by the introduction of an automated computerised leave recording system these mistakes would more or less disappear in future. 44. It is recommended that the Management should prepare a comprehensive time bound plan with a view to ensuring that all mistakes in leave accounts are corrected at an early date to avoid further financial losses to the Organization.	As the Administration's replies also indicate, the Statute of Limitation in the Organization's Staff Regulations and Staff Rules sets a deadline of two years on the recovery from the staff member of over-payments. However, as a management check, the internal audit process determines, on the retirement of the staff member, the effective cost of over-payment such as an excess leave balance. The Secretary-General's write-off authority is then sought. The Administration is in the process of introducing a Leave Data-Base, which will record individual transactions and serve as a basis for monitoring and control. The database for 2002 has been operational within Personnel Section since 1 January 2002, and holds a daily	As noted above

	record of leave taken. The system also holds end-year balances from prior years. The Administration's aim is to progressively promulgate the system to staff members so that leave is applied for and approved on the Intranet, on a basis similar to the Atlas Travel System. The system, which has completed trials, will strengthen the quality of the data and reduce the small error rates. The Secretary-General does not consider it necessary to undertake a comprehensive review – which would mean the leave records of all staff members – since the exit audit of staff members on retirement or resignation entails a reconciliation of all leave with the staff members' leave records.	
Paragraphs 45-48: Payment of medical insurance premium 45. The Organization switched over from the UN Worldwide Plan to the IMO-specific group medical insurance plan with J. Van Breda & Co., International insurance and reinsurance brokers based at Antwerp, Belgium from January 1999. At that time the switchover was in the interest of the Organization as Van Breda offered better premium rates to the Organization as compared to the UN Worldwide Plan. But from the year 2001 the premia payable by the IMO increased mainly due to the high incidence of the long-term sickness and absence of the staff members. Over the years, the devaluation of Sterling vis-à-vis US dollar has resulted in further increase in the	The External Auditor correctly reports that the Organization changed in 1999, from the UN World-wide Plan to an IMO-specific plan, which secured a relatively lower premium increase in 2000 based on the Organization's expenditure: contributions performance for the period 1994-1997; and additionally negotiated a "cap" on the percentage increase which could be permitted in subsequent years. However, the increase of the premium in 2001 and 2002 has been relatively higher than the UN Worldwide Plan. This largely reflects an unexpectedly high incidence of IMO staff	The Group considered this matter extensively, which was recognized as a matter of considerable importance to the Organization and particularly the prospective impact on staff members, which the Group considered should be ameliorated as far as possible. The Group's consideration of the matter and its conclusions are set out more extensively in the Chairman's report to the Council.

premium. 46. The comparative insurance premia paid by IMO vis-à-vis those payable under the UN medical plan for the year 2001 and 2002 indicated that the premia payable by the Organization under the IMO Plan was higher than the premia payable under the UN Worldwide Plan by 13.42 per cent to 32.39 per cent for various categories of the staff. 47. As the difference in the premium payable under the UN medical plan and the IMO plan during the year 2002 is substantial, if the Administration continues to operate the IMO specific Plan during the year 2002, the extra amount spent during the year would be approximately GBP99,000. Management stated that the Administration was reviewing the long-term budgetary implications of alternative Plan policies, taking into account the actuarial implications of the age profile of IMO staff and the Council was informed of the matter. 48. I recommend that the Management may complete the review on long-term budgetary implications of alternate plan policies early and inform the Council of the matter.	members on long-term sick leave whose sickness has given rise to a high level of expenditure on medical treatment. However, whilst the Organization's aggregate expenditure on health-care treatment has exceeded the premiums paid, the terms of the contract with VAN Breda limited the increase to the cap of 15%. The increasing costs of health care are a universal phenomenon and health inflation is rising considerably faster than general inflation. The Administration is reviewing the long-term budgetary implications of alternative Plan policies, taking into account the actuarial implications of the age profile of IMO staff in consultation with Van Breda and staff interests. Preliminary research suggests that insurers to the World-wide Plan are reviewing their level of exposure in order to link to levels of premium paid by high-cost duty stations with the actual medical costs incurred. The Secretary-General will continue to keep Council informed of future developments which will, in any case, also form part of the Council's consideration of the Work Programme and Budget for 2004-2005, in June 2003.	

Paragraphs 49-51: **Miscellaneous Issues** Internal Oversight Services 49. The IOS was formed in October 1999 by merging of the Evaluation Unit and Internal Audit. The Secretary-General, in reply to a concern expressed by the Member States on the efficiency and effectiveness of oversight functions in IMO, had assured the Council at its 20th extraordinary session that a restructuring by merger of the IOS and evaluation function would provide savings as well as better oversight services. The Sub-programme for Internal Audit in the Budget Document C 82/11 for the biennium 2000-2001, provides that IOS would conduct audits to ensure: a) The accuracy of accounting, financial and other data used for management information and sound internal controls; b) Integrity and soundness of management practices; c) Economical and effective use of resources; and d) The accomplishment of established objectives and goals for operations and programmes. 50. I have noted that the audit programme of the IOS covered some high risk and key areas during the financial year 2001. However, I observed that in the audit report on "Non-expendable and Expendable Items" prepared by the IOS, replies and comments of the audited entity had not been received. Similarly, reports on "Gift Items" and "Trust Funds" were issued without obtaining	The report does not fully reflect the Secretariat's response to the External Auditor. Written comments or clarifications on the issues raised are requested by a certain auditee's response. Depending on the comments provided, further audit work or discussion may be required to clarify the concerns raised in the comments and the draft report is revised, whenever necessary. IOS is of the view that management should provide timely replies to the audit issues. Audit reports must not only be objective but should also be timely to ensure their relevance. In cases where responses cannot be provided by the requested date, it is management's responsibility to provide IOS with a written reasonable explanation for the delay so that a new deadline date can be agreed upon. In order to standardize the reply time to audit queries and draft reports, it is the intention for future audits that replies to audit queries will be requested within two weeks of the issuance of the query, comments on draft audit reports will be requested within three weeks of the issuance of the draft report with the final report including any comments of the auditee to be issued within one month of the issuance of the draft report. It will be the auditee's responsibility to inform and provide IOS with a reasonable explanation if a reply cannot be provided by the requested date so that a new deadline can be mutually agreed. The IOS has made appropriate efforts to obtain	The Group recalled that the Council has previously welcomed the Secretary-General's decision to create an Internal Oversight Section (IOS) by unifying the Internal Audit and Evaluation Office functions. The Group agreed that the IOS played an important role in securing effective internal controls and welcomed the Secretary-General's decision to define the functions and responsibilities of IOS in the Organization's Financial Regulations and Rules and which would provide a sharpened focus for the IOS.

replies from the auditee. Head IOS stated that in some cases reports were issued without the comments of the auditee, as they received no comments by the deadline date. This suggested a weak supportive environment for internal oversight. 51. Regarding non-financial reports, Management stated that IOS does not provide audit assurance on non-financial reporting by the IMO Secretariat to the council/assembly and stated that, the subject being technical in nature was beyond the power of two professional staff. Providing independent assurance on the integrity of the information provided to the Legislative bodies is an important control objective, which merits oversight coverage. **Paragraphs 52-54:** 52. I also found no reports addressed to the legislative bodies regarding the work done by IOS. As often insisted by the Joint Inspection Unit, report to the legislative bodies is of prime importance in the oversight arrangements of organisations under the UN System. The governing bodies require assistance I their oversight role over the secretariat and this role is expected to be performed by the Internal Oversight services on a systematic basis. 53. The Financial Regulations and Rules of IMO do not define the functions and the responsibilities of IOS. It is also not clearly stated in the Financial Regulations that Internal	timely responses from auditees. The draft report on "Non-Expendable" and "Expendable Property" was issued on 8 October requesting comments by 19 October. The auditee was reminded of the outstanding reply on 22 October. No reply was received and the report was issued on 22 October. Acceptance of the recommendations was received on 4 December, approximately two months after the draft report was issued. The same is true for the report on the audit of "Trust Funds" where complete comments were received only by 28 February, more than two months after the draft report was issued requesting comments by 10 December 2002. A written reply agreeing to the findings and recommendations in the report on the audit of "Gift Items" was received from Director, Administrative Division on 2 October before the report was issued on 5 October 2001, contrary to what is conveyed in the audit report. The IOS advised the External Auditor, in respect of the audit of non-financial reporting that "IOS does not provide audit assurance on non-financial reporting by the IMO Secretariat to the Council/Assembly. This is beyond the manpower of two professional staff bearing in mind that many of the non-financial documents are of a technical nature." All areas relating to the operation of IMO merits some oversight coverage, including the area of non-financial reporting. However, due to limited resources (human and financial), the various areas considered for audit have to be prioritised. This is the very essence of the annual planning	The Group welcomed the Secretary-General's and External Auditor's proposal to establish a co-ordinated work plan.

Controls would include management controls also, even though in the budget submissions before the Assembly there is a clear reference to soundness of management practices, effectiveness in resource utilisation and achievement of targets or goals. Further, according to the Financial Regulations, the responsibility for internal control is with the Director of Administration who does not have any dedicated and specialised internal control personnel under him as the Internal Oversight Services function directly under the SG. The Head IOS while agreeing with us that the functions and responsibilities of IOS were not clearly specified in the Financial Regulations, stated that it did not preclude IOS from providing assurance to the Secretary-General that the internal controls were adequate to ensure economy, efficiency and effectiveness of operations. Management agreed that the Financial Regulations would need to be revised, including the role of IOS, in the light of the recommendations of the MANNET report.	exercise. The Auditor's report implies that IOS should report direct to the Organization's legislative bodies and notes the relevance of an Audit Committee. The Secretary-General has explained that a similar idea was proposed by the External Auditor following last year's audit although the proposal was for IOS to report to Council. This was discussed by the Council Interessional Working Group on the Accounts and Audit. The proposal was not supported as it was felt that another layer of reporting was not justified, that the purpose of IOS was to assist the Secretary-General and that of the External Auditor was to report to the Council. Management agrees that the functions and responsibilities of IOS are not clearly specified in the Financial Regulations and Financial Rules and that they should be amended accordingly.	The Group generally concluded that it continued to see no case for a change in the current institutional arrangement. The Group noted that, in the United Nations the Office of the Internal Oversight Service reported, de facto, to the General Assembly, but that Specialized Agencies followed the IMO reporting model.
54. I noted that IMO does not have an Audit Committee. The UN system recognises the importance of the Audit Committee. The existence of an effective audit committee is one of the accepted criteria guiding the evaluation of Internal Audit by External Auditors in the UN system. I have duly noted that during the meeting of the Council Interessional Working Group on Accounts and Audit, the idea of Audit Committees was not found acceptable. The Management was receptive to the need for an	Accordingly, the Secretary-General does not consider it necessary or appropriate to undertake an evaluation of the role of Internal Oversight Services, as recommended by the External Auditor. The functions and responsibilities of the Internal Auditor will be defined in to the Organization's Financial Regulations and Rules, consistent with Untied Nations policy and practice. These amendments will be submitted to the Council for approval at its 89th session in November 2002.	The Group noted and welcomed the Secretary-General's proposal to define the roles and responsibilities of the Internal Auditor in the Organization Financial Regulations and Rules in a document to be submitted to Council at its forthcoming 89th session.

Audit Committee or an alternative forum such as the Intersessional Working Group, the agenda for which could include all financial matters and internal oversight. It was, however, expressed that the impact on secretarial resources would also have to be considered.		
Paragraph 55: 55. Considering the critical potential of Internal Oversight in establishing the accountability of the Secretariat of the Secretary-General and the legislative governing bodies, I recommend an evaluation of the role of Internal Oversight Division for securing substantial compliance with the assurances given to the legislature at the stage of budget approval.		
Paragraphs 56 and 58: <u>Frauds and Presumptive frauds</u> 56. & 58. I was informed by IMO that there were no cases of fraud and presumptive fraud in the year 2001 in IMO. There was, however, no evidence to suggest that any fraud-risk assessment within IMO was carried out to assess the risk of financial frauds and misuse of powers.	A fraud-risk assessment will be incorporated into the IOS work programme.	The Group took note of this response which required no action on its part.
Paragraph 57: 57. I recommend the introduction of suitable procedures so that a reasonable assurance is available on these matters to the governing legislative bodies and external agencies.		

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