



SECRETARIAT OF THE PACIFIC COMMUNITY

**FORTY-FOURTH MEETING OF THE
COMMITTEE OF REPRESENTATIVES OF GOVERNMENTS AND ADMINISTRATIONS**
(Noumea, New Caledonia, 4-7 November 2014)

AGENDA ITEM 7.1: AUDIT AND RISK COMMITTEE REPORT

PURPOSE

1. This paper presents the report prepared by the Secretariat of the Pacific Community Audit and Risk Committee (ARC) to update CRGA 44 on its work in 2014.

RECOMMENDATIONS

2. CRGA is invited to:
- i. note the report from the Chair of the Audit and Risk Committee;
 - ii. approve the appointment of Pricewaterhouse Coopers as external auditor of SPC for the period 2014-2016; and
 - iii. approve the Financial Regulations.
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AUDIT AND RISK COMMITTEE REPORT

Background

3. The Audit and Risk Committee (ARC) was formally established at CRGA 42 in 2012 following a recommendation made by the Independent External Review (IER). At that meeting CRGA also endorsed the committee's charter and a charter for progressing and strengthening an internal audit function at SPC. The committee has met on three occasions in 2014 – in March, July and October.

Internal audit work plan

4. In 2013 the committee endorsed:

- i. an assurance framework to provide a structure for the internal audit and risk function;
- ii. a high-level strategic risk plan that reflected the areas of greatest potential risk given the nature of SPC's activities; and
- iii. a three-year internal audit and risk plan outlining the audit coverage to be provided over the following three years.

5. Following a call for expressions of interest from qualified accounting firms, the committee appointed the international accounting firm Ernst and Young to undertake the three-year work plan. The coverage in the first year was to include a review of:

- i. procurement policies and procedures;
- ii. cash management and investment policies and procedures;
- iii. foreign exchange management policies and procedures;
- iv. consultant engagement policies and procedures; and
- v. travel management and approval policies and procedures.

6. These areas had been identified as potential risk areas given the nature of SPC's activities.

7. To date, Ernst and Young has provided ARC with reports following their investigations in the areas of procurement, cash management and investment and foreign exchange management. All reports have indicated that, while some improvements can be made to strengthen procedures and compliance with approved policies, in general, SPC's current arrangements were sound. Ernst and Young has made a number of recommendations to further strengthen SPC's systems and procedures. ARC has endorsed these recommendations, and the management responses to them.

8. Ernst and Young is currently undertaking the field work for the remaining areas to be covered in 2014 – consultant engagement and travel management and approval – and ARC anticipates considering these reports at its next meeting.

9. The committee is satisfied that the work of Ernst and Young is contributing significantly to the overall objective of the internal audit and risk function in further strengthening SPC's already strong culture of financial probity and compliance.

10. Consistent with the agreed three-year work plan, ARC has approved the following areas for investigation by Ernst and Young in 2015:

- i. follow-up of issues identified for all 2014 activities;
- ii. grant management processes;
- iii. asset management processes;
- iv. information technology governance and control environment; and
- v. business continuity and disaster recovery processes.

11. As reported to CRGA 43, the committee has noted with satisfaction that SPC is progressively funding the internal audit work programme as a core function and will be fully core-funding the programme from 2015 onwards.

Accounting framework

12. Although SPC has been successfully using its own accounting regulations for many years, ARC and SPC management agreed that it was necessary to adopt one of the major international accounting frameworks as international best practice in this area had evolved and donors and stakeholders would be looking for such a change. SPC engaged Ernst and Young to review this issue and make recommendations.

13. ARC endorsed Ernst and Young's recommendation that SPC adopt the International Public Sector Accounting Standards (IPSAS) framework. The adoption of IPSAS had also been recommended by SPC's external auditors. SPC's 2014 accounts are to be presented using the IPSAS format.

2013 external audit

14. ARC met with SPC's external auditors in July 2014 to review and consider the draft audited annual accounts for 2013 and the accompanying management letter from the external auditors. The committee noted with appreciation that the external auditors would be providing an unqualified audit opinion on the 2013 accounts. The external auditors emphasised that SPC's internal controls were strong and they commended the strong compliance culture of the organisation. The committee agreed that the Director-General sign off on the 2013 annual accounts.

15. ARC reviewed the matters raised in the external auditor's management letter and SPC management's responses. The committee is satisfied with the management responses and the actions that are being taken or proposed.

Appointment of external auditor for 2014-2016

16. In July, ARC, supported by SPC management, conducted interviews with three firms that had submitted proposals to undertake the external audit function for the 2014-2016 SPC accounts. This followed the technical assessment of proposals by SPC's Procurement Committee.

17. The Committee endorsed the recommendation of the Procurement Committee that Pricewaterhouse Coopers be appointed and accordingly recommends to CRGA that Pricewaterhouse Coopers be appointed as SPC's external auditor for the period 2014-2016. Pricewaterhouse Coopers has been SPC's external auditor for the past several years.

Project audits

18. A substantial proportion of SPC's programme activity is delivered through project funding provided by a range of bilateral and multilateral development partners. These project activities incorporate their own audit requirements. ARC has included, as a standing item on each meeting agenda, a report on the audit outcomes on project-funded activities as they come to hand. With the exception of grant management issues, discussed below, all project audits received to date have provided unqualified audit opinions.

Grant management

19. In its report to CRGA 43, ARC noted that the audit of a United Nations Development Fund – Global Environment Facility (UNDP GEF) project had been qualified. This qualified audit related to the manner in which the funds are disbursed to national finance systems and the inability of recipient countries to adequately acquit the funds received at the national level. While this project audit is unqualified for the subsequent year, the committee has noted that a qualified audit has been made on the Global Fund Consolidated Grant.

20. SPC management has undertaken significant investigation at its own expense into the circumstances that have led to these qualified audits. The issues are complex and include weaknesses in recipient countries' financial systems and acquittals as indicated above, and deficiencies in monitoring and follow-up procedures by SPC staff in the Grants Management Unit.

21. In the context of SPC's overall budget, the amounts involved are significant. SPC management is currently in discussions with the Global Fund to resolve the issues and agree a way forward.

22. The issues relate to grant management prior to 2013. Since 2013 SPC has recognised the problems and its procedures have been strengthened. The inclusion of a review of grant management processes in the internal audit work programme of Ernst and Young in 2015 should further strengthen and improve SPC's activities in this area.

Financial Regulations

23. ARC has reviewed the draft of the revised Financial Regulations for SPC. These regulations provide an over-arching framework that will govern the financial administration and activities of SPC. The regulations are supported by financial policies and procedures as well as financial delegations approved by the Director-General. CRGA has the authority to approve any proposed amendments to the regulations.

24. With one possible exception, the amendments proposed in the revised draft essentially comprise small changes to reflect changes that have been introduced in the way SPC operates over recent years, including, for example, providing clarity about the role of the Audit and Risk Committee following the decision of CRGA 42.

25. The committee draws the attention of CRGA to the proposed Regulation 33 – Borrowings and Overdraft. SPC's governing agreements and treaties neither expressly permit nor prohibit borrowing by SPC.

26. The proposed regulation would provide that the Director-General may enter into borrowing arrangements subject to two important conditions – that the borrowing can only be from a member country or development partner and that it must be specifically approved by CRGA. The authority to borrow would not extend to borrowing from a commercial financial institution.

27. While there is currently no intention on the part of SPC to enter into borrowing arrangements, the committee considers that this limited authority, with its important limitations and safeguards, is appropriate.

28. The Audit and Risk Committee recommends that CRGA approve the revised Financial Regulations.

Financial Policies and Procedures Manual

29. ARC has approved the terms of reference for the engagement of a consultant to review SPC's financial policies and procedures to reflect best practice and organisational needs. These policies and procedures will be aligned with the Financial Regulations. It is anticipated that this work will commence early in 2015.

30. The Director-General can approve these policies and procedures with advice to CRGA.

Other issues

31. ARC will further strengthen its oversight role through the addition of regular updates in a number of areas as standing items on its meeting agendas. These include: progress on implementation of recommendations from the internal auditors; a register of gifts received by staff in the context of their work activities; a register of any legal actions being taken against SPC; a report on compliance of investments with the agreed policies; and a report on any insurance claims made against SPC.

32. The committee has received regular briefing from SPC management on the implementation of the 2014 budget and the anticipated budget outcome, and the budget outlook for 2015 and beyond.

33. ARC has noted that SPC is currently undergoing a European Union Seven Pillar Assessment. This is a comprehensive assessment of its systems and procedures. If found to be compliant, this will mean that SPC can be entrusted with implementation of EU funds under indirect management. This would significantly enhance the relationship between SPC and the EU.

Conclusion

34. The committee would again like to record its appreciation of the support it has received from the Director-General and the senior management team at SPC. The relationship between the committee and management has been extremely open and constructive and has ensured that continuing progress is being made in embedding internal audit and risk management as core areas of SPC activity.

RECOMMENDATIONS

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