

**SECRETARIAT OF THE PACIFIC COMMUNITY****FORTY-FIRST MEETING OF THE
COMMITTEE OF REPRESENTATIVES OF GOVERNMENTS AND ADMINISTRATIONS**

Noumea, New Caledonia, 1–4 November 2011

Financial Matters

**AGENDA ITEM 10.6: ESTABLISHMENT OF AN INTERNAL AUDIT FUNCTION AND A CRGA
AUDIT COMMITTEE**

(Presented by the Secretariat)

PURPOSE AND INTRODUCTION

1. This paper proposes the establishment of an internal audit function and a CRGA Audit Committee to strengthen the governance framework of the Secretariat. Two charters (annexed to this document) setting out their roles and responsibilities are presented for consideration and approval by CRGA.
2. The internal audit function and CRGA Audit Committee will provide independent advice to CRGA to assist in fulfilling its oversight responsibilities for the financial reporting process, system of internal control, audit process, risk management, effectiveness and efficiency of operations, and compliance with legal and regulatory requirements.
3. In line with good governance practice, both the internal audit function and the CRGA Audit Committee will be independent of the Secretariat.

DISCUSSION

4. The need for an internal audit mechanism has become more apparent given the size of the Secretariat. Recent institutional assessments of the Secretariat, which were commissioned by the European Union, also recommended an internal audit function.
5. Internal audit is an independent support service that provides a systematic and objective approach to evaluate and improve the effectiveness of the organisation's internal control, risk management and governance processes. It complements the monitoring and evaluation function undertaken by SPC's Strategic Engagement, Policy and Planning Facility and by donors, which commission reviews of services delivery by the Secretariat's technical programmes.
6. The internal audit function will assist the organisation in achieving its objectives, as articulated in its corporate plan and various divisional strategic plans in particular, thereby ensuring the effectiveness of the organisation's systems and processes.
7. More information about the general framework of the internal audit function, and details about its purpose, authority and responsibilities are contained in the draft Internal Audit Charter (Annex 1). The charter also sets out the scope of work and the responsibilities of the internal audit function and its relationship with the external auditor. It provides the internal auditor with full and unrestricted access to the Secretariat's management, records and staff, and to information considered necessary to undertake its work. The internal audit function will be provided with the necessary degree of independence.

8. It is proposed that the internal audit function be accountable to a CRGA Audit Committee and report administratively to the Director-General. The terms of reference for this Audit Committee are covered under the draft Audit Committee Charter (Annex 2). In essence, the Audit Committee directs, monitors and reports on the work of the internal audit function, on behalf of CRGA. It will also advise CRGA on the work of the organisation's external auditors.
9. The proposed charter recommends that the Audit Committee consist of three members: the Chair, who is a CRGA member, and two independent members, one of whom is to possess substantial financial or accounting experience or expertise. All members would normally be appointed by CRGA. None of the members can be a staff member of the Secretariat.
10. The Secretariat proposes that CRGA 41 appoint the inaugural Chair of the Audit Committee. Given that CRGA meets annually, it is also proposed that CRGA delegate the authority to the Chair of CRGA to approve the two independent members based on the recommendation of the Chair of the Audit Committee and the Director-General.
11. The Audit Committee charter does not define the length of the membership of Audit Committee members beyond stating that it will be at the discretion of CRGA and it will be a period of at least a year. The Secretariat proposes that the term of the Chair and the two independent members be initially set at two years.
12. It is proposed that amendments to the charters of the internal audit function and the CRGA Audit Committee require the approval of CRGA.
13. The internal audit function will be resourced initially through short-term funding obtained from Australia for the function to be outsourced on a trial basis for a year, during which an evaluation will be undertaken to determine whether an in-house, outsourced or co-sourced¹ arrangement is most suitable.
14. Pending approval of the charters and appointment of the CRGA Audit Committee, the Director-General established an interim internal Audit Committee in June this year, comprising himself as Chair and two Deputy Directors-General as members to oversee the internal audit function of the Secretariat if it were to be established during 2011. The interim audit committee will also provide a recommendation to CRGA in the selection of the external auditor for the financial years 2011–2013 (CRGA paper 10.3).
15. The recent institutional assessment of the Secretariat undertaken for the European Union by PricewaterhouseCoopers noted that the internal audit charter and the audit committee charter as now presented to CRGA were 'well structured and in full compliance with the Institute of Internal Auditors standards'.²

RECOMMENDATIONS

16. CRGA is invited to:
 - i. Approve the establishment of an internal audit function at the Secretariat and the draft Internal Audit Charter;
 - ii. Approve the establishment of a CRGA Audit Committee and the draft Audit Committee Charter;

¹ A co-sourced internal audit function is one where an in-house internal auditor works in conjunction with the outsourced auditor.

² Draft report – Assessment concerning joint management of the Secretariat of the Pacific Community – 12.07.2011 for the European Union by PricewaterhouseCoopers, page 88.

- iii. Appoint a member of CRGA to be the Chair of the Audit Committee, initially for a period of two years;
- iv. Delegate to the current chair of CRGA the authority to approve two additional independent members of the Audit Committee based on the recommendations by the Chair of the Audit Committee and the Director-General.

23 September 2011



SECRETARIAT OF THE PACIFIC COMMUNITY



TITLE OF DOCUMENT: INTERNAL AUDIT CHARTER

VERSION NUMBER: 1.0

DATE SUBMITTED TO EXECUTIVE: 26 June 2011

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PROPOSED REVIEW DATE:

Draft Internal Audit Charter

1. Introduction

This internal audit charter (hereinafter referred to as the 'IAC') sets out the purpose, authority, responsibilities and general framework of the internal audit³ function at the Secretariat of the Pacific Community (hereafter referred to as 'the Secretariat'). The IAC and the function contained therein is established by the Secretariat's governing body, the Committee of Representatives of Governments and Administrations (hereinafter referred to as 'CRGA'). The internal audit function will be overseen by a CRGA appointed 'Audit Committee'. The terms of reference for the Audit Committee are covered under a separate charter, the 'Audit Committee Charter, which is presented together with this IAC.

2. Role

The internal audit function is an integral part of the Secretariat's corporate governance framework to add value and improve the Secretariat's operations. It is an independent support service established by CRGA to provide independent, systematic and objective approach to evaluate and improve the effectiveness of the organisation's internal control, risk management and governance processes. It complements the monitoring and evaluation function undertaken by the Strategic Engagement, Policy and Planning Facility, which reviews actual programme delivery by the Secretariat's technical programmes and evaluates the impact of these technical services at the country level.

The internal audit function will assist the organisation in achieving its objectives, as articulated in its corporate plan and various divisional strategic plans in particular, thereby ensuring the effectiveness of the systems and processes that support resource use and programme delivery at the national level.

The internal audit function will comprise the following types of services:

- *Assurance services* – An objective examination of evidence for the purpose of providing an independent assessment of governance processes, risk management and internal control.
- *Consulting services* – An advisory service that is intended to add value to and improve the Secretariat's systems, procedures and operations.
- *Investigative services* – These are conducted based on reports of unusual or suspicious activity. Investigations would usually focus on specific aspects of the work of a unit⁴ or individual.

3. Scope of work under the internal audit function

The scope of activity of the internal audit will be sufficiently comprehensive to result in the effective review of operations of all of the organisation's divisions, programmes, sections, and units. It also covers the Secretariat's governance, financial, administrative and operational systems and activities.

The areas of focus under the internal audit function include:

³ The Institute of Internal Auditors has developed the globally accepted definition of 'internal auditing' as follows: 'Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an agency accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.'

⁴ Unit refers to a division, programme, section, or any unit of activity.

- a. **Financial audit** – reviews internal control processes regarding income and expenditure, cash and other assets, the accuracy of reporting in accordance with established policies and procedures, and complements work done by external auditors.
- b. **Compliance audit** – evaluates financial and operating controls and their conformance to laws, regulations, standards, contracts, agreements, policies and procedures.
- c. **Operational or performance audit** – examines the application and use of resources to determine whether they are used in the most efficient and effective ways to meet the Secretariat’s mission and objectives. It could include aspects of a financial or compliance review. Activities such as human resources services, cash handling, procurement, and equipment inventories are generally subject to this type of audit. It aims to promote greater levels of efficiency, effectiveness and economy of operations and enhances continuous improvement and adds value to the organisation’s operations.
- d. **Information system** – reviews the internal control environment of automated information processing systems. These audits typically evaluate a) system input, processing, and output; b) data controls, backup and recovery plans; and c) systems security.
- e. **Investigations** – seek to establish impropriety, such as alleged instances of fraud, abuse or waste.

4. Organisation

The head of the internal audit unit will report functionally to the chair of the CRGA Audit Committee, and administratively (day-to-day operations) to the Director-General.

5. Authority

The internal audit function and its staff will have full and unrestricted access to all of the Secretariat’s activities, records, premises, staff and information that it considers necessary to undertake its work. All SPC staff are requested to assist the internal audit unit in fulfilling its roles and responsibilities.

The head of the internal audit will have unrestricted access to the organisation’s senior management and the Audit Committee.

6. Independence and Objectivity

The internal audit function will operate independently from the organisation’s operations. It will set its own work plan, which will be considered and approved by the Audit Committee in collaboration with the Director-General. It determines matters such as audit selection, scope, procedures, frequency, timing or report content that best enables it to fulfill its role.

Internal audit staff do not have direct operational responsibility or authority over any activities audited. They can make recommendations but cannot be involved in implementation or any action that would impair their judgment and independence.

Internal audit staff must exhibit the highest level of professional objectivity in gathering, evaluating and communicating information about the particular activity or process being examined. Their assessments must be objective, based on facts and evidence, and not influenced by other interests.

7. Responsibilities

The scope of internal auditing under this charter encompasses the examination and review of the adequacy and effectiveness of the Secretariat’s governance processes, risk management and internal control processes as agreed on with the Audit Committee. It also evaluates the quality of performance in the carrying out of assigned responsibilities to achieve the Secretariat’s corporate goals and objectives.

The work includes:

- reviewing reliability and integrity of information, systems, processes, policies, procedures and operations, and appraising the adequacy of controls;
- appraising the extent of systems compliance with established policies, procedures and plans, especially where these have a significant impact on operations;
- reviewing controls for safeguarding assets and verifying their existence;
- evaluating the effectiveness, efficiency and economy of resource use;
- evaluating operations or programmes to ensure that results are consistent with established plans, and are implemented as planned;
- monitoring and evaluating governance processes and identifying and reporting significant governance issues;
- monitoring and evaluating the effectiveness of corporate risk management processes and reporting on significant risk exposures and control issues, including fraud risks;
- evaluating specific operations or conducting ad hoc investigations at the request of the Director-General or the Audit Committee;
- evaluating quality of performance of external auditors and the degree of coordination with the internal audit; and
- recommending improvements to governance, systems, processes, policies and procedures and reducing risk exposure.

8. Reporting and Monitoring

Following the conclusion of each audit, a written report will be prepared and issued by the head of the internal audit for distribution to appropriate parties. The internal audit report may include a response from management on corrective actions taken or to be taken by the management in response to specific findings and recommendations.

The internal audit function will follow up on findings and recommendations until they are cleared.

The head of the internal audit will prepare a consolidated report on all activities undertaken by the unit in accordance with the approved work plan for presentation to the CRGA Audit Committee and the Director-General every six months.

9. Professional Standards

All internal audit assignments must be undertaken with due professional care. In line with standards of professional internal auditing practice, the head of internal audit will ensure that:

- skills, competence, experience and qualifications are appropriate for the audits being performed;
- all internal audit assignments are properly supervised and, where required, on-the-job training provided;
- there is compliance with all relevant standards and codes of ethics; and
- all audit staff undertake continuing professional activities and maintain their affiliation to their professional bodies.

The internal audit work is confidential to the Secretariat and is not to be disclosed to third parties without the authority of the Director-General or Audit Committee.

10. Audit Plan — Scope

An annual audit work plan will be prepared and presented to the Audit Committee annually for consideration and approval. In formulating the audit plan and annual work programme, the head of the internal audit will

consult with key audit clients, including members of the Executive and heads of programmes and sections. The internal audit plan should be developed using a risk-based methodology.

The audit plan must:

- be sufficiently comprehensive in scope to meet the needs of the Executive and management;
- consider an assessment of risk of audit unit activities, their internal control environment, results of previous audit, and materiality;
- have an appropriate balance between financial, compliance, operational and performance audits. Information systems and special investigations are conducted as required.
- provide a schedule of audits to be undertaken with the resources available during the period covered by the plan; and
- allow flexibility to accommodate special tasks and projects requested by the Director-General or Audit Committee.

The scope of the internal audit does not extend to the performance of duties normally undertaken by operational units, except as these relate to the performance of audit work.

11. External Audit

Internal and external auditors have differing roles and responsibilities. An internal audit is an independent appraisal function that is resident within the Secretariat. The external auditor has the responsibility of expressing an independent opinion of the financial statement and stewardship of the organisation. As there are likely to be overlaps in the work performed by both an internal and external audit, internal audit assignments should be undertaken with the view of maximising the efficiencies of the internal and external audit processes. Internal audit work should not duplicate the work undertaken by external auditors.

12. Amendment of the Charter

Any amendment of the Charter is subject to the approval of CRGA on the recommendation of the Director-General and the CRGA Audit Committee.

13. Approval by the Director-General

The Director-General approved this charter on 27 June 2011 for submission and consideration by CRGA at its 41st meeting scheduled for 31 October to 4 November 2011.

14. Date of Coming into Force

This IAC, as amended by CRGA 41, will come into force on 1 January 2012.⁵

⁵ CRGA amendments will be incorporated into the IAC for full implementation by 1 January 2012.

Annex 2



SECRETARIAT OF THE PACIFIC COMMUNITY



TITLE OF DOCUMENT: Audit Committee Charter

VERSION NUMBER: 1.0

DATE SUBMITTED TO EXECUTIVE: 19 June 2011

DATE APPROVED BY DIRECTOR GENERAL: 27 JUNE 2011

COMMENTS FROM EXECUTIVE: To be submitted to CRGA 41 for consideration and approval.

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PROPOSED REVIEW DATE:

1. PURPOSE

The Audit Committee assists the Committee of Representatives of Governments and Administrations (CRGA) in fulfilling its oversight responsibilities for the financial reporting process, system of internal control, audit process, risk management, effectiveness and efficiency of operations, and compliance with legal and regulatory requirements. The Audit Committee will be appointed by CRGA.

2. AUTHORITY

The Audit Committee has the authority to:

- oversee the systems and processes noted above;
- conduct investigations into any matters within its scope of responsibility;
- report back to CRGA on the work performed by external and internal auditors;
- consult as necessary with accounting firms employed by the Secretariat in the conduct of its work; and
- seek any information it requires from staff, all of whom are directed to cooperate with the Audit Committee's requests.

3. COMPOSITION

The Audit Committee will consist of three members: the Chair, who is a CRGA member, and two independent members appointed by CRGA. None of the members can be staff of the Secretariat. Membership shall be at the direction of CRGA but for at least one year.

At least one member of the Audit Committee will possess substantial financial or accounting experience and expertise. The mix of skills of the Audit Committee should also include policy, regulatory, programmatic and impact assessment expertise. The secretary of the Audit Committee will be provided by the Secretariat.

4. MEETINGS

The Audit Committee will meet at least twice annually. Additional meetings may be called by the Chair, as needed. All committee members are expected to attend each meeting, in person or via tele- or video-conference.

The Audit Committee will invite members of the Executive, auditors or others as appropriate to attend meetings and provide pertinent information, as necessary. Meeting agendas will be prepared and provided in advance to members, along with appropriate briefing materials. Minutes will also be prepared.

5. RESPONSIBILITIES

The Audit Committee will carry out the following responsibilities.

Financial Statements

- Review with management and external auditors the results of the audit and any significant accounting or reporting issues, including any difficulties encountered.
- Review annual financial statements, and consider whether they are complete, consistent with information known to Audit Committee members, and reflect appropriate accounting principles.
- Review with management and external auditors all matters required to be communicated to the Audit Committee under generally accepted auditing standards.

Internal Control

- Keep under review the effectiveness of the internal control systems, risk management and risk mitigation process.
- Understand the scope of internal and external auditors' review of internal control over financial reporting, and obtain reports on significant findings and recommendations, together with management's responses.
- Ensure that timely and appropriate corrective action is taken by management.
- Keep under review the system for monitoring compliance with rules, regulations and laws.
- Ensure that risk management issues are adequately addressed.
- Ensure that attention is given to the effectiveness, efficiency and economy of operations.

Internal Audit

- Review with management and the internal auditor, the internal audit charter, activities, staffing, and organisational structure of the internal audit function.
- Review and approve the annual internal audit plan.
- Review the findings and recommendations in internal audit reports as well as management responses.
- Review the effectiveness of the internal audit function, ensuring continued independence and its performance.
- Consult regularly with the head of internal audit to discuss matters that the Audit Committee or internal audit believe should be discussed privately.

External Audit

- Review, if necessary, the external auditors' proposed audit scope and approach, including coordination of audit effort with internal audit.
- Review the performance and effectiveness of external auditors.
- Advise CRGA on the appointment of external auditors and the audit fee.
- Review external auditors' management letter and management responses.
- Consult with external auditors to discuss any matters that the Audit Committee, external auditors or internal audit function believe should be discussed separately.

Compliance

- Review the effectiveness of systems for monitoring compliance with organisational regulations and policies.
- Obtain regular updates from management and the organisation's legal counsel regarding compliance matters.

Reporting Responsibilities

- Report annually to CRGA about the Audit Committee's activities, issues and related recommendations.
- Provide a mechanism for open communication between internal auditors, external auditors, management and the CRGA Chair.
- Review any other reports the Secretariat issues that relate to Audit Committee responsibilities.

Other Responsibilities

- Initiate, where necessary, special investigations of policies, procedures and practices.
- Act as an external point of contact for any whistle-blowing issues.
- Review and assess, as required, the adequacy of the Audit Committee's terms of reference, and propose changes to CRGA for approval.
- Report annually to CRGA that all responsibilities outlined in the terms of reference have been discharged.

6. APPROVAL BY THE DIRECTOR-GENERAL

The Director-General approved this Audit Committee Charter on 27 June 2011 for submission and consideration by CRGA at its 41st meeting scheduled for 31 October to 4 November 2011.

7. DATE OF COMING INTO FORCE

This Audit Committee Charter, as approved by CRGA 41, will come into force on 1 January 2012.⁶

8. INTERIM AUDIT COMMITTEE

The Director-General has established an interim internal Audit Committee comprising the Director-General as Chair and the two Deputy Directors-General as members to oversee SPC's internal audit function in 2011.

⁶ CRGA amendments will be incorporated into the Audit Committee Charter for full implementation by 1 January 2012.