



FOURTH ITEM ON THE AGENDA

**Follow-up to the report of the
External Auditor on the accounts
for 1998-99**

1. At the 277bis Session (May 2000) of the Governing Body, the Committee considered the report of the External Auditor on the accounts of the 1998-99 financial period. The report of the External Auditor included recommendations and observations on certain financial and operational matters which are addressed below in the order in which they appear in the report.

**Action taken in response to the recommendations
in the report on the ILO's 1996-97 accounts****On the use of special accounts**

2. New operating procedures have resulted in improved monitoring and regular reports on these funds are now issued to the departments concerned. Previously dormant balances are now being utilized. As noted by the External Auditor this is an ongoing process.

Programme and performance evaluation***MERS***

3. Based upon the recommendations of an informal ILO workshop in October 1999 on the review of the Monitoring, Evaluation and Reporting System (MERS), the Office engaged in developing a simplified, user-friendlier version of the MERS software adapted to the strategic budgeting framework. The new OPAS (Operational Planning and Accountability System) software is presently in its final stages of testing and should be ready for Office-wide use at the operational level in 2001. An important feature of the new system is the linkage between the operational and the strategic level, including the operational objectives, indicators and targets. It is proposed that the new system will become the standard work-planning, monitoring and evaluation system for technical activities at headquarters and in the regions and that the workplans of all ILO units be placed on the Office-wide Intranet. The new system is not suited for administrative purposes and the ILO

is assessing commercial work-planning packages which will be offered, as an optional tool, to the administrative units concerned.

Evaluation strategy

4. An evaluation strategy for the Office was presented to the Governing Body at its November 2000 session (GB.279/PFA/8). The paper confirmed the evaluation practices proposed in Volume 3 of the Programme and Budget for 2000-01. More specifically, it confirmed that:
 - (a) the evaluation must be systematized and integrated into the strategic budgeting process;
 - (b) evaluation is important as a means of feeding information about performance levels back into decisions on programme priorities;
 - (c) the ILO should continue with both self- and independent evaluations;
 - (d) decentralized evaluation capacities will be developed;
 - (e) an evaluation plan will be developed and presented to the Governing Body as would the results of major evaluations; and
 - (f) present arrangements remain with regards to the evaluation of technical cooperation programmes.
5. In the course of the year 2000, the ILO undertook a survey of evaluation policies and practices in other UN organizations. The survey concluded that ILO evaluation practices are broadly in line with those in other UN organizations. The evaluation strategy further emphasizes that integrating evaluation into strategic budgeting will require changes in internal procedures. One priority of the Bureau of Programming and Management in 2001, and in 2002-03, will therefore be to organize training, both at headquarters and in the field, on strategic budgeting, evaluation and oversight.

Strengthening the role of the Evaluation Unit

6. The internal structures within the Bureau of Programming and Management will be modified to ensure a greater integration of evaluation in the strategic budgeting process. The Bureau will be responsible for Office-wide guidance on evaluation issues, the elaboration of guidelines and procedures and the coordination of implementation of the evaluation plan.

Better dissemination of lessons learned (updating of evaluation database)

7. The availability of the evaluation database via the ILO's Internet website has ensured that ILO officials and constituents have easier access to the evaluation documentation emanating from the ILO technical cooperation programme. Regarding the improvement of the content of the database, several options are under consideration. The possibility of linking the evaluation database to other decentralized evaluation databases will be examined, to ensure that all evaluative information available can be assessed through one central database. Consideration is also being given to making full evaluation reports available on the Internet instead of the present abstracts.

Tracking of actual costs incurred

8. A permanent cost-tracking system is costly and constraining, but the Office is using targeted work measurement when appropriate. The two most recent examples of such specific studies are the identification of actual costs of backstopping technical cooperation programmes as well as actual costs incurred in connection with the preparation of reports to the Governing Body and the International Labour Conference.

On property management

9. The External Auditor referred to the good progress made in the implementation of his recommendations in this area. The role of the different organizational units involved in managing property had been clarified and key information on the nature of property assets held in the field had been collected. Work on the accommodation strategy has now been finalized and incorporated in a property and equipment management manual.

Financial matters (1998-99)

Full implementation of the United Nations system Accounting Standards

Recommendation 1. The ILO should refine its procedures to provide earlier and better guidance for staff establishing accruals; and find better ways to account for the subsequent disbursement of accruals so that any savings are identified and credited to miscellaneous income.

10. The transition from cash accounting to accrual accounting in the ILO required a number of fundamental changes in accounting procedures for the Office to close the financial period. In view of the limited period of time between the decision by the Conference to amend the Financial Regulations and the closure of the financial period, it was not possible to automate this process. An extensive manual effort was required within a very short period of time to comply satisfactorily with the amended regulations.
11. The External Auditor estimated that the amounts accrued may have been overstated by some US\$600,000 (representing 0.1 per cent of total expenditure). Should there be any unutilized balances in the accrual accounts these will be credited to miscellaneous income in accordance with the Financial Regulations.
12. The External Auditor's reference to bulk posting can be explained as follows. At the end of 1999, where goods and services had been delivered but not yet paid for, the expenditure was accrued. During the subsequent financial period, in accordance with the Financial Regulations, the disbursements pertaining to these accruals were charged against the accrual account rather than to the current financial period. Individual matching of each disbursement with an individual accrual was not considered necessary. What is critical is that only disbursements relating to goods and services delivered in the prior financial period are so charged and that the total amount charged against accrued balances does not exceed the amount available. This approach is consistent with the intention of the amendment to the regulations which is to ensure the correct recording of expenditure to the financial period to which it relates.
13. Technical cooperation accounting systems have been modified and similar modifications are being made to regular budget systems to enable an automated accruals procedure to be

implemented for the closure of the 2000-01 biennium. The lessons learned from the first closure using accrual accounting will be incorporated into revised procedures and guidelines that will be dispatched to the regions well in advance of the closing of the current financial period.

Funding of extra-budgetary technical cooperation activities

Recommendation 2. The ILO should:

- *review all closed projects with deficits and take appropriate recovery or write-off action;*
- *make one branch responsible for monitoring income and expenditure and ensuring funds are called for promptly;*
- *update its guidance on the financial procedures to be followed on extra-budgetary technical cooperation projects.*

- 14.** The Office has always applied judicious flexibility in interpreting the Financial Rules so as not to impede unduly the delivery of technical cooperation to member States. In particular, once a project agreement has been signed by the donor and the Office, and the initial advance of funds has been received, authority is given to commence project activities. In the absence of indications of funding problems, project activities continue, notwithstanding delays in receiving further funds or the existence of temporary deficits on individual projects. It would not be cost-effective to limit project activities to funds actually received. Contracts for project staff must cover periods beyond the normal six-monthly advances, and project activities would be seriously disrupted if staff were repatriated every time there was a delay in the receipt of funds. Similarly, planning must extend beyond short-term fund availability to ensure project continuity. Donors are, understandably, unwilling to provide complete advance funding for project activities that may cover a number of years.
- 15.** Of the 55 projects with deficit balances, cited by the External Auditor, one project, which was shown as having a deficit of \$566,000, was actually fully covered but, due to a miscoding, appeared to be in deficit. A further 41 deficit balances were covered by funds available on other projects funded by the same donors. Of the remaining 13 projects, three related to countries suffering from conflicts and ten were subject to delays in the receipt of funds.
- 16.** Following receipt of the External Auditor's report, an extensive review of all closed projects was undertaken and the Office has engaged in renewed correspondence with donors where deficit balances existed on their accounts. With the donors' agreement, balances have been transferred from projects with surplus funds to those in deficit; progress payments that had been delayed have been received and further requests have been sent where necessary. It is likely that some write-off action may be required later this year due to the age of certain outstanding amounts. The Governing Body will be informed of any such write-offs.
- 17.** The External Auditor referred to the impact of exchange rate movements on project budgets. Many donors are required, by their own legislation, to express their funding commitment in their national currency. As the Office's unit of account is the US dollar, budget variances are inevitable. Almost all donor agreements include a clause providing for additional funding in the event that unforeseen needs, such as exchange losses, occur. In the past, donors have agreed to fund such needs, but they are becoming increasingly

reluctant to do so. Procedures are in place to revalue, on a regular basis, all budgets which are subject to currency fluctuations. This reduces the risk of deficits, albeit with some operational inconvenience.

18. The External Auditor's recommendation on merging the responsibility for monitoring income and expenditure with the follow-up of calls for funds is supported by the Office. The merger has already commenced within the Financial Services Department with one staff member having been transferred and a further transfer planned following the closure of technical cooperation projects for the year 2000. However, some separation of responsibilities is desirable and will continue, with the Cooperation Development Department continuing to act as the primary contact point with multi-bilateral donors. The Financial Services Department will continue to provide support to that Department. More frequent communications between the Cooperation Development Department, the Financial Services Department and the technical departments responsible for implementing projects has already improved the monitoring and forecasting of project implementation and funding needs.
19. The delays in the submission of project reports to donors arise in part due to the variety of formats and the frequency of such reports required by donors. The Office has been negotiating with multi-bilateral donors over the past two years to establish a standardized format and frequency of progress reporting. A standard format has now been agreed to by most of the major donors and this will improve the timeliness of reporting.
20. The general guidance relating to funding procedures is contained within the Financial Rules and Regulations. As the Office's practice for receiving donor funds and opening accounts has always been considered relatively straightforward, no formal guidelines had been prepared for these procedures. However, the transfer of responsibilities to a new unit has prompted the Office to address this recommendation by the External Auditor. The work should be completed in conjunction with the transfer of responsibilities referred to above.

Staff Health Insurance Fund (SHIF)

Recommendation 3. The ILO should clarify the auditing and reporting arrangements for SHIF, including the arrangements for auditing ITU benefit expenditure.

21. The External Auditor noted that the Regulations of the Fund state that "the Management Committee, in consultation with the executive heads of the ILO and ITU, shall appoint one or more auditors, who shall audit the financial transactions and accounts of the Fund and check the application of these Regulations". He further noted that the auditor of the Fund was the Internal Auditor of the ILO. Indeed, The Fund's Administrative Rules provide that: "In principle, the Management Committee will appoint as auditors the Internal Auditor of the ILO and a suitably qualified official of the ITU."
22. The External Auditor found certain weaknesses in current audit arrangements for the Fund, notably: (a) that the SHIF accounts do not include a separate audit opinion as is normally given by external auditors; and (b) that due to a new division of work between the ILO and ITU following the introduction of the new Health Insurance Information System (HIIS) on 1 April 2000, he had not been able to examine the source documentation relating to the ITU claims which are held separately by the ITU but which feature in the ILO's accounts.
23. The Fund's Management Committee decided to appoint both the ILO Internal and External Auditors as auditors of the Fund for 2001. Both ILO External and Internal Auditors will work in close cooperation with their ITU counterparts.

***Recommendation 4.** The ILO should review the legal and constitutional status of the Staff Health Insurance Fund and its relationship with the sponsoring bodies. This review should also consider whether the ILO should continue to include SHIF fund balances in its accounts.*

24. The Office of the Legal Adviser and the Financial Services Department are currently studying these recommendations, which relate to the Office's responsibility for "keeping the accounts of the Fund, holding its monies and arranging for the investment of the insurance funds, in consultation with the Management Committee" (article 3.11 of the Fund's Regulations).

***Recommendation 5.** The ILO should continue to keep under review the potential costs and benefits of outsourcing the operation of SHIF.*

25. The Office has decided to undertake a new study of the potential costs and benefits of outsourcing the Fund's administration. The study will be undertaken by consultants chosen in accordance with ILO Financial Rules on competitive bidding, among firms which have no direct interest in the administration of a health fund.

Inventory

***Recommendation 6.** The ILO should take steps to update their headquarters and field inventories as a matter of urgency. This should include a physical verification of the assets held.*

26. Following the recommendation of the External Auditor, work on the updating of inventory records was given high priority in 2000 both for headquarters and the field. All outstanding disposals were recorded and the headquarters inventory records were updated as at 31 December 2000. Property and inventory procedures were revised and updated and a property and equipment management manual established. Annual returns from field offices were followed up as were the valuations of project inventories. Difficulties associated with the use of multiple-inventory computer systems were resolved by the amalgamation of these systems into a single database system (Building Management System).
27. A complete physical check of the headquarters inventory is planned for autumn 2001, following the completion of an extensive space and office rearrangement exercise currently taking place at headquarters.

Management matters

International Programme on the Elimination of Child Labour (IPEC)

28. The External Auditor noted that work had been done to address the issues related to the International Steering Committee, but added that some work remained to be completed on the role and responsibility of the national steering committees. Draft guidelines were completed and sent to all IPEC field offices in February 2001. These guidelines will be useful especially for those countries starting new activities with IPEC and where the Memorandum of Understanding is due to be renewed. This will fully address the External Auditor's recommendations on the strategic management of the programme.
29. Regarding IPEC's budget and the External Auditor's comment that the programme and budget document will be further enhanced to reflect the audit observations, IPEC has

recruited an official who will be responsible for financial reporting. This resource will be used both to monitor ongoing delivery and to provide the figures for the next programme and budget. IPEC intends to consult with the External Auditor before the budget document is finalized.

- 30.** With reference to the External Auditor's comments and recommendations related to IPEC's management structure, IPEC enhanced its human resource management capacity by recruiting an HRD specialist in November 2000 to work on the type of personnel issues raised by the External Auditor. Work has already been completed to create standard job descriptions, improve IPEC's recruitment procedures, streamline contracts of employment for different categories of IPEC staff, especially field teams, and to develop performance assessment reports. This work will be carried out in close cooperation with HRD to ensure that personnel policies adopted by IPEC are consistent with the rest of the Office. IPEC is in the process of restructuring the operations side of its work, at which time the roles and responsibilities of staff, including the regional and country staff, will be clarified.
- 31.** HRD identified an ILO official to study the issues related to the adoption of the UNDP national officer classification for IPEC personnel in the field. A draft discussion paper on the Office-wide implications of creating a new personnel category (national programme officer, NPO) covering the advantages and disadvantages of such a move was prepared, comparing the rules governing the NPO at UNDP and UNICEF with the ILO PASO/Senior PASO categories. A proposal to introduce the NPO category is being put before the Governing Body during the current session.
- 32.** The External Auditor commented on the nature of IPEC activities being classified as subcontracts, therefore having to go through PROCUREMENT and the Treasurer's Office for financial clearances and waivers. These procedures have been revised with the waiver requirements being relaxed and IPEC is working with PROCUREMENT to further streamline procedures, including developing a Web-enabled tracking system of the approval process to identify potential blockages.
- 33.** Regarding internal controls over the use of IPEC funds, IPEC has contracted local audit firms to assess the internal controls and examine the expenditure of implementing agencies in certain countries. The first audit reports have been reviewed by the task force and the results of these audits will be used to enhance the guidance that has already been issued on internal controls (e.g. improved reporting formats; issuance of criteria governing the selection of implementing agencies; and cashbook checklists to assist local staff in the monitoring of the use of IPEC funds). IPEC employed a consultant in February 2001 to incorporate all of the changes made to IPEC procedures into a user-friendly procedural manual.
- 34.** Regarding the monitoring and evaluation of the programme, IPEC has developed a comprehensive evaluation strategy that was approved by management, including a workplan through to the end of 2001. The resources allocated to monitoring and evaluation have also been increased with an additional post being added to the Evaluation Unit in 2000.
- 35.** On management information needs, the External Auditor commented on IPEC's project database and also on the lack of financial reports available to IPEC senior management. IPEC employed a consultant to update the database and this is expected to become fully operational and Web-enabled by April 2001. IPEC also recruited an official to prepare financial management reports and, after discussing the reporting needs of IPEC management and senior programme staff, monthly financial reports have been prepared since June 2000. These have, inter alia, enabled the IPEC management to monitor its delivery rates, which was another concern of the External Auditor.

36. The External Auditor noted that the IPEC management intended to improve controls over administrative costs. IPEC intends to work with FINANCE and PROGRAM to ensure that the definition of administrative costs is consistent throughout the ILO, and will generate monthly expenditure reports to ensure that it monitors its administrative costs on a regular basis.
37. Due to the rapid expansion of the IPEC programme since 1999, the implementation of all recommendations made by the External Auditor has taken longer than was originally envisaged. IPEC has however strengthened its capacity by recruiting staff to work on key areas such as human resources, financial reporting, database administration and evaluations and making these an integral part of the revised IPEC structure. Further evidence of IPEC's increased capacity can be shown by a significant improvement in delivery, which increased from \$11.5 million in 1999 to \$22.8 million in 2000. The delivery rate over the two years also increased by approximately 23 per cent.

Procurement of goods and services

Recommendation 7. The ILO should review the current areas of procurement responsibility and seek to streamline the process by concentrating the tendering and selection of contracts within the Procurement Section.

38. In 2000, the Procurement Section took over responsibility for all procurement and contracting activities of the Internal Administration Bureau and is now also coordinating the tendering and selection processes for the Document and Publications, Printing and Distribution Branch, the Bureau of Information Technology and Communications, the Bureau of Library and Information Services and the InFocus Programme on Child Labour.
39. Initiatives have also been taken to enhance the Organization's understanding of, and adherence to, established procedures by the issue in 2000 of three comprehensive circulars on contracting and procurement for headquarters departments and ILO offices in the field. Meetings and briefings are now held with new officials and officials taking up new assignments in order to familiarize them with contracting and procurement procedures. Information pages are being established on the ILO's Intranet to promote the Organization's knowledge of procurement procedures. Monthly procurement meetings with technical units and project staff are also being held.

Recommendation 8. The ILO should review all major contracts where the same contractor has been in place for over four years with a view to testing the contract in the open market at the earliest opportunity.

40. In 2000, a review of all major contracts was undertaken as recommended by the External Auditor. A plan for the review of all contracts has been set up and this will be monitored on a regular basis to ensure proper management follow-up. To date, contracts dealing with catering services, the travel agency, building insurance, telecommunications and security services have been awarded following requests for tenders. The remaining contracts identified by the External Auditor are in the phase of being reviewed and will also be subjected to competitive bidding in the open market.

Recommendation 9. The ILO should review contracts which are renewed on an implicit basis and assess whether a fixed contract period would be more appropriate.

41. This observation has been noted and, whenever possible, existing contracts have been converted to include fixed contract periods and all new contracts now operate on this basis.

Recommendation 10. *The ILO should refer all major contracts of this type to the Contracts Committee for scrutiny when they are renewed.*

42. This comment is a valid one and all contracts whose value exceed \$70,000, including those of the type identified by the External Auditor, will be presented to the Contracts Committee for approval, both for renewal and for new contracts. The Contracts Committee is also consulted on policy issues and whenever it is deemed necessary prior to going to competitive tender.

Recommendation 11. *The ILO should ensure that sufficient time is allocated to the tender (or re-tender) process to allow proper application of the relevant and required procedures.*

Recommendation 12. *The ILO should tighten the procedures on the justification of waivers so that they conform more strictly to the laid down Financial Rules.*

Recommendation 13. *The ILO should aim to subject more contracts to open competition so that contracts can be properly tested against market conditions.*

Recommendation 14. *The ILO should annotate every waiver request with the relevant subsection of Financial Rule 10.30 which is being applied.*

43. The Office has issued a circular to all units at headquarters and in the field clarifying procedures to be followed whenever a waiver of competitive bidding procedures is requested. The circular specifically addresses the recommendations made by the External Auditor in that it emphasizes the strict application of Financial Rule 10.20(a) (requirement for competitive bidding) and the requirement of identifying the relevant subsection of Financial Rule 10.30 on every waiver request.

44. The circular also emphasizes:

- the importance of submitting waiver requests in good time so that sufficient time is available for competitive bidding procedures to be carried out, should a waiver not be granted;
- the requirement that waivers requested by the application of Financial Rule 10.30(c) (urgency) will only be granted where they relate to bona fide urgent cases.
- the Office's position regarding retroactive waiver requests.

Cases of failure to comply with competitive bidding rules and procedures may be referred to the Committee on Accountability for further action, in accordance with Financial Rule 13.30(b).

Recommendation 15. *The ILO should identify and implement procedures to improve procurement planning and introduce standards to measure the effect of such procedures.*

45. Implementation of a fully integrated procurement management system is planned for the latter part of 2001. This system will be used by the departments and field offices concerned and will specify minimum lead times for departments initiating procurement requests. The Procurement Section has also been involved with the Development Cooperation Department in the formulation of a project manual which will include a chapter on procurement planning.

Recommendation 16. *The ILO should put in place the means to ensure that performance and effectiveness of all areas of procurement can be monitored and measured.*

46. Performance indicators have now been introduced in monthly reports issued by the Procurement Section covering the status of procurement activities, procurement statistics, actions planned and taken and resource management. This first monthly report was issued in November 2000.

Recommendation 17. The ILO should cover ethical issues in its guidance on procurement in ways which puts the onus equally on both employee and supplier to abide by the relevant regulations.

Recommendation 18. The ILO should set up registers to disclose financial interests and the receipt of gifts and hospitality.

Recommendation 19. The ILO should establish a code of conduct which reminds staff of their responsibilities in regard to ethical issues and which staff are required to sign on a periodic basis.

47. The issue of business ethics and codes of conducts in relation to gifts and entertainment is being addressed at monthly staff meetings in the Procurement Section. Additionally, a minute is issued annually to all Procurement Section staff reminding them of the ILO's policy on gifts and entertainment. Ethical issues in relation to procurement are currently being reviewed in consultation with the Human Resources Department with a view to incorporating such issues within the ILO's overall personnel policies.

Administration of travel

Recommendation 20. The ILO should expedite the updating of the guidance on travel to reflect the current roles and responsibilities of branches involved in authorizing and processing travel expenditure.

48. A new circular on travel is about to be issued with a view to simplifying and rationalizing all procedures concerning travel, including authorization and supervision processes.

Recommendation 21. The ILO should press ahead with the automation of the travel authorization process.

49. The new automated travel authorization is part of the scope of the new financial systems which are to be implemented by the ILO.

Recommendation 22. The ILO should review the accounting treatment of income from airlines and notional savings. Conference approval should be obtained if the ILO wishes to continue the existing practice of using the income to finance staff posts in VOYAGES.

50. The past practice of using travel income to finance staff posts in VOYAGES for the travel process has been discontinued and the process for redeployment of the staff concerned has begun. The accounting treatment of income from airlines as well as notional savings is being rectified and savings will be credited to regular budget programmes or technical cooperation projects.

Recommendation 23. The ILO should review the role of VOYAGES and consider a move to sample checking travel itineraries.

51. The work carried out by the Travel Unit has been systematically reviewed and, under new guidelines which are being prepared, travel procedures will be directly processed by the Office's travel agency under the supervision and delegated authority of the Internal Administration Bureau. Travel processes, including itineraries, will continue to be

monitored by the Internal Administration Bureau on a sample basis. Transportation of personal effects, removals, travel documents and insurance will continue to be handled by the Internal Administration Bureau.

Ongoing follow-up

- 52.** The Director-General will continue to work in close liaison with the External Auditor with regard to follow-up of his recommendations, as he attaches great importance to them and wishes to derive full benefit for the Organization from the work performed by the External Auditor.

Geneva, 26 February 2001.