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Financial reports and audited financial statements, and reports of the Board of Auditors

Financial reports and audited financial statements and reports of the Board of Auditors for the period ended 31 December 2007

Report of the Advisory Committee on Administrative and Budgetary Questions

I. Introduction

1. In accordance with regulation 7.12 of the Financial Regulations and Rules of the United Nations (ST/SGB/2003/7), the Advisory Committee on Administrative and Budgetary Questions received copies, some in advance form, of the financial reports, audited financial statements and reports of the Board of Auditors to the General Assembly for 15 entities of the United Nations system for the biennium ended 31 December 2007 and for the voluntary funds administered by the United Nations High Commissioner for Refugees and for the capital master plan for the year ended 31 December 2007. A list of the audit reports appears in the table below. As usual, the report of the Board of Auditors to the accounts of the United Nations peacekeeping operations for the financial period from 1 July 2007 to 30 June 2008 (A/63/5 (Vol. II), chap. II) will be considered by the Advisory Committee in early 2009. In addition, the Committee had before it an advance version of the concise summary of the principal findings and conclusions contained in the reports submitted by the Board of Auditors to the General Assembly at its sixty-third session (A/63/169) and of the report of the Secretary-General on the implementation of the recommendations of the Board of Auditors on the accounts of the United Nations, the United Nations funds and programmes and the international tribunals for Rwanda and the Former Yugoslavia for the financial period ended 31 December 2007 (A/63/327 and Add.1). The Committee also considered and will issue a separate report on the report of the Board of Auditors on the activities of the Procurement Task Force and the report of the Secretary-General on the implementation of the recommendations of the Board of Auditors contained therein (A/63/167 and Add.1).

2. The Board issued unqualified opinions for seven entities (the United Nations, United Nations Development Programme (UNDP), the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNWRA), the United Nations Office on Drugs and Crime, the United Nations Institute for Training and Research (UNITAR), the United Nations Children's Fund (UNICEF) and the United Nations Joint Staff Pension Fund). The Board issued modified audit reports with various emphases of matter for nine entities (the International Trade Centre UNCTAD/WTO), the United Nations Office for Project Services (UNOPS), the International Tribunal for the Former Yugoslavia, the International Criminal Tribunal for Rwanda, the Office of the United Nations High Commissioner for Refugees (UNHCR), the United Nations Environment Programme, the United Nations Human Settlements Programme (UN-Habitat), the United Nations Population Fund (UNFPA) and the United Nations University). The reports include replies of the aforementioned entities to recommendations and observations of the Board of Auditors, as well as additional information on measures taken to implement the recommendations of the Board. The entities have generally concurred with the recommendations of the Board and have proceeded, as and where appropriate, to implement them. In instances where they do not agree with the recommendations of the Board or contend that they are unable to begin implementation, they have provided an explanation. Upon request, the Board provided the Advisory Committee with the following table showing the type of opinion issued by the Board on the financial statements of each entity as well as the number of recommendations accepted or not accepted by each:

			Recommendations		
	Organization audited	*Type of opinion issued on the financial statements*	*Accepted*	*Not accepted*	*Total*
1.	United Nations (A/63/5 (Vol. I))	Unqualified	63	3	66[a]
2.	International Trade Centre UNCTAD/WTO (A/63/5 (Vol. III))	Unqualified with emphasis of matter	3	1	4
3.	United Nations University (A/63/5 (Vol. IV))	Unqualified with emphasis of matter	17	2	19
4.	United Nations Development Programme (A/63/5/Add.1)	Unqualified	74	8	82
5.	United Nations Children's Fund (A/63/5/Add.2)	Unqualified	42	—	42
6.	United Nations Relief and Works Agency for Palestine Refugees in the Near East (A/63/5/Add.3)	Unqualified	31	—	31
7.	United Nations Institute for Training and Research (A/63/5/Add.4)	Unqualified	10	2	12
8.	Office of the United Nations High Commissioner for Refugees (A/63/5/Add.5)	Unqualified with emphasis of matter	21	—	21
9.	United Nations Environment Programme (A/63/5/Add.6)	Unqualified with emphasis of matter	11	—	11
10.	United Nations Population Fund (A/63/5/Add.7)	Unqualified with emphasis of matter	58	2	60

Organization audited	Type of opinion issued on the financial statements	Recommendations		
		Accepted	Not accepted	Total
11. United Nations Human Settlements Programme (A/63/5/Add.8)	Unqualified with emphasis of matter	15	1	16
12. United Nations International Drug Control Programme (A/63/5/Add.9)	Unqualified	18	1	19
13. United Nations Office for Project Services (A/63/5/Add.10)	Unqualified with emphasis of matter	48	—	48
14. International Criminal Tribunal for Rwanda (A/63/5/Add.11)	Unqualified with emphasis of matter	18	1	19
15. International Tribunal for the Former Yugoslavia (A/63/5/Add.12)	Unqualified with emphasis of matter	6	1	7
16. United Nations Joint Staff Pension Fund (A/63/9)[c]	Unqualified[b]	27	—	27
17. Capital master plan (A/63/5 (Vol. V))	Not applicable[d]	9	—	9

[a] Not including 4 recommendations that the Administration considered to be within the purview of the General Assembly.

[b] Reports on the implementation of the recommendations of the Board of Auditors are not yet available.

[c] The audit report on the accounts of the Joint Staff Pension Fund are included in the report of the United Nations Joint Staff Pension Board.

[d] The financial statements were consolidated in those of the United Nations (A/63/5 (Vol. I)).

3. The comments and recommendations of the Advisory Committee on the report of the Board of Auditors on the United Nations Joint Staff Pension Fund for the biennium ended 31 December 2007 (A/63/9, annex IX), will be submitted separately. Similarly, the Committee will comment on the audit reports on the International Criminal Tribunal for Rwanda (A/63/5/Add.11, chap. II), the International Tribunal for the Former Yugoslavia (A/63/5/Add.12, chap. II) and the capital master plan (A/63/5 (Vol. V)) in the context of its consideration of the financing of the tribunals and the sixth progress report of the Secretary-General on the capital master plan.

4. Many of the issues covered by the Board with respect to the United Nations may have relevance to other reports that the Advisory Committee is taking up during its current session, in particular on human resources management, information technology, including the enterprise resource planning system, and the International Public Sector Accounting Standards (IPSAS). The Committee will comment further and draw upon the Board’s observations on such matters in the context of its consideration of those reports.

5. The Advisory Committee also expects to revisit as necessary the observations and recommendations of the Board of Auditors and the other issues discussed in its reports on the financial statements of funds and programmes during the Committee’s review of the biennial budgets of those entities for the next fiscal period. Prior to its hearings with the Board of Auditors, the Committee met with the representatives of UNHCR. The Committee’s report to the UNHCR Executive Committee (A/AC.96/1055/Add.1) contained a number of comments relating to the report of the

Board. The Committee also had an informal exchange of views with representatives of UNOPS.

6. During its consideration of the reports, the Advisory Committee met with the members of the Audit Operations Committee, who provided additional information and clarification. The Advisory Committee also met with representatives of the Secretary-General to discuss the status of implementation of recommendations of the Board.

II. General observations and recommendations

7. **The Advisory Committee welcomes the continued high quality of the Board's reports and notes the Board's efforts to condense and prioritize its findings in order to make them more structured and reader-friendly.** In response to the Committee's previous recommendation (A/61/350, para. 8), the Board has streamlined its reporting and aligned the structure of its reports with that of the financial statements, making cross-referencing easier. **The Committee also welcomes, in particular, the quality of the concise summary of principal findings and conclusions (A/63/169), which provides a useful overview of the Board's work. However, the Committee believes that the thematic structure of the concise summary could be further refined to match, for ease of reference, that of the Board's other reports.**

8. The Advisory Committee was informed that the Board had used more than 2,073 auditor-weeks during the audit cycle for the biennium 2006-2007. This included the Board's peacekeeping audits but excluded senior management time, general coordination, assistance and training. During the audit period, the Board issued 176 management letters to organizations on matters of programme and financial management. Some of the significant comments contained in those management letters are reflected in the Board's reports to the General Assembly.

9. As has been customary in previous reports, the Board of Auditors has included observations and recommendations on a number of cross-cutting issues, such as non-expendable property, end-of-service and post-retirement benefits, programme expenditure, treasury and cash management and human resources management. During its hearings with members of the Audit Operations Committee, the Advisory Committee was informed that the Board intended to examine issues relating to results-based budgeting and results-based management in the context of its review of the financial statements of the United Nations for the biennium 2008-2009.

10. The Board has included in its reports an annex showing the status of implementation of the Board's recommendations as at 31 December 2005. Upon request, the Advisory Committee was provided with the following table showing the total number of recommendations and the status of implementation since the biennium 2000-2001:

Status of implementation of recommendations

Period	*Number of recommendations*	*Fully implemented*	*Partially implemented*	*Not implemented*
2000-2001	378	172	178	28
2002-2003	545	282	229	34
2004-2005	788	505	250	33
2006-2007	500	481	19	—

11. In its consideration of the various reports of the Board of Auditors, the Advisory Committee noted a number of cross-cutting issues, such as assets management, end-of-service and post-retirement benefits, IPSAS and non-expendable property, on which the Board has issued recommendations and made observations. The Committee notes that the non-implementation or delayed implementation of recommendations can expose the United Nations and its funds and programmes to a variety of risks. In particular, as the United Nations moves forward in introducing and consolidating a culture of risk management and better accountability mechanisms, the Committee draws attention to the importance of the implementation of the provisions of paragraphs 10 and 11 of General Assembly resolution 62/223 A, by which the Assembly reiterated its requests to the Secretary-General to provide in his reports on the implementation of the recommendations of the Board of Auditors on the accounts of the United Nations as well as on the financial statements of its funds and programmes a full explanation for delays in the implementation of the recommendations, in particular those recommendations not yet fully implemented which are two or more years old, and to indicate in future reports an expected time frame for the implementation of the recommendations as well as the priorities for their implementation and the office holders to be held accountable. **The Committee also recommends that the basis for the prioritization be provided. In this regard, the Committee encourages the Secretary-General to designate focal points in each department/office to facilitate the implementation process and ensure accountability for the requisite action. Furthermore, the Committee is of the view that the Board should strengthen its validation process with a view to improving its ability to evaluate the results and impact of the Administration's efforts to implement the Board's recommendations.**

12. **In the view of the Advisory Committee, the format of the reports of the Secretary-General on the implementation of recommendations of the Board (A/63/327) could be better structured in order to facilitate cross-referencing with the reports of the Board. For instance, consistency in the use of headings by the Board would make the document more reader-friendly.**

13. The Advisory Committee recalls financial regulation 7.5, which states that "the Board of Auditors may make observations with respect to the efficiency of the financial procedures, the accounting system, the internal financial controls and, in general, the administration and management of the Organization". The Committee notes that, in addition to auditing the accounts and financial transactions, the Board carried out such reviews, which focused primarily on the efficiency of financial procedures, the internal financial controls and, in general, the administration and management of the organizations (see A/63/169, para. 10). **The Advisory Committee welcomes the Board's work in this area.**

14. **The Advisory Committee appreciates the coordination and collaboration of the Board of Auditors with other oversight bodies, including the Office of Internal Oversight Services and internal audit services of the United Nations funds and programmes, as well as the Joint Inspection Unit. The Committee considers that such coordination and collaboration adds value to the effectiveness of the overall oversight process and contributes to the optimal use of audit resources of the United Nations organizations by ensuring that the audits and reviews are of a complementary nature. In this regard, the governing boards of the funds and programmes may wish to consider the Advisory Committee's report in conjunction with the reports of the Board and in the light of the position of the General Assembly.**

III. United Nations

15. The main recommendations of the Board on the accounts of the United Nations for the financial period ended 31 December 2007 are set out in paragraph 10 of its report (A/63/5 (Vol. I), chap. II). The Board issued an unqualified opinion with regard to the financial statements of the United Nations. In the paragraphs below, the Advisory Committee highlights a number of key issues concerning the Board's report on the United Nations. Many of the observations and recommendations of the Committee in this section also apply to the other organizational entities covered by the Board's audits. Observations and recommendations relating solely to the other organizational entities are set out in section IV below.

Financial and related matters

16. The Board of Auditors observed that the financial statements showed a positive net income, assets in excess of liabilities and a positive cash flow balance. However, despite a significant increase in the Organization's total cash, the cash-to-liabilities ratio decreased significantly owing to the recording for the first time of end-of-service and post-retirement liabilities valued, as at 31 December 2007, at $2.33 billion. They are composed of $2.04 billion (87.5 per cent) for after-service health insurance liabilities, $0.15 billion (6.5 per cent) for liabilities relating to repatriation benefits and $0.14 billion (6 per cent) for compensation for accumulated leave. The Board notes that aggregate liabilities for end-of-service and post-retirement liabilities of all the entities audited were estimated to exceed $4.1 billion as at 31 December 2007 (see A/63/169, para. 29). The General Assembly, in its resolution 61/264, decided that, pending the validation of accrued after-service health insurance liabilities and auditing by the Board of Auditors, it would revert to the matter at its sixty-third session. Upon enquiry, the Committee was informed that the estimate of $4.1 billion was in fact an underestimate because the United Nations Joint Staff Pension Fund had not yet disclosed its liabilities and the other entities reported on had disclosed their liabilities to varying degrees.

17. **The Advisory Committee emphasizes that such liabilities should be disclosed as soon as possible by all concerned entities in preparation for the implementation of IPSAS.** In this connection, the Advisory Committee recalls the Board's view that the recording of end-of-service and post-retirement liabilities in the accounts calls for a comprehensive and effective funding strategy, as overall accounting for end-of-service and post-retirement liabilities has been achieved in most cases through an adjustment to reserves and fund balances, which does not

constitute a sustainable funding mechanism (see A/63/169, para. 32). In this connection, the Committee notes that the General Assembly will revert to this issue at its sixty-third session (see resolution 61/264, para. 16). The Committee comments further on IPSAS in paragraphs 20 to 23 below.

18. The Board of Auditors noted that as at 31 December 2007, unpaid assessed contributions for the United Nations regular budget amounted to $573.4 million, as against $361.1 million at the end of the previous biennium; this constitutes an increase of $212.3 million (58.8 per cent). The amount is cumulative, comprising unpaid assessed contributions from the biennium 2006-2007 as well as outstanding assessed contributions from previous bienniums.

19. The Board observed that the management of contributions in the Contributions Service of the Department of Management was a manual process relying on spreadsheets for the calculation and notification of assessed contributions as well as for the preparation of the periodic reports. The detailed data were kept in paper form and the cash receipt vouchers were issued manually. While no errors were identified, the Board detected delays in the issuance of cash receipt vouchers, the application of the payments to the corresponding assessments and the editing of the periodic reports on the status of contributions. The Board also noted that a new automated system was in the process of implementation and recommended that it be expedited. The Administration responded in its implementation report that the Board's recommendation was a "high priority" with a completion target date of the fourth quarter of 2008. Upon enquiry, the Committee was informed that an automated system was being tested and would be implemented in a phased manner by the end of 2008. **The Advisory Committee notes with regret the lack of automation in the management of contributions and concurs with the Board's recommendation.**

Implementation of the International Public Sector Accounting Standards

20. In accordance with General Assembly resolution 61/233 A and in response to the comments of the Advisory Committee (see A/61/350), the Board of Auditors carried out a gap analysis relating to the implementation of IPSAS as well as new or upgraded enterprise resource planning systems. The Board noted that United Nations entities were at different stages in the preparation for IPSAS and that a number of challenges remained. For example, the UNDP IPSAS implementation plan had not yet been approved; UN-Habitat had not yet initiated the preparation process; and UNOPS would require a tailor-made system to ensure compatibility with the Atlas system used by its business partners. With respect to the United Nations, the delay in funding the enterprise resource planning system would have a direct impact on the implementation of IPSAS and was likely to result in its postponement to 2011 at the earliest, instead of 2010 as originally planned (see A/63/169, para. 68 (a)).

21. The Advisory Committee was informed that there was a certain amount of flexibility in the interpretation of how IPSAS standards should be applied. **The Committee is of the opinion that the application of the standards will need to be monitored closely to ensure consistency within the United Nations system. In the view of the Committee, the United Nations System Chief Executives Board for Coordination should continue to play a key role and, in this regard, the Committee invites the Board to continue to follow this issue.**

22. The Board pointed out in its report the inconsistency in the financial statements as they do not cover the United Nations as a whole (see A/63/169, paras. 5 and 6). Inter-fund and inter-agency transactions, balances and relations are not adequately accounted for in all the financial statements of United Nations entities and there is consistently double-counting of transactions and assets. The Board also noted that while the United Nations system accounting standards do not require the preparation of consolidated financial statements, the International Public Sector Accounting Standards stipulate that a controlling entity shall present consolidated financial statements in which it consolidates its controlled entities. Upon enquiry, the Advisory Committee was informed that the introduction of IPSAS would not automatically result in the system-wide consolidation of financial statements because of the complexities of the United Nations system with its agencies, funds and programmes and various other entities. On the other hand, the Committee was informed that IPSAS could serve as a tool for the comparison and analysis of activities of various entities within the United Nations system. The Committee was informed that the Office of Legal Affairs had been consulted to provide an opinion on how the matter of consolidation should be handled, with a view to developing a legal framework to determine which entities would legally control other entities. **The Committee concurs with the Board's recommendation (see A/63/5 (Vol. I), chap. II, para. 27). It also recommends that the General Assembly keep the matter of consolidation or aggregation of the financial statements of the United Nations under review as the Organizations move towards migration to IPSAS.**

23. The Advisory Committee will comment further on IPSAS in the context of its consideration of the first progress report of the Secretary-General on the adoption of the International Public Sector Accounting Standards by the United Nations (A/62/806). In this regard, the Committee notes that the Joint Inspection Unit is currently engaged in a review of the preparedness of United Nations system organizations for IPSAS.

Enterprise resource planning system

24. The Board of Auditors considers that the enterprise resource planning system is one of the main drivers to make the overall management of the administration more modern and uniform. The Board also considers that the report of the Secretary-General on enterprise systems (A/62/510/Rev.1) constitutes a sound basis for a decision to be taken by the General Assembly at the earliest opportunity on the enterprise resource planning system, and recommends adoption of a decision on those proposals (A/63/5 (Vol. I), chap. II, para. 136). **The Advisory Committee concurs with the Board.** The Committee's own recommendations are contained in a separate report.

25. **Given the importance of enterprise resource planning and its significant cost implications, the Advisory Committee is of the view that implementation of the system requires careful monitoring. Accordingly, the General Assembly should be kept apprised of developments in that regard. The Committee looks forward to future reviews by the Board as regards to the preparatory process for enterprise resource planning, as well as for IPSAS.**

Technical cooperation activities

26. The Board examined results-based budgeting in the area of technical cooperation. It noted that because of the lack of clear objectives and valid indicators, an objective assessment of the activities carried out was difficult and was limited to examination of the accompanying narratives on progress made. The Board also observed that the monitoring modalities of the Development Account were an exception to that finding. The documents drawn up for the preparatory work for projects and then later for their development, as well as those setting out ex ante monitoring indicators, enable project managers to assess the results achieved at the end of the project. **The Advisory Committee welcomes the procedures followed by the Development Account in this respect and therefore concurs with the Board's recommendation that the Administration put in place, for all of its technical cooperation activities, a results-measurement mechanism comparable to that used for projects funded by the Development Account.**

Non-expendable property

27. The Board of Auditors observed once again that the inventory of goods at Headquarters in New York was incomplete (A/63/5 (Vol. I), para. 179). The Board also observed discrepancies between physical inventories and computer records at the United Nations Office at Vienna, the Economic Commission for Latin America and the Caribbean and the United Nations Office at Nairobi. **The Advisory Committee notes that improper accounting for non-expendable property has been a recurring theme in external and internal audit reports and believes that the matter needs to be addressed urgently, in particular in the context of the introduction of IPSAS. The Committee concurs with the Board's recommendation that the Administration prepare and implement formalized internal control procedures for non-expendable property and encourages the Board to assist in guiding the Organization in this area.**

Buildings and space management

28. The Advisory Committee notes with concern the Board's observations that at Headquarters there is an inadequate understanding of the actual use and configuration of work areas and a lack of an overall strategy for using space and that space is managed on the basis of urgent requests. **The Committee concurs with the Board's recommendations that the Administration formulate written procedures for space management and ensure their application in the following areas: planning for needs, allocating space and arbitrating requests, retrieving floor space and limiting urgent requests, with a view to optimizing space utilization.**

29. The Board has also emphasized the importance of a robust, long-term regular maintenance plan, in particular at the Organization's headquarters locations, in order to avoid cumulative problems that would lead to costly and large-scale repairs and renovations. The Board made a number of observations concerning construction and maintenance projects, which reaffirmed the Committee's long-standing view that the Secretariat in New York should play a coordinating role in planning, managing and monitoring construction and major maintenance projects. **The Advisory Committee shares the Board's views and approach.** The Committee's report on construction

and maintenance projects in Addis Ababa, Vienna and Nairobi (A/63/465) addresses those issues.

30. **With regard to the construction in Nairobi, the Advisory Committee agrees with the Board's recommendation that the Administration ensure that the United Nations Office at Nairobi undertakes a comprehensive analysis of the costs incurred by the presence of 29 United Nations agencies and their staff outside the Gigiri compound (and not 19, as listed in document A/62/794, annex I). Indeed, the Committee believes that such an analysis should already have been undertaken earlier and reflected in the report of the Secretary-General on construction. In this connection, the Committee was informed, upon enquiry, that there may be up to 29 agencies in total located off the premises, but a number of them are well-established in their existing office locations and therefore may not be interested in moving to the Gigiri compound. The Committee also concurs with the Board's recommendation that the Administration ensure that the United Nations Office at Nairobi maintain its capacity to offer common services to other United Nations entities and obtain fair compensation for them.**

Human resources management

31. The Advisory Committee notes the extensive review by the Board of Auditors on a number of subjects of concern in the area of human resources management. The Committee will comment further and draw upon the Board's observations and recommendations in the context of its consideration of human resources management issues during its current session.

Consultants and experts

32. Administrative instruction ST/AI/1999/7 refers to the need to rely on a central roster of candidates of consultants and contractors. The Board observed that the Department of Economic and Social Affairs did not have a common roster of consultants that its divisions could rely upon. The Board noted that those divisions have indicated that consultants are recruited on the basis of objective information aimed at taking into account the adequacy of their skills and professional experience. The Board also noted that there was a tendency to re-hire consultants instead of hiring new ones, and that between 2004 and 2007 most consultants originated from three European countries. The same administrative instruction also stated that external consultants should be hired only in cases where in-house expertise is not available. During its hearings with the Audit Operations Committee, the Advisory Committee was informed that to date, the Board had not examined whether the Department of Economic and Social Affairs and other departments had conducted a search for in-house expertise prior to hiring external consultants. **The Committee recalls General Assembly resolution 53/221 and other relevant resolutions, and in this regard encourages the Board to examine this matter further.**

Internal audit

33. The Advisory Committee notes the Board's observation that significant progress has been made in the operation and organization of the Internal Audit Division of the Office of Internal Oversight Services (OIOS), but that the Division's

risk-based methodological framework remains a work in progress. In addition, the Committee notes that OIOS is currently reorganizing its investigative function and that it has developed an information technology audit capacity. The Committee notes from the Board's report that the completion rate of audits programmed in the Division's workplan was fairly low in 2006 and 2007; fewer than half of the planned audits had actually been carried out. The Board found that this was due to the magnitude of the programme and to the management of the audit process. The Board indicated that the management and supervision of the work of the internal auditors could have been improved with an adequately applied time-sheet system. The Board also observed that the delays in performing the planned audit work were often caused by delays in the review of the supervisor's draft report, the response of the audited entity and the finalization of the report.

34. **While the Advisory Committee notes the progress highlighted by the Board in the work of the Internal Audit Division, it is concerned that the Division's risk-based methodological framework is not yet complete. Furthermore, the Committee is concerned at the low rate of completion of planned audit assignments and stresses that this needs to be reversed. The Committee concurs with the Board's recommendations and encourages the Board to continue to follow up on these matters. The Committee recommends that the General Assembly request OIOS to complete the risk-based framework of the Internal Audit Division and keep the Assembly apprised concerning measures taken to improve overall audit performance.**

Fraud and presumptive fraud

35. The Administration provided the Board with a report of cases of fraud and presumptive fraud for the biennium 2006-2007. A total of 14 cases were reported, as compared to 7 during the biennium 2004-2005. The cases of fraud and presumptive fraud were valued at $644,505 for 2006-2007. The Board noted that the list of fraud cases submitted to it by the Administration failed to include the investigations of fraud and misuse of United Nations procurement and purchasing undertaken by OIOS and its Investigations Division. **The Advisory Committee concurs with the Board that the Administration should include in the cases of fraud and presumptive fraud transmitted to the Board those cases detected and investigated by the Investigations Division of OIOS and, if applicable, the Procurement Task Force.**

IV. Funds and programmes

Financial and related matters

36. With regard to treasury management, the Board noted problems in a number of funds and programmes with financial records, including bank reconciliations. The Board noted that bank reconciliations at UNDP were not always performed on a monthly basis, were not signed and contained long-outstanding items, partly because the procedure for preparing bank reconciliations within the Atlas system was new to UNDP personnel. During the hearings, the Advisory Committee was informed that as a result, bank account overdrafts occurred despite there being sufficient funds in bank accounts. Similar difficulties were observed at UNICEF. Also at UNICEF, unliquidated obligations pertaining to the biennium 2004-2005

were cancelled but were then recorded incorrectly as miscellaneous income in 2006-2007, resulting in the overstatement of income for that period. Upon enquiry, the Committee was informed that this manner of recording financial transactions was possible within the framework of the United Nations system accounting standards but would not be under IPSAS.

37. In its report on UNOPS for the biennium 2004-2005, the Board issued a qualified audit opinion with seven emphases of matter. For 2006-2007, the Board issued a modified audit opinion with three emphases of matter. The three emphases of matter pertained to inter-fund balances with UNDP, shortcomings in assets management and inadequate Atlas project controls. With regard to unresolved inter-fund balances, the Board was unable to confirm and verify inter-fund balances with UNDP and UNFPA, as well as 21 balances with other United Nations entities. **The Advisory Committee concurs with the Board that any outstanding inter-fund balances must be resolved expeditiously. The Committee notes that while the Board's comments indicate an overall improvement in UNOPS operations, further measures are required. The Committee notes this encouraging trend but stresses the importance of continued review by the Board, in particular in respect of the recent partial merger of UNOPS with the Inter-Agency Procurement Services Office.**

38. The Board of Auditors observed that some funds and programmes had accumulated insufficient reserves. For example, the reserves and fund balance at UNITAR decreased from $12.8 million during the biennium 2004-2005 to $9.5 million during 2006-2007. UNITAR explained to the Board that the nature of its funding required it to spend what it received from donors and not to build reserves. Upon enquiry, the Advisory Committee was informed that this was also the case with other funds and programmes: funds were earmarked for specific projects by donors and therefore could not be utilized to build a cash reserve. **The Committee addressed the matter in its previous report (A/61/350, para. 53), noting that it was essential that all organizations develop comprehensive funding strategies and principles to guide their fund-raising policies in order to support the objectives set by their governing bodies and that it shared the Board's views that the organizations of the United Nations system should develop effective funding strategies and diversify funding sources, as appropriate.**

39. With regard to the results-based budgeting and results-based management modalities, the Board observed that, in general, indicators of achievement and related narratives required further refinement. The Board noted that effective indicators of achievement needed to be specific, measurable, attainable, relevant and time-bound and pointed to deficiencies in this regard at a number of funds and programmes, including UNDP and UNITAR. **In the case of UNDP, for example, the Board noted examples where indictors of achievement were not in accordance with UNDP guidelines. In the view of the Advisory Committee, the development of adequate performance indicators is essential. The Committee will continue to follow up on the matter in future hearings with funds and programmes and recommends that the Board continue to place emphasis on the review of the results-base budgeting and results-based management modalities in its future audits.**

Project implementation

40. The Board notes that a risk-based assessment model for nationally executed projects was introduced at UNDP in 2007 that identifies continuing weaknesses in the nationally executed expenditure modality processes and results, including control weaknesses in the financial management of projects. The Board identified deficiencies in the audit process for nationally executed projects at UNFPA, as well as shortcomings in the process of selecting and appointing auditors and discrepancies in the logs and databases of audit results for nationally executed projects. The Board also observed control weaknesses with respect to nationally executed projects at UNICEF, UNFPA, UNWRA and UNHCR. **The Advisory Committee welcomes the introduction of the nationally executed expenditure risk-based assessment model at UNDP but concurs with the Board that adequate controls, including a functioning oversight process, must be in place in order to ensure the model's success. The Committee trusts that lessons learned from the introduction of the risk-based assessment model at UNDP will be shared with other funds and programmes.**

41. The Board observed that the use of direct execution for the implementation of UNDP projects had increased from 2 per cent in 2001 to 33 per cent in 2007. The Advisory Committee was informed, during its hearings with the Audit Operations Committee, that the increase was due to changes in the mix of contributions from donors. The Board identified deficiencies in the audit process for nationally executed projects and expressed concern that some financial reports for those projects reflected control weaknesses in financial management. Upon enquiry, the Committee was informed that the Board was of the view that the frequency and extent of the audit process for nationally executed projects should be reviewed by UNDP. **The Committee believes that UNDP should continue to improve its monitoring of the audit process for nationally executed projects and commence regular reviews, especially in view of the large amounts of financial resources linked to nationally executed expenditure. The Committee also encourages the Board to continue its review of this matter and to provide an update in its next audit.**

Revenue-producing activities

42. At UNICEF, the Board observed that some National Committees were retaining up to 100 per cent of the gross proceeds from the sale of greeting card products even though rule 9.04 of the special supplement to the UNICEF Financial Regulations and Rules states that they may be authorized to retain only up to 25 per cent of such sales. **The Advisory Committee concurs with the Board that UNICEF should ensure that the 25 per cent retention limit is applied and that, if necessary, UNICEF should evaluate and formalize any exceptions to the rule.**

Inter-agency coordination and common services

43. The Advisory Committee notes that a range of common services has been established among United Nations system organizations and emphasizes that such arrangements may require periodic review. **The Committee also emphasizes that common services arrangements should avoid duplication of functions, as well as additional costs to the entities concerned.**

Disaster recovery and business continuity

44. The Board reiterated its observation that UNWRA had not developed a disaster recovery or business continuity plan. The Board noted that UNWRA had hired a consultant to develop a draft disaster recovery plan and signed a memorandum of understanding with the Department of Field Support to use the data centre in Brindisi, Italy, for that purpose. **The Advisory Committee concurs with the Board's recommendation that UNWRA develop a comprehensive plan and welcomes the Agency's efforts in that regard. The Committee will follow up on this matter in the context of future hearings with UNWRA and trusts that the Board will review the progress made in its next audit.**

Non-expendable property

45. With regard to overall assets management, the Board continued to observe discrepancies between physical inventories and computer records. For example, at UNHCR, the Board noted that while purchases of non-expendable property were recorded in the accounts at the time of the order, they were entered into the property database only at the time of receipt. The Board noted that this practice had led to a gap between purchased assets and inventoried assets. UNHCR responded that it had followed up on assets that had been procured but not recorded in the system and that the incorrect recording had been the result of a technical system problem. The Advisory Committee comments further on this matter in the context of its recent report to the UNHCR Executive Committee (A/AC.96/1055/Add.1).

46. **The Advisory Committee concurs with the Board's observations and recommendations. It regrets the absence, in general, of any significant changes since the Board's previous review. The Committee is particularly concerned that, in anticipation of IPSAS, the management of non-expendable property needs to be formalized. In this regard, the Committee recalls paragraph 41 of its previous report (A/61/350), in which it cautioned that with the adoption of IPSAS and full-accrual accounting, non-expendable property and inventory would appear as assets on financial statements and have to be capitalized and accounted for. The Committee commented further that the integration of non-expendable property into the accounting system would require the systematic, comprehensive and accurate recording of such equipment into information systems, both at Headquarters and at field offices. The Committee reiterates its recommendation that each organization establish workable procedures with strong internal controls in this regard.**

Internal audit function

47. The Board found that the internal audit functions at funds and programmes were performing satisfactorily but noted areas in need of improvement. UNOPS established an in-house audit office in September 2007, ending its internal audit agreement with UNDP. The Board recommends that UNOPS take measures to implement its audit workplan and increase coverage of regional offices and headquarters. At UNDP, the Board observed that deadlines of audit workplans were met at a rate of only 70 per cent and that internal audit resources needed to be aligned in order for the audit function to be able to fulfil its quality assurance function. With regard to the latter, UNDP responded that the allocation of resources was risk-driven. The Board also noted that UNDP had commissioned an independent

quality assessment of its internal audit activity, which concluded that UNDP partially conformed to the International Standards for the Professional Practice of Internal Auditing and generally conformed to the Code of Ethics of the Institute of Internal Auditors. However, a number of matters needed to be resolved. In particular, questions about the audit function's independence were raised since it receives its financing through the UNDP Bureau of Management, which is also an auditee. **The Advisory Committee notes that UNDP agreed with the Board's recommendation that it address the matters identified in the quality assessment report. In this connection, the Committee points out that an effective internal audit entity needs to be able to conduct its work without restrictions and recommends that UNDP ensure the full independence of its audit function without further delay.**

Annex

Background information regarding unqualified and qualified opinions, and modified reports[a]

The International Standard on Auditing (ISA) 700, paragraph 39, states that “An unqualified opinion should be expressed when the auditor concludes that the financial statements give a true and fair view or are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.”

ISA 701 describes two situations when the auditor’s report is modified:

- The first relates to matters that do not affect the auditor’s opinion in which case an emphasis of matter is given. Paragraph 5 of ISA 701 states that “In certain circumstances, an auditor’s report may be modified by adding an emphasis of matter paragraph to highlight a matter affecting the financial statements which is included in a note to the financial statements that more extensively discusses the matter. The addition of such an emphasis of matter paragraph does not affect the auditor’s opinion .... The emphasis of matter paragraph would ordinarily refer to the fact that the auditor’s opinion is not qualified in this respect.”

- The second situation relates to matters that do affect the auditor’s opinion. Paragraph 11 of ISA 701 states that “An auditor may not be able to express an unqualified opinion when either of the following circumstances exist and, in the auditor’s judgment, the effect of the matter is or may be material to the financial statements:

  (a) There is a limitation on the scope on the auditor’s work; or

  (b) There is disagreement with management regarding the acceptability of the accounting policies selected, the method of their application or the adequacy of financial statements disclosures.

  The circumstances described in (a) could lead to a qualified opinion or a disclaimer of opinion. The circumstances described in (b) could lead to a qualified opinion or an adverse opinion.”

Paragraph 12 of ISA 701 states that “A *qualified opinion* should be expressed when the auditor concludes that an unqualified opinion cannot be expressed but that the effect of any disagreement with management, or limitation on scope is not so material and pervasive as to require an adverse opinion or a disclaimer of opinion.”

[a] Provided by the Board of Auditors.